

# *Fix, Rebuild and Grow*

Wm Morrison Supermarkets PLC  
Annual Report and Financial Statements 2016/17



# Fix, Rebuild and Grow

*We have a plan to Fix, Rebuild and Grow our business for all of our stakeholders. We have six priorities which we will deliver through our five ways of working to fulfil our ambitions for our four sets of stakeholders.*

## 6 priorities

We have six priorities to guide us and shape our ambition to Fix, Rebuild and Grow Morrisons.

- To be more competitive
- To serve customers better
- Find local solutions
- Develop popular and useful services
- To simplify and speed up the organisation
- To make the core supermarkets strong again

[Read more about our progress on page 6](#)

## 5 ways of working

Our colleagues know our customers better than anyone and are listening hard. We have five ways of working that underpin our approach and enable colleagues to make the best decisions for customers and each other.

- Customers first
- Teamwork
- Freedom in the framework
- Listening and responding
- Selling, controlling costs, growing profits, removing waste

[Read more about our progress on page 12](#)

## 4 sets of ambitions

Creating value for all key stakeholders in a fair, responsible, capital light and sustainable way.

### Customers



[Read more on page 10](#)

### Colleagues



[Read more on page 12](#)

### Suppliers



[Read more on page 13](#)

### Shareholders



[Read more on page 14](#)

[Read more on pages 10 to 14](#)

**Throughout the Directors' report and Strategic report:**

(1) Unless otherwise stated, 2016/17 refers to the 52 week period ended 29 January 2017 and 2015/16 refers to the 52 week period ended 31 January 2016. 2016 and 2017 refer to calendar years.  
 (2) Underlying profit is defined as reported profit before impairment, provision for onerous contracts and other items that do not relate to the Group's principal activities on an ongoing basis, profit/loss arising on disposal and exit of properties and sale of businesses and investments, and the impact of pension volatility, at a normalised tax rate, as reconciled in note 1.4 of the Group financial statements. Underlying operating profit is reported operating profit before impairment, provision for onerous contracts, profit/loss arising on disposal and exit of properties and sale of businesses and investments, and other items that do not relate to the Group's principal activities.  
 (3) Like-for-like (LFL) sales reflects the percentage change in year-on-year store sales (excluding VAT and fuel), stripping out the impact of new store openings and closures in the current or previous financial year.

## Improving the shopping trip for customers



The shopping trip is improving with more customers buying more from Morrisons more often.

Like-for-like transactions up 4%

[Read about our ambitions for our customers on page 10](#)

## A turnaround led by colleagues



The turnaround is being led by our colleagues and our ambition is for our motivated and highly valued team of colleagues to increasingly share in the success of Morrisons.

Colleague bonus equivalent to around 9% of underlying profit

[Read about our colleague ambitions on page 12](#)

## Building long term relationships with suppliers



We are building long term partnerships with suppliers, growing and serving customers better together.

Like-for-like volumes up 2%

[Read about our progress for our suppliers on page 13](#)

## Creating value for shareholders



We are creating value for shareholders and aim to demonstrate sustained growth in total shareholder returns.

Total dividend 5.43p, up 8.6%  
Underlying profit before tax £337m, up 11.6%

[Read about our progress for shareholders on page 14](#)

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### Online annual report

Read how we are creating value for all our stakeholders:

[www.morrisons-corporate.com/annual-report-2017](http://www.morrisons-corporate.com/annual-report-2017)



## Chairman's statement

# Building a business for all our stakeholders

*Our mission is a modest one, but we can contribute widely to society*

Andrew Higginson  
Chairman



We strive to be a place where our colleagues can get on

Dividend

5.43p

in line with policy

I am writing this statement with the business in good heart after a year of profit and dividend growth, further debt reduction, and five quarters of positive like-for-like sales.

Uncertain times are ahead. Although the UK consumer remains resilient so far, the consequences of Brexit and significant currency movements are not yet clear. Morrisons has planned and prepared for Brexit but, in truth, no one knows exactly what is to come.

By listening hard to customers – something David Potts and his team do from shop floor to Board room – Morrisons will not allow itself to become victims of that uncertainty. The Board and the senior team will work tirelessly whatever the trading conditions to build a successful business for the millions of customers that shop with us every week.

So, we face the uncertainties with a positive mind-set, and there will be no excuses from us.

Take scale as an example. Morrisons is often accused of being structurally disadvantaged and unable to compete with bigger rivals. That is nonsense. Morrisons has always been relatively small, but for decades competed brilliantly and drove terrific returns for shareholders. Scale rarely defines retail winners and losers.

Most often it is outstanding execution that results in a great shopping trip. Customers have a vast choice of retailers and it is they who decide the winners and losers, quite literally, by 'voting with their feet'.

Food retail is an ordinary business, touching most consumers' lives almost every day. It is fiercely competitive. To execute 'the ordinary' consistently well is far from easy and relies on outstanding leadership.

It is no coincidence that Morrisons much improved performance coincides with the appointment of David and his new senior team. Morrisons skilled food makers and shopkeepers are loyal, passionate and dedicated, and virtually all are unchanged since David started. Whilst all have contributed to the improved performance, it is the leadership that has changed.

This is pertinent to the discussions and AGM resolutions relating to our proposals for the next three year Executive remuneration policy. In construct it is similar to our existing policy that expires this year, however we have tweaked the performance measures to reflect the challenges ahead enabling the Executive team to earn up to the maximum bonus potential if outstanding long term performance is delivered.

Our mission is a modest one – to provide our customers with good quality food, great service and prices – but our contribution to society can be very wide. We strive to be a place where our colleagues can get on – a meritocracy where good, hard-working people can succeed whatever their background, and everyone shares in success. That is exactly what happened to David and many of the senior team at Morrisons who have worked their way up from the shop floor.

We provide training and apprenticeships for thousands of food makers and shopkeepers. We pay the best we can, well above the National Living Wage, and offer bonuses to colleagues in all our stores, factories and depots. Over a thousand colleagues participate in our Long Term Incentive Plan, including all our store managers.

With over 110,000 colleagues and over 11 million customers per week, Morrisons sits at the heart of, and must reflect, the society we serve in Britain. With plenty of choice available to them, our customers are our toughest and best regulator. It is right and proper that our business is scrutinised, and that our customers can see that we behave well. Be it in our values, our actions, the impact we have on the environment, our suppliers, or in the quality and safety of the food we sell. We take all our responsibilities seriously, knowing that if we fall short, our customers may choose to shop elsewhere.

With all these demands on the business, we must also remember that our reason to exist is to make a return for our shareholders.

As we build a sustainable recovery, we intend to also build a track record of returns for our shareholders. 2016/17 was the first for our new dividend policy. That policy is for the dividend to be covered around two times by underlying earnings per share, and I am pleased that we recently announced a 2016/17 dividend of 5.43p per share (up 8.6% on last year).

As cash flow improves, our balance sheet is getting stronger and we are on track for our target of net debt to fall to less than £1bn by the end of 2017/18.

We continue to prioritise balance sheet strength over efficiency. As we keep improving profitability and further de-leverage the business, we will continue to be guided by our capital allocation framework.



#### Sir Ken Morrison CBE

Everyone at Morrisons was very sad to hear recently of the passing of Life President, and former Chairman, Sir Ken Morrison CBE.

Sir Ken was an inspirational retailer and the driving force behind Morrisons for more than half a century, transforming the company from a small family business into one of the UK's top 100 companies. He developed the culture, values and clear direction for the business which remain the bedrock of the firm today. His legacy includes many enduring innovations, such as Market Street and Morrisons' unique vertical integration model.

Sir Ken will be greatly missed by many thousands of his current and former colleagues. On a personal level, Ken was an enormous help to me as we made some significant changes to set the business on a new course; his knowledge of retail and his strategic insights remained as relevant and intuitive as they were when he first built the business.

To honour his memory in the most appropriate way we can, we will strive to develop the company that he built and loved.

**Andrew Higginson**  
Chairman

## Governance highlights

### Board composition and membership

- The Board comprises five independent Non-Executive Directors and two Executive Directors.
- All Directors stand for re-election annually at the AGM.
- Rooney Anand is the Board's Senior Independent Director and a Non-Executive.
- The Board is satisfied that Belinda Richards has recent and relevant experience appropriate to her position as Audit Committee Chair.
- There is clear division of responsibilities between the roles of Chairman and the Chief Executive.

### Board effectiveness

- The Directors have all attended an acceptable number of Board and Committee meetings.
- The Board is satisfied that Non-Executive Directors commit sufficient time to the Group and contribute to its governance and operations.

### External auditor

- The Audit Committee is satisfied that the Group's statutory auditor PwC, who were appointed in 2014/15, are performing effectively.
- The Board has a policy on the engagement of the external auditor to supply non-audit services.

### Accountability

- The Board is satisfied with the effectiveness of internal control and that risk is being managed effectively across the Group.
- Consideration has been given to financial reporting matters with sufficient challenge provided to management relating to judgemental areas.
- The Group's internal audit function perform periodic reviews of the key areas of the business, including the recognition of commercial income.



See **Corporate governance report** on pages 23 to 32

Chief Executive's statement

# Becoming more popular and connecting with customers

*We are listening to customers and they are powering the plan to Fix, Rebuild and Grow Morrisons*

David Potts  
Chief Executive



During the year, we improved the offer, became more competitive and served customers better

2016/17 was Morrisons first full year of Fix. The first year that the new senior team and our hardworking food maker and shopkeeper colleagues have been able, together, to set about the task of delivering a sustainable turnaround.

That turnaround is being powered by listening hard to customers and responding quickly. Customers continue to provide us with the insight we need to make improvements to the shopping trip. During the year, we improved the offer, became more competitive and served customers better, thereby becoming more popular and re-connecting more with our core customers.

Customers tell us that the Morrisons offer is good quality and great value, and during the past year we did much more to improve this further. One highlight was our new premium own label 'Best' range. We launched nearly 500 products in the autumn and a further 100 especially for Christmas shoppers. Customer feedback on the quality and breadth of 'Best' range has been excellent, and we see further significant potential for more 'Best' products.

We improved the offer in other areas such as Food to Go, Free From, Nutmeg clothing, meal solutions and craft beer. Our improvements are starting to be recognised and rewarded, and we were delighted to win a series of prestigious awards during the year. We won Meat and Fish Retailer of the Year, In-store Bakery Retailer

of the Year, National Café Chain of the Year, Cheddar Cheese Retailer of the Year, and International Wine Challenge Supermarket of the Year for the second year running.

We continue to become more competitive for customers. There were several waves of 'Price Crunch' during the year, with low prices held as long as possible for customers. 'Morrisons Makes It' is a fresh range made by our specialist food makers in our stores and in Manufacturing, combining our unique craft skills with great value. Through these, and other ways of simplifying our offer, we are developing a more competitive Morrisons price list that provides great value for customers.

Customer satisfaction continues to improve. During the year, we introduced a new ordering system into all stores, which is improving on-shelf availability for customers. Other ways of serving customers better included the introduction of more self-service belted checkouts, and further forecourt convenience trials which utilise our strengths as a wholesaler while making the Morrisons brand accessible for more customers. Supplying to Amazon has also started well.

The response from our customers has been very encouraging. On a like-for-like basis, we served 4.0% more transactions during the year, and 4.6% more during the fourth quarter which includes Christmas and new year. Like-for-like sales were up 1.7%, and were positive in every quarter. With deflation throughout the year, sales volumes were up. This means more customers are buying more at Morrisons.

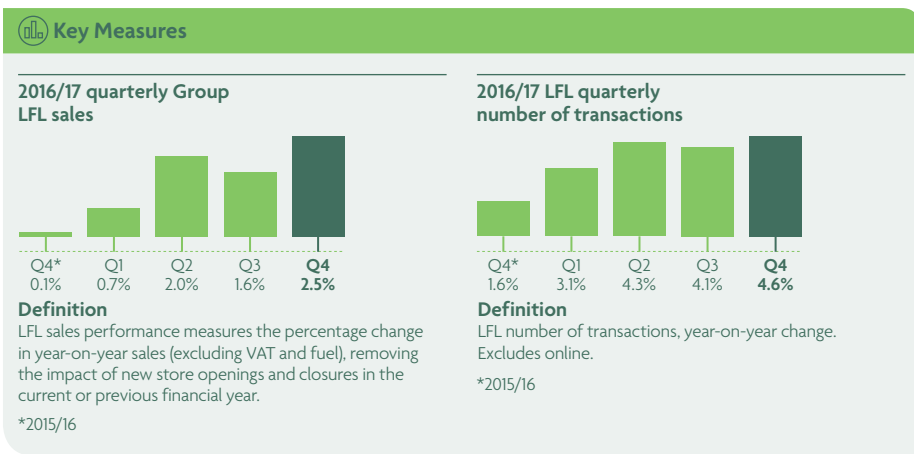
Our plan is for this to continue, with Morrisons becoming a broader, stronger business. We have many opportunities to invest in growth, and cut waste and costs.

Key Measures

Morrisons brand warmth\*



\* Source: YouGov, 12 week moving average w/e 04/12/16



We are confident we can lay the foundations to move to the Rebuild and Grow phases of this turnaround. We have made a good start, achieving the first £18m of the £50m to £100m incremental profit opportunity that we identified across four areas – wholesale, online, popular and useful services, and reducing interest. We are following the customer and investing in changes in their behaviour, to grow profitability in a capital light way. As well as our partnership with Amazon, we are working on various new capital light projects such as Morrisons Daily convenience stores on Rontec forecourts and the revival of the Safeway brand for wholesale customers. We also announced a partnership with Timpson and a new plan for Morrisons.com to grow profitably across Britain with Ocado, as well as various initiatives to reduce our gross debt and interest charge.

Our growth will be assisted by recycling extensive future cost savings back into the customer offer. We have exceeded our original target of £1bn of savings over three years, but there is more to come. The new ordering system is a good example of us saving money while becoming better shopkeepers. It is simpler and saves time for colleagues, and is reducing stock levels. In addition, we have identified further productivity opportunities in areas such as in-store administration, distribution between Manufacturing and Retail, and procurement.

As Andrew noted and Trevor details later, cash flow and working capital continue to improve, we are making good progress on reducing debt, and our balance sheet is strong. This provides the platform for delivering growth and for progressing Morrisons from Fix to Rebuild and Grow.

Although 2016/17 was a good year, it was just the start of the Morrisons turnaround. We have lots more to do and our colleagues have lots more ideas. As I set out in my Chief Executive's statement last year, this turnaround will be colleague-led, and so it is proving. Our performance so far is entirely due to the continuing hard work, passion and dedication of the Morrisons team of skilled food makers and shopkeepers, and I would like to thank every colleague for their invaluable contribution.

**David Potts**  
Chief Executive



**Listening to our customers...**

**...and responding**

We significantly expanded our Free From range.



**Listening to our colleagues...**

**...and responding**

'Morrisons Makes It' products showcase the best of our colleagues' food maker skills.

Our six priorities

# The progress we've made on our six priorities

*We've made good progress but we have more to do as we continue to turnaround the business*

**1**

## To be more competitive

Customers want great value, good quality fresh food

**We are listening and responding**

- Regular waves of 'Price Crunch', driving down prices on thousands of everyday items. Keeping those prices as low as possible for as long as possible
- A Morrisons price list, with the right prices for the items our customers want to buy
- 'Morrisons Makes It' is a range of fresh items made by our specialist food makers, combining our unique craft skills with great value
- A focus on Fresh, Market Street and sharing our expertise with customers
- Partnering with suppliers to buy and sell for less, and saving our customers every penny we can
- Ranges such as 'Best,' Nutmeg, Free From and Food to Go. We are selling more things people want to buy

**2**

## To serve customers better

Customer service makes Morrisons different

**We are listening and responding**

- Queue lengths are shorter and we are opening more tills for customers
- Our new ordering system is improving availability, saving colleagues time and reducing stock levels
- Serving more customers, with LFL transactions up 4.0% last year
- Customers are noticing the improvements and responding, with customer satisfaction scores up again this year
- Improving the quality of Morrisons own brand, for everyday, important seasons and events, and special gatherings for family and friends
- Broadening Morrisons and making the brand more accessible by following the customer into online, digital, convenience and new services
- Installing Wi-Fi in all stores

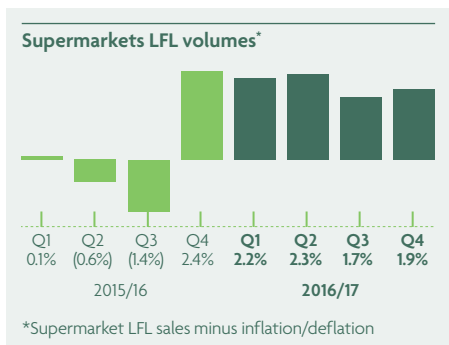
**3**

## Find local solutions

Each supermarket is unique to its local community

**We are listening and responding**

- Locally sourced products in local stores, such as strawberries, apples, kale, sprouts and poinsettia
- Local events and communication
- Regional initiatives such as Hogmanay, Yorkshire Day and Scottish favourites
- The Fresh Look programme helps tailor the look and feel of stores to the local community. Listening groups at each store drive all aspects of the improvement
- Specialist buyers for regions such as Scotland, Wales and London
- Our data can target individual customers to better personalise our offer
- Tailored plans to compete against new competitor stores





4

## Develop popular and useful services

Another reason to visit Morrisons

### We are listening and responding

- Always competitive on fuel, with busy forecourts and extended opening hours
- Welcoming and hospitable cafés in 401 stores, with over 130 modernised last year. Improved menus, shorter queues and friendly service
- ‘Morrisons Daily’ convenience trials
- Partnerships such as ‘Timpson at Morrisons’ bringing new in-store services to our customers
- Developing opportunities for complementary retail and service initiatives in our car parks
- Popular pick-up services such as Amazon, Doodle and InPost now available in hundreds of stores
- In-store pharmacies provide an important service for customers

Petrol filling stations

334

Cafés

401

Pharmacies

118

5

## To simplify and speed up the organisation

Speed and teamwork makes us responsive for customers

### We are listening and responding

- A leaner, diverse team with many new internal and external senior colleagues working together well with our skilled food makers and shopkeepers
- Building stronger, lasting, mutually beneficial relationships with our suppliers. Working together to buy and sell simply
- Continuing to eliminate wasted effort and cost, making the business more efficient and responsive to customers. Over £1bn saved over the three-year programme, with further opportunity including automated ordering, distribution and in-store administration
- Further initiatives in areas such as digital communication, improved management information and a culture of continuous improvement
- Technology investment has helped to automate processes and speed up and simplify the business



6

## To make core supermarkets strong again

Investing in the core

### We are listening and responding

- Fresh Look programme is improving up to 100 stores a year. Some components, such as Food to Go and Nutmeg, are being rolled out across all stores
- Investing in fresh food and Market Street to improve range, quality, colleague knowledge and services such as tastings and customer advice
- More training, talent programmes, succession planning and rewards for colleagues to bring our best people through
- Developing leaner processes in-store
- Aligning in-store bonuses with Mystery Shopper and customer service scores
- Improving use of loyalty card and digital data to inform the business of how to identify emerging trends and better serve customers
- Creating value for all our different stakeholders – customers, colleagues, suppliers and shareholders



Our business model

# Food makers and shopkeepers

*We have been listening to what our customers want from Morrisons... good quality fresh food, great value for money, great and consistent customer service and where possible authentically British*

## Resources

### Customers

11 million customer transactions every week

### Colleagues

Over 110,000 colleagues and a high quality management team

### Sites

491 conveniently located supermarkets

17 manufacturing sites

8 distribution centres

### Brand

A well known brand which is becoming more popular and accessible to more customers

### Financial strength

Strong balance sheet and cash flow with largely freehold estate and low debt is a firm foundation for the business

## Our business:

### Food maker

**We have food makers in our 491 stores and our 17 manufacturing sites**

- We make fresh food visibly and daily on Market Street for our customers
- We also make fresh food in our manufacturing sites across the UK
- Over half of the fresh food we sell, we make ourselves
- We work with suppliers to effectively source the products we don't make ourselves

### Distributor

**We have a national distribution network that moves the food we make and buy**

- Our stores are serviced by seven regional and one national distribution centres
- This gives us the opportunity to support our growth through other channels
- We are working on ways to further improve the efficiency of our network – particularly 'hand offs' between manufacturing, distribution and retail

## How we are different

Our food making skills are a recognisable point of difference providing products that are unique to us

Controlling the whole supply chain means we know where our food comes from and can provide our customers with what they want, when they want it

## Delivered through our six priorities

- 1 To be more competitive
- 2 To serve customers better
- 3 Find local solutions

## Five ways of working underpin what we do

- 1 Customers first
- 2 Teamwork
- 3 Freedom in the framework

### Retailer

#### We sell what we make and buy in-store and online

- Listening informs improvements we make
- A competitive Morrisons price list, providing good quality fresh food at the right price
- Shopkeepers caring deeply about service

- Our More Card helps us to understand and serve our customers better
- Over 50% of the UK population has access to our online offer
- Customers know what is new and different at Morrisons

### Wholesaler

#### We are a wholesaler, providing our products to retail partners and third parties

- We can leverage the strength of our brand and manufacturing capability to deliver quality products

- We aim to make our brand more accessible and increase volume through our existing assets

Understanding our customers powers the decisions we make. Customers trust our brand and see us as competitive and locally relevant

Through stores, manufacturing, online and our wholesale partners, we can leverage our brand to achieve **meaningful and sustainable growth without the need for significant investment**



See **Our six priorities** on page 6

4 **Develop popular and useful services**

5 **To simplify and speed up the organisation**

6 **To make the core supermarkets strong again**

4 **Listening and responding**

5 **Selling, controlling costs, growing profits, removing waste**

## Outcomes for our stakeholders

### 1 Customers

- More customers, buying more from us, more often
- Customers can get what they want when they want it
- Transactions up 4%

Read more on page 10

### 2 Colleagues

- Engaged and motivated colleagues
- Colleagues sharing in the success of the business
- Colleague bonus scheme which equates to around 9% of UPBT

Read more on page 12

### 3 Suppliers

- Establishing lasting relationships
- Working together with simplified terms
- Volume growth

Read more on page 13

### 4 Shareholders

- A strong balance sheet
- A cash generative business with reducing debt
- Sales, profit and dividend up

Read more on page 14

## Environmental and social value

- Making a positive contribution to society
- Reducing food waste
- Taking care of the environment



Read our Corporate responsibility section on page 20

## Performance review

# Our customers

*What customers tell us is at the heart of the decisions we make to improve their shopping trip*

## HIGHLIGHTS

Number of customer transactions  
each week

over 11m

Average number of customers  
per month who participated  
in listening sessions

over 30,000

## Key Measures

Satisfied with time taken to queue\*



\*Source: Morrisons is Listening survey

### Listening to customers

With over 11 million customer transactions every week, listening hard and responding quickly is crucial as we continue to turnaround the business. We have established a number of ways for the whole Morrisons team to get closer to customers and improve the shopping trip.

On average we connect with over 30,000 customers every month through our online panel of customers and regular in-store listening sessions. They have told us about changes to their shopping behaviour including shopping more frequently and looking for new products such as Free From, vegetarian and low sugar products.

We are continuing to increase the breadth and depth of our customer listening. This allows us to get first hand feedback from customers on their shopping journey.

The Morrisons 'MyView' customer panel is an important way of getting closer to our customers. 'MyView' allows customers to contribute regularly to online discussions and surveys, giving us immediate feedback on which we can act quickly. The panel, for example, has helped us to improve our cafés where customer feedback directly led to a new café menu with an expanded vegetarian range and more meals with fewer than 600 calories.

Our social media channels give us access to direct feedback from customers as do customer emails and calls through to our Contact Centre. In this way, thousands of customer comments can be used to improve our products and our service.

At Morrisons we recognise that our customers are all different. We have identified five family segments and understood what is important to each of them regarding their shopping. To help us understand the needs of each of the family types, we have begun a six month programme where we are in regular contact with a number of Morrisons families. We talk to them regularly both online and through social media to understand how they feel about Morrisons, and what we can do to improve their shopping

experience with us. This is an important way of staying in regular touch with the different types of people who shop with us, and adapting our business to suit their needs.

We will listen even harder to our customers throughout 2017, as we still have more to do.

### Serving customers better

Service and expertise are key parts of our ambition for customers. More customers tell us they are either satisfied or highly satisfied with their store experience and say we have started to improve on a number of the measures that are important to them.

At Morrisons we are food makers and shopkeepers offering good quality food at great value. Our customers tell us that they rate us highly in terms of quality fresh food and recognise our food making credentials through our skilled and specialist colleagues and our service counters. They also associate us with British products, working closely with farmers and making more of our own food than other retailers.

Customers tell us that our in-store food makers on Market Street are a unique point of difference. Having our experts on hand to help and advise is part of the Morrisons experience. During the year, we made changes in some stores, by opening up Market Street departments such as butchery to make the fresh food we produce in-store each day more visible to customers.

Throughout the year, we showcased a number of 'Morrisons Makes It' products – unique products made by our specialist food makers, each at great value for money. We continue to invest in price through our 'Price Crunch' programme becoming more competitive for customers, and developing the Morrisons price list for customers.

We committed to improving the customer experience at the checkout, particularly the length of time our customers take to queue. We have made good progress, and customers tell us that this has made a big difference to their shopping trip. Significantly more

customers are now highly satisfied with the time taken to queue than they were in 2015.

Customers also tell us that our colleagues are friendly and we have made good progress improving the availability of products on our shelves.

#### More Card

The More Card programme is now well established and growing in popularity. The number of customers actively using a More Card continues to grow, meaning more customers are regularly collecting More Card points which can be converted into savings on their shopping. The More Card programme is one of the ways the business is able to listen, helping us to serve customers better and be more competitive by providing a range of benefits and personalised rewards.

Since November 2015, customers have been able to earn More Card points every time they shop with us. Customers can earn More Card points in-store and online, when they buy fuel on our forecourts and when they eat in our cafés.

We continue to find ways to enhance the customer benefits of the More Card programme. We recently introduced Baby & More – a new way for parents (and parents-to-be) to enjoy offers and earn additional More Card points on the baby-related products they buy. In addition, customers can now save for Christmas using their More Card with our Christmas Savers programme.

#### The market

The UK food retail market remained highly competitive throughout the year. We do not expect that to change during 2017/18. We will learn from the constantly evolving market and our competitors, and believe that intense competition can again bring out the best in Morrisons.

The longer term impact of Brexit is still unknown. Specifically for food shoppers, if sterling stays at its currently low level we would



#### Listening to our customers...

##### ...and responding

Our More Card allows customers to collect points every time they shop with us. These points can be converted into savings on their shopping trip.



expect pressure to build on imported food input prices.

As a British manufacturer and retailer sourcing home grown product wherever possible, and as British farming's biggest single direct customer, we feel well-placed to mitigate some of those pressures. We are determined to work with growers, farmers, manufacturers and other suppliers to do the best we possibly can for our customers. Morrisons is a value brand and our customers respond well to us working hard to deliver the best possible quality at the lowest price.

We do not operate in a vacuum and market forces are very important. For example, the current oil price rise has been putting pressure on prices at the pump, making household food budgets tighter for our customers. We are also mindful of other market and economic factors such as rising property, employment, energy and distribution costs.

While recognising the volatility of the various market forces, we plan for them and can work with them. Our turnaround is about investing in opportunities and good execution, and is more in our control than it is dependent on the market. If we continue to serve our customers better, we expect to continue to recover Morrisons whatever the prevailing food retail market conditions.

In addition, as we broaden Morrisons and make the brand more accessible, our addressable market also broadens too.

It is clear that customer shopping habits are evolving, with customers choosing to shop more frequently and through more channels, with online and convenience increasingly important markets.

We are following the customer into online, convenience and areas of wholesale supply.

However, the supermarket channel still represents the majority of the UK grocery market. It is forecast that this will continue to be the case for many years. Therefore, making our core supermarkets strong again is a key priority for our turnaround.

We also have exciting opportunities to provide our customers with more popular and useful services when they visit our stores. So, our market is widening into other areas outside of, but complementary with, food retail.

## Performance review continued

# Our colleagues

*Listening to colleagues is informing our plan*

### HIGHLIGHTS

People progressing from the shop floor to more senior positions in 2016/17

920

Number of store managers who participated in 'My Job' training

491



### Listening to our colleagues...

#### ...and responding

Our annual 'Mastercraft' competition has been extended to Manufacturing colleagues and more categories.

#### Our five ways of working

Our five ways of working, introduced across the business during 2016, provide the framework of how we operate as a business and colleagues are reviewed against them as part of their annual performance review. The five ways of working are:

- Customers first
- Teamwork
- Freedom in the framework
- Listening and responding
- Selling, controlling costs, growing profits, removing waste

#### Our colleagues have a say in what matters

Listening is fundamental to shaping our colleague-led turnaround plan. Our 'Your Say' survey was completed in March 2016 by two-thirds of colleagues and included over 69,000 free text comments, every one of which was read.

Our measure of overall colleague engagement was over 75% in 2016 and included improvement in all business areas. Each area of the business saw an improvement in key questions such as 'I receive a fair day's pay for the work I do' and 'I am proud to work here', reflecting our significant payroll investment, especially the increase to £8.20 per hour for all our store colleagues.

We introduced 'Your Say' forums in July 2016 across all stores and sites for colleagues at all levels. These are colleague driven groups that are empowered to listen hard and respond quickly to make Morrisons a better place to work and shop. Any suggestion which cannot be acted upon locally is sent centrally for review and response.

#### Highly valued and treated with respect

It is critical that colleagues feel valued and that they share in the success of the business. The business wide colleague bonus scheme was changed for 2016/17 with each store or site rewarded for performance against service measures which they can influence directly. In its first year, the new measures resulted in a payout equivalent to around 9% of the underlying profit before tax. During the year, we launched a new uniform for store colleagues which is better suited to each role. In addition, we now provide a free laundry service for colleague uniforms in all our fresh food areas.

Having listened to our colleagues we have developed a new recognition programme which has been introduced across all business areas during 2016. The new 'Thank You' programme gives our managers the tools and freedom to be able to recognise their colleagues in a way which is personal to them.

#### The opportunity to develop and grow

During the year, we have focused on developing our colleagues to achieve our priorities and to support our turnaround.

This year we designed our 'My Job' and 'Our five ways of working' programmes which have been delivered to all of our store managers and Buying teams. These colleagues spent time understanding their roles and developing both their technical and leadership skills. In 2017, we intend to extend the programme to all our store management teams and to Manufacturing, Logistics and People teams.

To support our food makers and shopkeepers we trained over 6,000 colleagues on Fruit & Veg during 2016 and trained 2,500 new Retail team managers on the technical skills for their role.

Our apprentice and graduate programmes remain popular, with around 200 colleagues starting their career on one of our schemes in areas including craft skills, engineering and finance. Accelerated learning programmes in Manufacturing and Logistics have continued to provide a way to fast track colleagues to gain new skills at pace, and progress to the next stage in their career plans.

We made a commitment to all colleagues across the business that they will have a career conversation every year. This has supported us in managing our talent and succession plans more effectively, leading to successfully placing individuals into key roles across the business.

We held our sixth annual 'Mastercraft' competition in November. 'Mastercraft' is our in-house competition celebrating the talent of our very best food makers and shopkeepers that we have in our business.

The title of 'Mastercraft Champion 2016' was contested by 46 finalists (including for the first time colleagues from our Manufacturing business) across Butchery, Fish, Deli, Bakery, Cake Shop, Wine, Fruit & Veg and Flowershop. The day was a huge success and highlights what makes Morrisons unique, our food making and shopkeeping skills, through our talented in-store and site colleagues.

# Our suppliers

*Working closely with our supply chain to improve the shopping trip for customers*

## HIGHLIGHTS

Percentage of Morrisons branded beef, lamb, pork, chicken, milk and eggs sourced in the UK

# 100%

Suppliers taking part in our listening survey

# over 500



### Listening to our suppliers...

#### ...and responding

In October 2015, we launched 'Milk For Farmers'. We have since expanded the range to 15 product lines.

Our turnaround is powered by listening and that will define how and what we improve. We work closely with our suppliers to build strong, mutually beneficial relationships and to ensure the best results for our customers.

### Strong supplier relationships

Our ambition is always to have lasting, mutually beneficial arrangements with our suppliers, responsible and fair trading terms and practices in line with the Groceries Supply Code of Practice (GSCOP). We work closely with our suppliers to encourage and promote responsible practices throughout the supply chain, helping to ensure sustainable supply for future generations.

During the year, we worked on improving the way we buy our products – to buy and sell simply. This included simplifying our supplier arrangements to facilitate relationships built on trust and teamwork, allowing us to speed up, be more competitive and ultimately serve customers better.

Our ways of working with our suppliers centre around building a culture of putting customers first, mutual respect and listening. We have been listening hard to our suppliers as we continue to turnaround the business. During 2016, we conducted an independent supplier listening survey in which over 500 suppliers participated. This survey, which will be repeated regularly, builds on our day-to-day interactions with suppliers and allows us to understand views across many different categories. We understand that how we need to work with our suppliers will differ by category and according to size of supplier. This survey allows us to gain a significant level of insight into how we can work more effectively with all our different suppliers.

### Our supply chain

Our vertically integrated business model means we control more of our supply chain and have closer relationships with farmers and growers. We have greater control over supply chain visibility, quantity and quality, which reduces risk as we know where our food comes from. These relationships allow us to better understand our supply chain and work together to ensure the highest quality and ethical standards.

We take pride in our British heritage and buy British wherever possible. 100% of our Morrisons branded beef, lamb, pork, chicken, milk and eggs are sourced in the UK. Buying British reduces food miles, adds to the national economy, strengthens agricultural industries and supports rural communities.

In October 2015, we launched our 'For Farmers' range, giving customers the choice to buy a brand of products where a clear element of the proceeds goes back to farmers. During the year, we have increased the range to 15 product lines, covering milk, cream, cheese, butter and bacon. Customers value this choice and these options have proved popular, with strong sales across the range. For example, over 58 million litres of 'Milk for Farmers' has been sold in our stores. The range has generated over £5m of additional income for farmers, since it was launched.

Read what we've been doing in our Corporate responsibility section on page 20.

### Modern Slavery statement

Morrisons is subject to the provisions of the Modern Slavery Act 2015 and the Group will publish its first statement this year in line with the required timescales. A copy of the statement will be available on [www.morrisons-corporate.com](http://www.morrisons-corporate.com) and submitted to the Business and Human Rights Resource Centre's (BHRR) Central Registry for Modern Slavery Statements.

## Chief Financial Officer's review

# Our shareholders

*Capital discipline and generation of significant levels of sustainable free cash*

**Trevor Strain**  
Chief Financial Officer



The balance sheet is a strong foundation for all elements of our strategy

## HIGHLIGHTS

Net debt\*

**£1.2bn**

£1.6bn lower than its peak in 2013/14

Free cash flow\*

**£2.3bn**

Delivered over three years

\*See the Glossary on page 122 for definition

## Introduction

2016/17 was a year of good progress towards our aim of becoming a broader, stronger business. We continued to listen hard to what our customers and colleagues told us. Responding quickly and delivering on our six priorities meant a better shopping trip for customers, which enabled us to deliver improved like-for-like sales, positive volumes and higher profits.

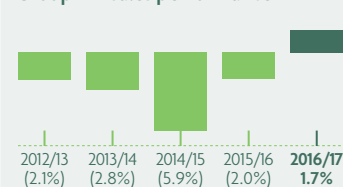
Capital discipline and a focus on cash and returns remains at the heart of what we do, and we are pleased with the progress we have made this year but we remain in the Fix phase of our recovery and have much more to do.

The balance sheet with high freehold ownership, well funded pension schemes and falling debt are sources of financial strength and create a strong foundation for all elements of our strategy. Three years ago we announced a £1bn cost saving programme. We have delivered savings of over £390m in the year, taking the total over the three years to over £1bn. We are making good progress against our target of £50m to £100m of incremental profit from becoming a broader, stronger business. We exceeded our £2bn three-year free cash flow target six months early and have continued to reduce net debt, ending the year at £1.2bn, less than half of the level of three years ago.

During the next year we aim to grow the business by connecting more with our core customers and improving the supermarkets, whilst tightly controlling costs. Growth will continue to be capital light, disciplined and sustainable. Our focus on cash improvement programmes will continue next year.

## Key Measures

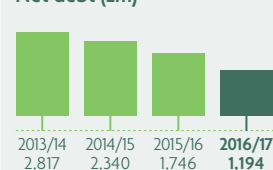
### Group LFL sales performance



### Definition

See page 5 for definition.

### Net debt (£m)



### Definition

A metric that shows the Group indebtedness. Net debt is cash and cash equivalents, non-current financial assets and current financial assets, less borrowings, current financial liabilities and non-current financial liabilities.

## Summary income statement

	2016/17 £m	2015/16 £m
Turnover	16,317	16,122
Operating profit	468	314
Net finance costs	(145)	(99)
Share of profit of joint ventures	2	2
<b>Profit before tax</b>	<b>325</b>	<b>217</b>
<b>Underlying profit before tax</b>	<b>337</b>	<b>242</b>
One-off restructuring costs	–	60
<b>Underlying profit before restructuring costs and tax</b>	<b>337</b>	<b>302</b>
Underlying earnings per share	10.86p	7.77p



## Turnover

Total turnover during the period was £16.3bn, up 1.2% year-on-year. Store and online turnover of £12.7bn, excluding fuel, was down by 0.5%. This comprised LFL up 1.7% (including a contribution of 0.9% from online) and a negative 2.2% contribution from net new space due to the impact of the closure of underperforming stores.

Sales improved through the year, and we were pleased that quarter four was our fifth consecutive period of positive LFL sales growth and the seventh consecutive period of positive LFL volume growth.

Deflation eased through the year but we continued to invest in being more competitive and driving volume growth through the core business. Customers responded to the improvements we made to the shopping trip and transactions were up 4.0% for the year.

Fuel sales increased by 7.3% to £3.4bn.

The impact of weaker sterling and increasing oil prices in the second half meant prices rose year-on-year, but we continued to remain very competitive and both fuel sales and volumes were, once again, strong.

## Operating profit

	2016/17 £m	2015/16 £m
Operating profit	468	314
Underlying adjustments:		
– Impairment and provision for onerous contracts	(6)	87
– Profit/loss on disposal and exit of properties and sale of businesses and investments	(32)	(97)
– Pension scheme set-up costs	–	35
– Other exceptional costs	2	–
<b>Underlying operating profit</b>	<b>432</b>	<b>339</b>

Operating profit was £468m (2015/16: £314m). Since the impairments made in 2014 and 2015, individual store performance has varied and as a result we have booked a write back of £6m made up of freehold stores impaired written back (£191m), freehold stores impaired (£147m) and charges on onerous contracts (£38m). In addition, in line with our plan to optimise assets, we generated profit on disposal of £32m, including £13m relating to the completion of the disposal of our investment in Fresh Direct Inc. Before these items, underlying operating profit was £432m (2015/16: £339m).

## Underlying profit

	2016/17 £m	2015/16 £m
Reported profit before tax	325	217
Underlying adjustments:		
– Impairment and provision for onerous contracts	(6)	87
– Profit/loss on disposal and exit of properties and sale of businesses and investments	(32)	(97)
– Costs associated with the repayment of borrowings	56	–
– Pension scheme set-up costs	–	35
– Net pension interest income	(8)	–
– Other exceptional costs	2	–
<b>Underlying profit before tax</b>	<b>337</b>	<b>242</b>
<b>Underlying profit margin</b>	<b>2.1%</b>	<b>1.5%</b>

Reported profit before tax was £325m (2015/16: £217m), and underlying profit before tax, which excludes exceptionals, was £337m (2015/16: £242m). Basic earnings per share increased to 13.1p (2015/16: 9.51p). Underlying basic earnings per share increased to 10.86p (2015/16: 7.77p), reflecting the increase in underlying profit before tax.

## Debt, cash flow and working capital

### Summary cash flow

	2016/17 £m	2015/16 £m
Cash generated from operations before onerous capital payments	1,207	1,055
Onerous capital payments	(94)	(29)
<b>Cash generated from operations</b>	<b>1,113</b>	<b>1,026</b>
Proceeds from sale of property, plant and equipment and sale of businesses and investments	123	320
Capital expenditure	(419)	(365)
Dividends paid	(118)	(260)
Dividends received	8	8
Purchase of shares in subsidiary	–	(3)
Purchase of own shares	(5)	(13)
Tax and interest	(129)	(136)
Costs incurred on repayment of borrowings	(42)	–
Other non-cash movements	21	17
<b>Movement in net debt</b>	<b>552</b>	<b>594</b>
Opening net debt	(1,746)	(2,340)
<b>Closing net debt</b>	<b>(1,194)</b>	<b>(1,746)</b>

We exceeded our £2bn three year free cash flow target six months early, and have continued to reduce net debt ending the year at £1.2bn, down £552m from last year.

Cash capex was £419m. Cash outflow on onerous commitments which were previously provided was £94m.

Operating working capital inflow was £360m, taking the total delivered over three years to £914m. A focus on cash is firmly embedded in the business, and we made further progress against our cash improvement programmes. The key driver of the inflow in the year was improving the commercial dynamics in our fuel business.

## Interest

Net finance costs were £145m, up from £99m last year due to one-off costs of £56m relating to our commitment to reduce debt. During the last year, we have redeemed \$250m US Private Placement loan notes (USPP), and completed tender offers of £360m across three sterling bonds and one euro bond. We also repaid a £200m bond facility which reached maturity. We chose not to renew a £150m credit facility that expired. Underlying net finance costs were £97m (2015/16: £99m). Liquidity remains very strong and our £1.35bn revolving credit facility has been undrawn since October 2015.

## Tax

The management of our tax affairs is focused on ensuring that we pay the tax we are obliged to pay in accordance with the law and that our tax affairs are consistent with our broader corporate objectives. We regard this as being important in protecting our reputation and brand, and have a tax management framework which ensures the needs of all of our stakeholders are considered.

The Group is committed to paying all of its taxes in full and on time. We are a major contributor across a wide range of UK taxes. In 2016/17, Morrisons made net payments of £1,056m to the UK Government of which £545m was borne by Morrisons and the remaining £511m was collected on behalf of our colleagues, customers and suppliers.

UK corporation tax payments made during the year were £31m compared to the current tax charge of £57m in the income statement. The difference is because the Group was not required to make any payments relating to the 2015/16 tax charge, which would normally fall due for payment during 2016/17, during the year because it was paid in full in the prior year. The payments made during 2016/17 represent instalment payments against the 2016/17 tax charge.

The remaining balance of the 2016/17 tax charge is due for payment next year. The Group expects tax payments made in future years to be broadly equal to the current tax charge for that year.

## Chief Financial Officer's review continued

### Summary balance sheet

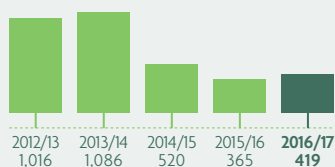
	2016/17 £m	2015/16 £m
Fixed assets and investments	7,761	7,775
Working capital	(2,009)	(1,710)
Provisions and tax	(767)	(749)
Net pension asset	272	186
Net debt	(1,194)	(1,746)
<b>Net assets</b>	<b>4,063</b>	<b>3,756</b>

### Pensions

The assumptions relating to the pension schemes remain prudent. The net surplus on the balance sheet is £272m, an increase of £86m since last year. In the period, with the Trustees, we completed the triennial funding valuation which shows a funding surplus in each of the three schemes.

### Key Measures

#### Capital expenditure (£m)



#### Definition

Measured as additions to property, plant and equipment, investment properties, intangible assets held-for-sale and investments as per the cash flow statement.

### Capital expenditure

Capital expenditure increased to £419m, from £365m in 2015/16. This was lower than the planned c.£450m, as some projects moved into 2017/18. We expect this timing difference, in addition to last years' underspend, to reverse in 2017/18.

A large part of our expenditure was spent on refreshing our stores. We completed 100 Fresh Look refits during the year and expect to complete the whole of the estate in the coming years.

### Space

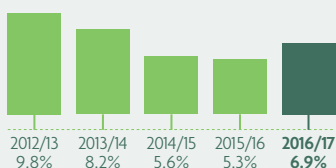
	At 31 January 2016	New stores	Extensions	Store closures	At 29 January 2017
<b>Total number of stores</b>	498	1	–	(8)	491
Total area in square feet (000)	14,142	40	43	(131)	14,094
Number of petrol filling stations	336	–	–	(2)	334

### Return on Capital Employed (ROCE)

ROCE at 6.9% remains a key measure. We are focused on improving returns through the work we are doing on the operational performance drivers, specifically volume and costs. We are also optimising existing assets and will continue to deal with underperforming assets.

### Key Measures

#### Return on Capital Employed (ROCE)



#### Definition

ROCE is a relative profit measure showing the return generated from investments in assets. For a more detailed definition, see the Glossary on page 122.

### Key balance sheet metrics

	2016/17	2015/16
Interest cover	4.6 times	4.1 times
Net debt/EBITDA	1.4	2.2
Gearing	30%	46%
ROCE	6.9%	5.3%

### Financial strategy

#### Capital allocation framework

- 1 Investing in maintaining the estate and reducing cost
- 2 Maintaining debt ratios to support investment grade rating
- 3 Investing for profitable growth
- 4 Paying dividends in line with stated policy
- 5 Returning surplus capital to shareholders

Our capital allocation framework is set out above and is unchanged. Our first priority is to invest in our stores and infrastructure, and to reduce costs. Second, we will seek to maintain debt ratios that support our target of an investment grade credit rating. Third, we will invest in profitable growth opportunities. Fourth, we will pay dividends in line with our stated policy and then any surplus capital will be returned to shareholders.

#### Shareholder returns

To reflect the Board's commitment to the capital allocation framework described above, whilst providing the necessary financial resources to invest in delivering the turnaround, we set guidance that total annual dividends should be sustainable and covered around two times by underlying earnings. In line with this guidance, the final dividend will be 3.85p per share, bringing the total for the year to 5.43p.

Profits are up, debt is down and we generated positive cash, before disposals and after dividend. There is a significant amount of self-help and we are confident in the opportunity to deliver £50m to £100m incremental profit from making Morrisons a broader, stronger business. The balance sheet is strong, and getting stronger, and with continued improvement in the customer shopping trip we aim to deliver improving returns and value to shareholders.

**Trevor Strain**  
Chief Financial Officer

# Managing our risks

*Recognising the effect of uncertainty on our business means that we are in a better position to achieve our objectives, respond to emerging risks and create opportunities*

## Risk management approach

The achievement of our six priorities depends on our ability to make sound, risk-informed decisions. Managing risk and uncertainty is an integral part of doing business. We manage increasing uncertainty as we respond to rapid changes in our industry and the wider political-economic climate by maintaining a business-wide understanding of our key risks and how to manage them. This assists in delivering our promises to customers and shareholders.

## The risk management process

Our risk management framework has been built to identify, evaluate, mitigate and monitor those risks which threaten the achievement of our six priorities. The framework incorporates both a top-down approach to identify the Group's principal risks and a bottom-up approach to identify operational risks.

At the core of the risk management process are the risk registers for each function. These detail the key operating risks and are used to assess the gross level of risk (likelihood and impact), mitigating controls, the resultant net level of risk and risk mitigation plans with dates and target level of risk. The risk registers are owned and managed by operational management, with the head of each function certifying annually that these have been reviewed and action plans are in place where required. The risk registers are formally reviewed by a sub group of the Executive Committee.

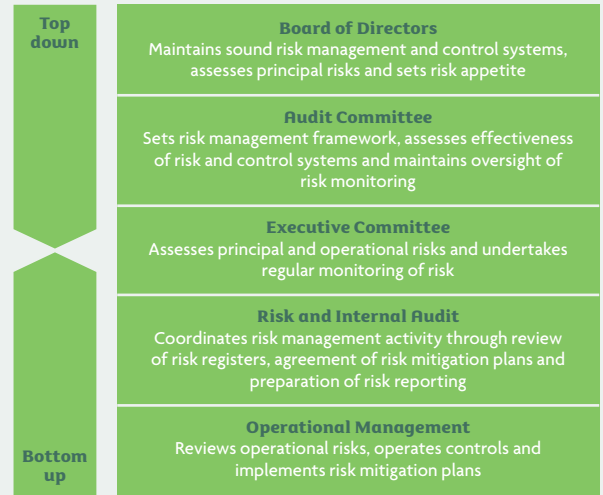
A Group risk register is reviewed and updated at least twice annually by the Executive Committee. It details the Group's principal risks, owners, the level of risk and mitigating actions. The Executive Committee's assessment of these risks takes into account the operating risks, strategic risks, external factors and any emerging risks. The principal risks are monitored every month by the Executive Committee using key risk indicator reporting, supplemented by more detailed reviews as appropriate.

The Risk and Internal Audit function facilitates the preparation of both functional and Group risk registers. It supports the Audit Committee in reviewing the effectiveness of our risk management and internal control systems.

### The risk management process



### The risk management framework



Where potential weaknesses are identified, our Risk and Internal Audit teams work with the business to agree robust actions to mitigate these.

The Audit Committee supports the Board in establishing a robust risk management framework by approving the risk management process and reviewing the Group's principal risks and key risk indicator reporting.

Read more on risk governance in the Audit Committee report on page 28.

## Key areas of focus

Key activities in 2016/17 included the review and update of the key controls framework ensuring that key controls are identified and assessed as part of the review of risk registers. The Group's risk appetite framework has also been developed. The focus in 2017/18 will be establishing the rotational monitoring of key controls and aligning reporting and ways of working to risk appetite.

## Principal risks

The Directors have carried out a robust assessment of the principal risks facing the Group, including those that would threaten its business model, future performance, solvency or liquidity.

These risks are further detailed on the following page.

This assessment of principal risks has resulted in some changes from those risks disclosed last year. Specifically, a 'regulation' risk has been added which includes Groceries Supply Code of Practice (GSCOP) and other key areas of compliance. The 'supplier relationships' risk has been removed as the key elements are now covered in other risk areas.

The impact of the UK's exit from the EU has been considered and, whilst not seen as a separate risk, it has been reflected in some of the other risk areas. There are some uncertainties, particularly in relation to the impact of imported food prices and potential changes to access to EU labour; however, there has been no material change at this stage to the Group's residual risk profile.

Certain risks are inherent in the business and are fundamental to the achievement of all of our key priorities. Other risks could directly impact the achievement of certain key priorities.



### Viability statement

For more information, see page 30

## Risk continued

# Principal risks





*The principal risks have been identified following a robust assessment by the Directors*

Key changes in the year include the introduction of a 'regulation' risk and the consideration of the impact that an exit from the EU would have on the business. The risks, which are shown in no particular order, are disclosed along with their alignment to the six priorities and the movement in residual risk during the year. Residual risk is stated after considering the actions taken by management in response to new and emerging issues impacting the identified risks.








RISK TYPE	DESCRIPTION	MITIGATION
<b>Business interruption</b> 	<p>There is a risk that a major incident, such as a natural disaster or strike action, could cause significant disruption to business operations. The Group's response must be appropriate to minimise disruption and reputational damage.</p>	<ul style="list-style-type: none"> <li>• We have recovery plans in place covering our stores, depots, sites and offices;</li> <li>• These plans include, where appropriate, secondary locations which would be used as backup in case of an incident;</li> <li>• A Crisis Management Group is in place to oversee these plans and to manage and respond to any major incidents; and</li> <li>• We conduct supplier risk assessments and have contingency plans in place, where possible, to manage the risk of loss of supply.</li> </ul>
<b>Competitiveness</b> 	<p>The Grocery sector continues to have high levels of competitive activity, particularly in relation to price and enhancement of service. The impact of the EU referendum on exchange rates has affected some commodity prices and we need to remain competitively priced through these fluctuations.</p> <p>If we do not engage with our suppliers and effectively manage our trade plan to remain competitive, there is a risk that we will not achieve our financial targets.</p>	<ul style="list-style-type: none"> <li>• We review and actively manage our key price-points, sales proposition, and promotional and marketing campaigns such as 'Morrisons Makes It' which emphasises our point of difference;</li> <li>• We work closely with our suppliers to build joint business plans, ensuring a competitive customer offer and a resilient supply base;</li> <li>• We continually review our range and quality and respond to customer feedback; for example, 'The Best' premium own brand range was launched during 2016;</li> <li>• Competitor pricing positions and market trends are reviewed on a weekly basis; and</li> <li>• Our strong balance sheet and proven ability to generate cash will allow us to further invest in our proposition.</li> </ul>
<b>Customer</b> 	<p>There is a risk that we don't meet the needs of our customers in respect of price, range, quality and service. We need to be responsive to changes in customer confidence and trends resulting from changes to the economy and the UK's exit from the EU. If we don't provide the shopping trip that customers want, we could lose sales and market share.</p>	<ul style="list-style-type: none"> <li>• One of our six priorities is 'to serve customers better' and we have a range of activities to support that (see page 6);</li> <li>• A large-scale programme of customer listening groups is in place to gain a deep understanding of what our customers want and, where we can improve, these have informed key activities such as our store 'Fresh Look' programme;</li> <li>• We closely monitor research on customer perceptions and respond quickly where possible with support from a senior level. For example with a steering group to address any particular risks arising from the UK's exit from the EU; and</li> <li>• We have worked with wholesale partners to make Morrisons products accessible to more customers and continue with plans to further expand the geography covered by our Online offering.</li> </ul>
<b>Data</b> 	<p>A security breach leading to loss of customer, colleague or Group confidential data is a key aspect of this principal risk. A major data security breach could lead to significant reputational damage and fines. The risk environment is challenging, with increased levels of cybercrime and the forthcoming General Data Protection Regulation (GDPR).</p>	<ul style="list-style-type: none"> <li>• The Group has an Information Management Security Group which has the responsibility for overseeing data management practices, policies, awareness and training;</li> <li>• Information security policies and procedures are in place, including encryption, network security, systems access and data protection;</li> <li>• This is supported by ongoing monitoring, reporting and rectification of vulnerabilities; and</li> <li>• The Group is taking steps to ensure compliance with the GDPR which applies from May 2018.</li> </ul>

RISK TYPE	DESCRIPTION	MITIGATION
<b>Financial and treasury</b> 	<p>The main areas of this principal risk are the availability of funding and management of cash flow to meet business needs, fluctuations in commodity prices and foreign exchange rate movements.</p>	<ul style="list-style-type: none"> <li>• The Group's Treasury function is responsible for the forward planning and management of funding, interest rate, foreign currency exchange rate and certain commodity price risks (see note 7). They report to the Treasury Committee and operate within clear policies and procedures which are approved by the Board;</li> <li>• There are governance processes in place to control purchases in foreign currency and management of commodity prices; and</li> <li>• For livestock and produce, we track prices and forecasts and enter into long term contracts where appropriate to ensure stability of price and supply.</li> </ul>
<b>Food safety and product integrity</b> 	<p>There is a risk that the products we sell are unsafe or not of the integrity that our customers expect. It is of utmost importance to us and to the confidence that customers have in our business that we meet the required standards. If we do not do this it could impact business reputation and financial performance.</p>	<ul style="list-style-type: none"> <li>• Strict standards and monitoring processes are in place to manage food safety and product integrity throughout the Group and our supply chain;</li> <li>• Regular assessments of our suppliers and own manufacturing facilities are undertaken by a dedicated team to ensure adherence to standards;</li> <li>• Our vertical integration model gives us control over the integrity of a significant proportion of our fresh food;</li> <li>• Management regularly monitors food safety and product integrity performance and compliance as well as conducting horizon scanning to anticipate emerging issues; and</li> <li>• The process is supported by external accreditation and internal training programmes.</li> </ul>
<b>Health and safety</b> 	<p>The main aspect of this principal risk is of injury or harm to customers or colleagues. Failure to prevent incidents could impact business reputation and customer confidence and lead to financial penalties.</p>	<ul style="list-style-type: none"> <li>• We have clear policies and procedures detailing the controls required to manage health and safety risks across the business;</li> <li>• An ongoing training programme is in place for front-line operators and management;</li> <li>• A programme of health and safety audits is in place across our stores, depots, sites and offices with resources dedicated to manage this risk effectively; and</li> <li>• Management regularly monitors health and safety performance and compliance.</li> </ul>
<b>People</b> 	<p>Our colleagues are key to the achievement of our plan, particularly as we make changes to the business. There is a risk that if we fail to attract, retain or motivate talented colleagues, we will not provide the quality of service that our customers expect.</p> <p>Business change and the challenging trading environment may impact on colleagues leading to an increase in this risk. There is uncertainty on potential changes to employment regulations when the UK leaves the EU and this could result in a retention and recruitment risk, particularly at some manufacturing sites.</p>	<ul style="list-style-type: none"> <li>• We have competitive employment policies, remuneration and benefits packages;</li> <li>• A Group-wide reward framework is in place and roles are evaluated against an external framework, driving stronger consistency of rewards;</li> <li>• Our training and development programmes are designed to give colleagues the skills they need to do their job and support their career aspirations;</li> <li>• Line managers conduct regular talent reviews and processes are in place to identify and actively manage talent (see more in our Colleagues section on page 12);</li> <li>• Colleague engagement surveys, listening sessions and networking forums are used to understand and respond to our colleagues; and</li> <li>• A senior level steering group is in place to monitor and take action on any particular people risks relating to the UK's exit from the EU.</li> </ul>
<b>Regulation</b> 	<p>The Group operates in an environment governed by strict regulations including GSCOP, competition, employment, health and safety, and regulations over the Group's products. There is uncertainty on any potential changes to regulations relating to the UK's exit from the EU. In all cases, the Board takes its responsibilities very seriously and recognises that breach of regulation can lead to reputational damage and financial penalties to the Group.</p>	<ul style="list-style-type: none"> <li>• We have a GSCOP compliance framework in place including training for relevant colleagues and processes to monitor compliance;</li> <li>• We have a senior level working group in place to review and improve GSCOP compliance activity;</li> <li>• We have a channel for suppliers to provide feedback and a Code Compliance Officer;</li> <li>• We have a senior level steering group in place to monitor and take action on any potential regulatory change resulting from the UK's exit from the EU; and</li> <li>• We have training, policies and legal guidance in place to support compliance with Competition Law and other regulations.</li> </ul>

Key

-  Increase in residual risk
-  No change
-  Decrease in residual risk
-  New risk in the current year

Link to six priorities

-  To be more competitive
-  To serve customers better
-  Find local solutions
-  Develop popular and useful services
-  To simplify and speed up the organisation
-  To make the core supermarkets strong again
-  Underpins all six priorities

Corporate responsibility

# Focusing on the issues that matter to our stakeholders

## Responsible retailing

Our corporate responsibility programme ensures we operate in a way that is right for our customers, colleagues, suppliers and shareholders whilst making a positive contribution to society and taking good care of the environment.

This section covers corporate responsibility highlights during our 2016/17 financial year as well as future plans for our strategy. It is just a snapshot. Further information on how we operate as a responsible retailer can be found on our website at [www.morrisons-corporate.com/cr](http://www.morrisons-corporate.com/cr).

## What's next?

We have been listening to our stakeholders to help review and redevelop the programme to ensure it remains relevant to our business. This year's Corporate Responsibility Report will set out our new strategy for 2017/18 and beyond detailing key priority issues for the business alongside our streamlined commitments and KPIs.

## UN Sustainable Development Goals

We aim to be good corporate citizens and support global initiatives. As such, we are looking at the UN Sustainable Development Goals and how we can align our strategy to them in a meaningful way.



Our Corporate Responsibility Report 2016/17 will be available for you to download later in the year. Please visit [www.morrisons-corporate.com/cr](http://www.morrisons-corporate.com/cr)

## Help British suppliers to be competitive, profitable and sustainable

### Why it matters?

British farming is essential to our business as it keeps supply chains short and efficient. It's important that we support suppliers to create profitable, affordable, high quality products for our customers.

### What we're doing

**100%**  
British own brand fresh meat sold in our stores

**£5.1m**  
extra income generated for farmers through 'ForFarmers' range

### What we will do next

- We will establish British Beef Shorthorn as the breed for our 'Best' range.
- We will build a pig production programme for greater eating quality and affordability.
- We will develop more integrated dairy beef supply chains through alliances with our milk processors and their farmers.
- We will support local suppliers through 'The Nation's Local Foodmakers' programme.

## Ensure the highest standards of food safety and integrity

### Why it matters?

It is a priority that our products and services meet all food safety and legal standards. This significantly reduces risk and meets customer expectation for quality and value.

### What we're doing

**7%**  
below the FSA target for campylobacter levels

Focus on antibiotics use within farming

### What we will do next

- We will establish the monitoring and continuous improvement of antibiotic use in chicken, eggs and pork production.
- We will continue to meet Food Standards Agency (FSA) targets on campylobacter levels.
- We will ensure the most suitable methods are used for microbiology testing.

## Ensure fair working conditions for our suppliers

### Why it matters?

We take responsibility for ensuring that workers are treated well and paid fairly throughout our supply chain. Doing so secures the best suppliers, improves product integrity and reduces our risk.

### What we're doing

**1,000**  
ethical trade audits undertaken in 2016

**500**  
key supplier colleagues attended modern slavery awareness training

### What we will do next

- We will ensure visibility of valid ethical audits of high and medium risk tier one suppliers.
- We will publish our modern slavery and human trafficking statement by the end of June 2017.

## Making a positive difference in the communities we serve

### Why it matters?

Our stores play an active and positive role in their local community. Doing so helps us to support causes close to the hearts of our colleagues and customers.

### What we're doing

**£7.5m**  
donated by the Morrisons Foundation to local charities

**£2.6m**  
raised for charity partner Sue Ryder (£7.2m since Feb 2014)

### What we will do next

- We will work with our new charity partner, CLIC Sargent, over the next three years to raise funds to help stop cancer impacting young lives.
- We will continue to make a positive difference in the communities close to our stores by donating over £5m in grant awards.
- We will continue to support high profile partnerships in our stores such as the Poppy Appeal and Children in Need.

## Making it easier for customers to live healthier lives

### Why it matters?

As a food retailer, we must provide healthier choices to our customers. Doing so reflects social need, can help to increase sales and greater enhance our brand perception.

### What we're doing

  
New healthier eating brand 'Eat Smart' launched

**88**  
tonnes of sugar removed from own brand breakfast cereals

### What we will do next

- We will reduce sugar as an ingredient in key categories which contribute to children's sugar intake.
- We will implement a nutrition and wellness strategy.
- We will continue to roll out Eat Smart endorsed products.

## Source responsibly

### Why it matters?

Increasing global demand and pressure for key commodities can lead to ill managed supply chains, erosion of land, illegal logging and the destruction of natural habitats and ecosystems. We must ensure that our supply chains remain sustainable and that we conserve the natural capital we're dependent on.

### What we're doing

  
Continued work with Responsible Fishing Scheme

**RSPO**  
certified palm oil in own brand products

### What we will do next

- We will continue to work on seafood sourcing improvement projects to ensure fresh fish is responsibly sourced.
- We will ensure all timber and timber derived products are third party certified sustainable or from 100% recycled material.
- We will continue to monitor supplier compliance to source Roundtable on Sustainable Palm Oil (RSPO) certified palm oil and derivatives in own brand products.

## Reduce food waste

### Why it matters?

We must drive smarter supply chains by reducing avoidable food waste. Doing so can reduce environmental risk, create innovation and drive efficiencies.

### What we're doing

Over **2m**  
unsold food products from stores donated to local community groups

**25,000**  
tonnes of Wonky Veg sold during 2016

### What we will do next

- We will continue to increase the amount of surplus food we redistribute from our operations to ensure that good food is never wasted.
- We will work with Waste and Resources Action Programme (WRAP) to look at food waste hotspots within our operations.
- We will further support the 'Love Food Hate Waste' initiative, to help our customers reduce food waste in their home.


## Look after our colleagues

### Why it matters?

The success of Morrisons is dependent on recruiting, developing and retaining the right people. Supported and engaged colleagues enable us to deliver great customer service and meet our six priorities.

### What we're doing

'Your Say' forums launched

  
For more information please go to Our colleagues section on page 12

### What we will do next

- We will ensure our colleagues have the right tools to do their job through 'My Job' training. We will progress the best talent within our business and support diversity.
- We will continue to run 'Your Say' forums and improve overall engagement scores.

Continued on the next page

## Corporate responsibility continued

### Reduce general operational waste and carbon emissions

#### Why it matters?

It's important that we minimise environmental risks to our business, protect natural capital and create efficiencies throughout our operation.

#### What we're doing

**26.9%**  
reduction in operational carbon emissions (2005 baseline)

**2025**  
Courtauld commitment signatories

#### What we will do next

- We will help to deliver progress against our commitment to WRAP's Courtauld 2025 agreement, which is a collaborative action to cut the resource needed to provide our food and drink by one-fifth over ten years.
- We will continue to make progress against our 30% absolute reduction in operational carbon emissions by 2020.
- We will ensure Carbon Trust re-certification, which we have achieved since 2008. The Carbon Trust Standard recognises organisations that take a best practice approach to measuring and managing their environmental impacts.

#### Group GHG emissions for year ending 31 December

Emission source	2004/05 Baseline year	2015/16 Prior year	2016/17 Current year	Change vs baseline
<b>Combustion of fuel and operation of facilities</b>				
Natural gas	99,641	153,473	165,486	66.1%
Haulage	144,497	112,555	119,257	(17.5%)
Business miles	41,656	35,764	33,298	(20.1%)
<b>Fugitive emissions</b>				
Refrigerant	504,431	239,222	235,934	(53.2%)
<b>Energy purchased for own use</b>				
Electricity	780,585	671,562	588,969	(24.5%)
<b>Other</b>				
Staff travel	1,680	1,100	983	(41.5%)
Waste	36,730	20,876	16,657	(54.6%)
Online deliveries	–	9,894	15,101	–
<b>Total</b>	<b>1,609,221</b>	<b>1,244,445</b>	<b>1,175,685</b>	<b>(26.9%)</b>
Intensity ratio: kg CO <sub>2</sub> e per ft <sup>2</sup> GIA	49.0	30.2	27.8	(43.3%)

#### Reducing emissions

##### Methodology

The information above is taken from our Group Carbon Footprint, prepared internally in partnership with Jacobs who also independently verify the Group Carbon Footprint. We have reported for the calendar year 1 January to 31 December for all years in order to remain consistent with our historical footprint reports.

We have used the UK Government's Environmental Reporting Guidelines (June 2013) to prepare these numbers, and the latest emissions factors from the UK Government GHG Conversion Factors for Company Reporting (2016).

The 2013 Environmental Reporting Guidelines state that the baseline year should be recalculated if there have been structural changes that would significantly impact on the organisation's baseline year figures. For this year, we have revised our historical emissions figures to take account of the sale of a number of sites and revisions to carbon conversion factors.

The Group Carbon Footprint includes all major sources of carbon emissions from the operation of the Group's supermarkets, manufacturing and distribution sites, and operation of its haulage fleet. Some minor exemptions are:

#### Subsidiaries and joint ventures

- Wm Morrison (HK) Ltd – Hong Kong office that deals with energy locally.
- Wm Morrison Bananas Ltd – leases a site which is operated by a third party.

#### Sites

- A number of distribution sites are operated by third parties who are responsible for the energy and carbon, including sites at Dordon and Birstall, and sites operated by Clipper Logistics PLC and Bunzl Cleaning & Hygiene Supplies.

#### Omissions

- Fuel oil – only four sites have fuel oil, which is estimated to account for less than 0.1% of the total footprint.

#### Approval of the Strategic report

Pages 2 to 22 of the Annual Report form the Strategic report. The Strategic report was approved by the Board on 8 March 2017 and signed on its behalf by:

**Jonathan Burke**  
Company Secretary  
8 March 2017



## Corporate governance report

# Chairman's governance statement

*I am pleased to introduce on behalf of the Board, Morrisons Corporate governance report for the financial year 2016/17*

**Andrew Higginson**  
Chairman



In a business as fast paced as Morrisons, good corporate governance becomes all the more important

### Corporate governance statement

The Board considers that its corporate governance policies and procedures are appropriate and that the Group has applied the principles and complied with the provisions of the 2014 UK Corporate Governance Code (the 'Code') throughout the financial year 2016/17 and to the date of this Annual Report. The one exception to this is in relation to the external assessment of Board effectiveness which will be discussed later in this report.

The Code is available on the Financial Reporting Council's website ([www.frc.org.uk](http://www.frc.org.uk)).

### Compliance statement

The Board's Corporate governance compliance statement sets out how the Group complies with each of the provisions of the Code. It is available in the investor relations section of the Group's website, [www.morrisons-corporate.com](http://www.morrisons-corporate.com).

This year was another very competitive time in the UK grocery market, but a year in which Morrisons made good progress in its turnaround. This is perhaps best reflected in improving like-for-like sales.

The Board has been very active in supporting management in this journey and overseeing the operational improvement as we provide a better shopping experience for customers. The Board has also devoted time to further developing the Group's long term strategy in such a competitive environment, from overseeing the balance sheet strategy, to reviewing risks and risk appetite, from improving capability in both people and systems, and to ensuring that the Group fulfils its role as a good corporate citizen.

The Board has also spent time with the new Executive Committee and the restructured Leadership team, to help and pass on their experience. Given that several of the Board members took up their positions shortly before the start of the year, there has also been an ongoing familiarisation programme to enable Directors to fully understand the diversity of the business and its component parts.

We were sorry to lose the service of Irwin Lee as a Non-Executive Director during the year. Irwin decided to return to his native Philippines and go back into a full time executive role. We are grateful for his contribution to the Group.

### Board composition and effectiveness

I am delighted to see the Board and management team working well together to guide the Group through this turnaround. I am satisfied that the Board is independent and contains an appropriate mixture of skills and experience. The experience the Board members bring from other companies and industries is being proven to be invaluable in guiding Morrisons on the long and important journey we must make. I also consider that each of the Non-Executive Directors has committed and is able to commit an appropriate amount of time in fulfilling effectively their role and responsibilities on the Board.

As the majority of the Board were appointed during the last financial year, we took the decision to delay the external review of Board effectiveness by one year as noted later in this report. This year we undertook an internal evaluation of the effectiveness of the Board and its Committees. The results are summarised on page 27. The evaluation did not highlight any particular areas of concern, although Board members provided helpful and insightful suggestions which will be considered.

### Diversity

As I stated last year, the turnaround of Morrisons will be customer and colleague led. As such, we recognise the importance of diversity across our colleague base, and the Board itself. This has been key this year, as we have restructured much of the leadership of the business. The Board continues to meet our policy to maintain female representation at not less than 20% with an aspiration to increase this to at least 30%. At the end of the financial year, 29% of total Board composition was female, and at no point during the year was there less than 25% female representation on the Board. The diversity of our Retail team continues to be an area of focus. The proportion of female store managers has increased from 7% to 10% this year whilst the proportion of female regional managers has increased to 30% from 9% last year. We have also actively increased the gender diversity of the Leadership team which is now 18% female.

Progress on the diversity agenda is measured through regular functional talent reviews. These reviews consider the ethnicity, gender, age and length of service of all colleagues.

Retail, particularly grocery retail, is a very fast paced industry. It is particularly important that we have good corporate governance and continually review and challenge ourselves to do better. We will continue to listen hard to our stakeholders and respond quickly where we can as we continue the journey to Fix the business.

**Andrew Higginson**  
Chairman

Board of Directors

# Always listening...

**Trevor Strain**  
Chief Financial Officer



**Appointment**  
Trevor joined the Group in June 2009 as Commercial and Operations Finance Director. In June 2011, he became Finance Director Corporate and took responsibility for the Group's productivity programmes. Trevor joined the Board as Chief Financial Officer on 10 April 2013.

**Experience**  
Prior to joining Morrisons, Trevor worked for Tesco PLC in a number of roles until his appointment as UK Property Finance Director in 2006 and subsequently UK Planning and Reporting Finance Director. Trevor began his career with Arthur Andersen and is a member of the Institute of Chartered Accountants in England and Wales.

**Jonathan Burke**  
Company Secretary



**Appointment**  
Jonathan was appointed as the Group's Company Secretary on 15 February 2017, replacing Mark Amsden.

**Experience**  
As a qualified accountant and Company Secretary, Jonathan has worked at Morrisons for the last 25 years holding various finance, compliance and project roles. He also held the role of Company Secretary between 2001 and 2009.

**Rooney Anand**  
Senior Independent Non-Executive Director



**Appointment**  
Rooney joined the Board as a Non-Executive Director and Senior Independent Director on 1 January 2016.

**Experience**  
Rooney is a highly experienced retail and fast moving consumer goods (FMCG) executive. Following a career with United Biscuits and then Sara Lee, he joined Greene King PLC in 2001 as Managing Director of its brewery company. He was appointed CEO in 2005. Rooney is credited with changing Greene King from a regional brewery and pub business, to a brand-led pub, restaurant and hotel operator. In 2015, he completed Greene King's £770m takeover of the Spirit Pub Group, which made Greene King the largest managed pub group in the UK.

**Committee membership**  
N R C

**Paula Vennells**  
Non-Executive Director



**Appointment**  
Paula joined the Board as a Non-Executive Director on 1 January 2016.

**Experience**  
Paula is currently Chief Executive of the Post Office, a role she has held since April 2012. Paula joined the Post Office in 2007. Previously she was Group Commercial Director of Whitbread PLC having started her career with Unilever and L'Oréal. Paula has held directorships in sales and marketing with a number of major retailers including Dixons Stores Group and Argos. She is Non-Executive Chair of First Rate Exchange Services Limited.

**Committee membership**  
N R C A

**Andrew Higginson**  
Chairman



**Appointment**  
Andrew joined the Group as Deputy Chairman and Chairman Elect in October 2014 and became Chairman at the end of January 2015.

**Experience**  
Andrew is currently the Chairman of N Brown Group PLC and a Non-Executive Director of Woolworths Holdings Limited (South Africa). Andrew was previously the Chairman of Poundland Group PLC, Senior Independent Director of BSKyB PLC and a Non-Executive Director of the Rugby Football Union and McCurrach UK Limited. Andrew was an Executive Director at Tesco PLC for 15 years.

**Committee membership**  
N R C

**Belinda Richards**  
Non-Executive Director



**Appointment**  
Belinda joined the Board as a Non-Executive Director on 1 September 2015. She became Chair of the Audit Committee on 1 January 2016.

**Experience**  
Belinda had a career in professional services for over 25 years, where she operated as a senior adviser in corporate finance and strategy. She was a corporate finance partner at Deloitte and Global Head of Merger and Separation Advisory Services until 2010. Belinda is currently the Senior Independent Director of Grainger PLC, where she also chairs the Remuneration Committee, a Non-Executive Director of Aviva UK Life & Pensions and a Non-Executive Director of the Monks Investment Trust PLC. Belinda serves on the Advisory Group of Audit Committee Chairmen at the Financial Reporting Council and is a member of the Governing Council of the Centre for the Study of Financial Innovation, a not for profit think tank focused on research in Financial Services.

**Committee membership**  
N R C A

**David Potts**  
Chief Executive



**Appointment**  
David joined the Group as Chief Executive on 16 March 2015.

**Experience**  
David is a vastly experienced retailer who joined Tesco PLC at the age of 16 and worked there for 39 years. He rose to become CEO of its Ireland business, its UK retail stores business and then CEO of Tesco Asia. David was also on the Tesco PLC Board from 1998 until he left in 2011. Prior to his appointment as CEO of Morrisons, David held several advisory positions with a number of private equity and consultancy firms and developed his own retail concept to sell general merchandise. He also worked on two extensive retail projects in the UK.

**Committee membership**  
C

**Neil Davidson**  
Non-Executive Director



**Appointment**  
Neil joined the Board as a Non-Executive Director on 1 October 2015. He became Chair of the Corporate Compliance and Responsibility Committee on 1 January 2016.

**Experience**  
Neil has had an extensive career in manufacturing, starting with Northern Foods PLC where he rose to become Managing Director of its milk division. He subsequently became CEO of Express Dairies PLC and then Arla PLC. He has also been a Non-Executive Director of Persimmon PLC and Northern Recruitment Group PLC and the Chair of Leicestershire County Cricket Club. He is currently the Chairman of Produce Investments PLC.

**Committee membership**  
N R C A

**Committee key**

- N Nomination Committee
- R Remuneration Committee
- C Corporate Compliance and Responsibility Committee
- A Audit Committee
- Committee Chairman

Executive Committee



The Executive Committee is driving a culture of listening within the business to all of our key stakeholders

The Executive Committee regularly joins customers on 'accompanied shopping trips' to get direct feedback on shopping experiences.



At the AGM the Board and Executive Committee invite shareholders to ask any questions they may wish to raise.

The 'Your Say' forums are a way for the Executive Committee to listen to feedback and suggestions from colleagues to improve Morrisons for our colleagues and customers.

**Clare Grainger**  
Group People Director



**Appointment**  
Clare joined Morrisons in February 2009 and was appointed Group People Director on 1 September 2015.

**Experience**  
Clare started her career at Asda and held a number of roles both within Head Office and the Retail division. She progressed through a variety of senior human resources (HR) roles including Head of HR at HBOS/Lloyds Banking Group, where she led a number of programmes to drive differentiation in both sales and services. She joined Morrisons in 2009 holding a number of HR director roles. Most recently, Clare was also Interim Group Retail Director.

**David Potts**  
Chief Executive



See Directors on page 24

**Trevor Strain**  
Chief Financial Officer



See Directors on page 24

**Darren Blackhurst**  
Group Commercial Director



**Appointment**  
Darren joined Morrisons in June 2015 as Group Commercial Director.

**Experience**  
Darren started his career at Tesco in 1988, holding a number of buying positions in fresh food and grocery. In 1994, he was seconded to Tesco's French business Catteau before holding a number of category director positions. Darren became Commercial Director for Tesco Lotus Thailand in 2002. He joined Asda in 2006 as Executive Trading Director for Food and in 2008 was appointed Chief Merchandising Officer. In 2011, he joined Matalan as Chief Executive before moving to B&Q as Commercial Director in 2014.

**Committee membership**



**Gary Mills**  
Group Retail Director



**Appointment**  
Gary joined Morrisons in August 2015 as Group Retail Director.

**Experience**  
Gary has more than 30 years' retail experience, with Stewarts Supermarkets in Northern Ireland and then with Tesco PLC where he held a variety of senior positions including Retail Director for Convenience and Retail Director for the North and Northern Ireland. Gary's experience covers all areas of retail and all formats, including supermarkets and convenience stores.

**Andy Atkinson**  
Group Marketing and Customer Director



**Appointment**  
Andy joined Morrisons in 2011 and was appointed as Group Marketing and Customer Director in January 2016 having held the interim position for over five months.

**Experience**  
Andy previously held a number of senior Commercial and Trading roles within the organisation. Prior to joining Morrisons, Andy held a variety of senior commercial roles within Boots, progressing to Commercial Director. Andy started at Coca-Cola expanding his career with roles at Walt Disney and then L'Oréal.

Corporate governance report continued

# Leadership

## Structure of the Board and its Committees



### PLC Board

#### Members<sup>1,2</sup>

Andrew Higginson, David Potts, Trevor Strain, Rooney Anand, Neil Davidson, Belinda Richards, Paula Vennells

#### Key objective

- Overall conduct of the business and strategy setting.

#### Responsibilities

- Development and approval of the strategy and key policies of the Group;
- Monitoring of progress towards achieving all Board and Group objectives;
- Management of culture and values;
- Monitoring of financial performance, critical operational issues and risks by reviewing performance against strategy, objectives, business plans and budgets;
- Formal approval of the Group's Risk Register;
- Approval of all communications to shareholders, including the Annual Report and Financial Statements, half-yearly financial report and interim management statements;
- Approval of changes to the Group's capital structure, external financial reports, major expenditure; and
- Approval of membership of the Board on recommendation of the Nomination Committee.

<sup>1</sup> All Non-Executive Directors are independent.

<sup>2</sup> Irwin Lee stepped down from the Board on 31 August 2016.

Throughout the year, the majority of the Board consisted of independent Non-Executive Directors.

### Board responsibilities

The formal schedule of matters reserved for the Board remains unaltered from 2015/16 and is set out in the Corporate governance compliance statement which can be found in the investor relations section of the Group's website, [www.morrisonscorporate.com](http://www.morrisonscorporate.com).

The Board is committed to a clear division of responsibilities between the Chairman and the CEO. This has been reviewed by the Board during the year and is also set out in the Corporate governance compliance statement.

### Board Committees

The decisions delegated by the Board to its Committees and the activities of those Committees during the financial year 2016/17 are described within each Committee's report below.

During the year, the Group considered the changes recommended by the 2016 UK Corporate Governance Code (the 'Code') and implemented those changes, as appropriate, throughout the Group.

The Corporate governance compliance statement contains the terms of reference of the Committees and these have been updated during the year to take into account changes in the Code.

## Senior Independent Director

Rooney Anand was appointed as the Senior Independent Director on 1 January 2016 when he joined the Board. Rooney has extensive knowledge of the retail and fast moving consumer goods industries.

The Senior Independent Director provides shareholders with an alternative contact to the Chairman, the CEO and the CFO. The Senior Independent Director also carried out the Chairman's performance review.

## Board activities in 2016/17

The Board's focus in this financial year was:

- setting the strategy;
- review of results and forecasts and approval of regulatory announcements;
- review of the annual business plan and monthly updates from the Executive Committee regarding its delivery;
- the conduct of the business in accordance with its values;
- review of the performance of the CEO;
- approval of the 2017/18 budget and commercial plans, including productivity savings required to invest in the core offer;
- approving the plan for the Group's balance sheet and capital structure strategy;
- approving the Group's continued operations and growth opportunities in online, wholesale and manufacturing; and
- review of the governance structure and activities of the subcommittees of the Board.

## Effectiveness

### Non-Executive Directors

The Non-Executive Directors bring a varied range of skills and experience to the Group. Details of their experience outside the Group are set out in their respective biographies on page 24.

The Board is satisfied that all Non-Executive Directors, including the Non-Executive Chairman, remain independent according to the definition contained in the Code. The criteria used to determine independence are set out in the Corporate governance compliance statement, which can be found in the investor relations section of the Group's website, [www.morrisons-corporate.com](http://www.morrisons-corporate.com).

The minimum time commitment expected of the Non-Executive Directors is 12 days per year, including attendance at the AGM, Board away days and site visits, plus adequate preparation time. The Board is satisfied that each of the Non-Executive Directors commits sufficient time to the business of the Group and contributes to the governance and operations of the Group. This has been confirmed by the Board effectiveness evaluation referred to below.

The Chairman arranges regular discussions between all the Non-Executive Directors (including himself) as a group without management present.

### Board evaluation

The Board arranges for its own performance, and that of its Committees and Directors, to be reviewed annually. This is usually facilitated by an external agency every three years with the most recent external review taking place in 2013/14. As the majority of the Board members were appointed shortly before the start of the financial year 2016/17, it was decided that the Group would conduct an internal Board effectiveness review this year and conduct an external review in the early part of 2017/18.

It was felt that the Group and the Board would receive more value from an external review once members of the Board had had sufficient time to settle into role. An internal review led by the Chairman and the Company Secretary took place in 2016/17.

The evaluation comprised the Company Secretary conducting an interview with each member of the Board individually covering the following key areas:

- overall Board and Committee effectiveness;
- the work of the Board, including the approach to control, risk, strategy and transactions, and the regulatory environment;
- organisation and conduct of Board meetings;
- timing and content of Board papers;
- efficiency of time;
- Board and senior management succession;
- the mix of skills and experience on the Board;
- the amount of time devoted to Board and Committee matters;
- training and awareness; and
- overall Director performance.

Responses were collated by the Company Secretary and discussed with the Chairman and the Board.

The review concluded that the Board operates well and cohesively and that the Chairman fostered an atmosphere of open discussion which encouraged full participation.

The improvements that the Group had made to Board organisation and agendas in the previous year were thought to work well. Papers were well written and received in a timely fashion.

The Board engaged on appropriate topics for discussion with the right balance of information provided. The move to fewer Board meetings but with Board members travelling to the meeting the night before, allowed longer, more intensive Board sessions and the chance to engage more informally with each other, and with the Executive Committee.

## Attendance at meetings

	Board	Nomination	Remuneration	Audit	CCR
Andrew Higginson	8/8	3/3	6/6	–	4/4
David Potts	8/8	–	–	–	4/4
Trevor Strain	8/8	–	–	–	–
Rooney Anand <sup>1</sup>	7/8	2/3	5/6	–	4/4
Neil Davidson	8/8	3/3	6/6	7/7	4/4
Belinda Richards	8/8	3/3	6/6	7/7	4/4
Paula Vennells <sup>2</sup>	8/8	3/3	5/6	6/7	3/4
Irwin Lee <sup>3</sup>	5/5	1/1	4/4	5/5	2/2

<sup>1</sup> Rooney Anand was unable to attend one meeting due to a pre-existing commitment which was known to the Group at the time of his appointment.

<sup>2</sup> Paula Vennells was unable to attend one meeting due to a pre-existing commitment which was known to the Group at the time of her appointment.

<sup>3</sup> Irwin Lee stepped down from the Board on 31 August 2016.

## Corporate governance report continued

Members felt this had been useful in getting to know each other and the senior members of the business, leading to better understanding.

Board members made helpful and insightful suggestions for improvement, particularly on areas of the business they would like more discussion on. These suggestions will be implemented in 2017/18 as part of the Group's ongoing effort to constantly improve its corporate governance.

Executive Directors are included in the Group's performance appraisal process, which includes setting clear and measurable objectives and reviewing performance against those objectives on a bi-annual basis. The Chairman and Non-Executive Directors are responsible for monitoring and reviewing the performance of the Chief Executive, who in turn is responsible for monitoring the performance of the CFO.

During the year, the Group also reviewed and considered its relationship with its principal advisers, and concluded these were effective.

### Membership

The Nomination Committee considers that the Board and Executive Committee contain the skills and experience necessary in light of the Group's current activities and strategic direction.

### Re-election of Directors

All the current Directors submit themselves for re-election at the AGM to be held on 15 June 2017. After reviewing the outcome of performance evaluations, the Board confirms that the contributions made by the Directors offering themselves for re-election at the AGM in June 2017 continue to be effective and that the Board supports their re-election.

### Directors' interests

The interests of the Executive and Non-Executive Directors of the Group, and their immediate families, in the shares of the Group, along with share options, are contained in the Directors' remuneration report set out on pages 33 to 46. At no time during the year did any of the Directors have a material interest in any significant contract with the Group or any of its subsidiaries.

## Executive Committee

### Members<sup>1</sup>

David Potts, Trevor Strain, Andy Atkinson, Darren Blackhurst, Clare Grainger, Gary Mills

### Key objectives

Implementation of strategy and actions in respect of financial planning and performance; day-to-day management of operations.

### Responsibilities

- Development and implementation of strategy.
- Oversight of:
  - financial performance, reporting and control;
  - risk management;
  - operational improvement programmes; and
  - control and supervision of all Group operational activities.
- Making recommendations to the Board in respect of:
  - budgets and long term plans;
  - dividend levels; and
  - ad-hoc events.
- Succession planning for senior management.

<sup>1</sup> Mark Amsden stepped down from the Committee on 15 February 2017.

### Executive Committee activities in 2016/17

The Executive Committee's focus in this financial year was:

- driving trading performance and reviewing financial performance;
- reducing the cost base of the organisation;
- implementing the Group's six priorities;
- overseeing the Group's compliance with its obligations under the Groceries Supply Code of Practice (GSCOP);
- overseeing the Group's commitment to corporate social responsibility in particular in minimising food waste, in supporting the Group's charity partner Sue Ryder and in supporting the charitable Morrisons Foundation;
- overseeing the Group's continued development of its wholesale, online and manufacturing operations;
- approval of capital budgets;
- determining the draft budget and long term plan;
- periodic review of performance against strategic objectives;
- determination of principal risks for the Group;
- approval of the projects with Ocado, Amazon, Duddle, Timpson, Palmer & Harvey and Rontec;
- review of changes to speed up and simplify the business;
- implementation of a new sales-based ordering system; and
- agreeing improvements to the Group's IT infrastructure.

## Audit Committee report

### Members<sup>1</sup>

Belinda Richards (Chair), Neil Davidson, Paula Vennells

### Key objectives

Effective governance of financial reporting, internal controls and risk management systems; review of significant accounting judgements, assumptions and estimates; management of the relationship and appointment of the external auditor; monitoring and review of the effectiveness of the Group's Risk and Internal Audit function.

### Responsibilities

The Board has delegated to the Audit Committee the responsibility for reviewing on its behalf and making recommendations to the Board as to:

- the integrity of financial reports, including reviewing significant financial reporting issues and considering how these issues have been addressed;
- whether the Annual Report is fair, balanced and understandable;
- the effectiveness of the Group's internal control and risk management system;
- the effectiveness of the Risk and Internal Audit function; and
- the independence and appointment of the external auditor, approval of their fees; and monitoring of the Group's policy on non-audit services.

<sup>1</sup> Irwin Lee stepped down from the Committee on 31 August 2016.

### Audit Committee Chair

The Board is satisfied that Belinda Richards has recent and relevant financial experience appropriate to her position as Chair of the Audit Committee. Belinda is considered to have sufficient financial experience, having been a corporate finance partner at Deloitte for over ten years. Additionally, she serves on the Advisory Group of Audit Committee Chairmen at the Financial Reporting Council.

### Audit Committee activities in 2016/17

During the year, the Committee has:

- considered the appropriateness of the Group's Annual Report and Financial Statements and Half-yearly report;
- reviewed the effectiveness of the internal controls and the work of Risk and Internal Audit and discussed key risks (described in more detail on pages 17 to 19);
- reviewed key policies including those governing tax, treasury, expenses and corporate hospitality;
- reviewed the recognition of commercial income and the controls in place over compliance with GSCOP;

- understood the Governance Code and reporting requirements; and
- reviewed the Viability statement.

In respect of financial reports, the Committee's focus was:

- the accounting judgements made by management that could have a significant effect on the Group's financial results;
- the clarity of disclosure of financial information; and
- whether the Annual Report, taken as a whole, is fair, balanced and understandable – the Directors' statement on this can be found on page 49 of this Annual Report.

### Financial reporting matters

The Audit Committee has considered whether suitable accounting policies have been applied and has reviewed key accounting judgements and estimates made by management during the year. The key judgements and financial reporting matters considered by the Committee are outlined in this section.

#### Impairment of property, plant and equipment, intangible assets and onerous property contracts

Impairment and onerous property contracts continue to be a focus area for the Committee. The Group's policy to assess impairment on an annual basis, or where changes in circumstances indicate impairment (or impairment reversal), is disclosed in note 3.1 of the financial statements. The impairment review is comprehensive, covering non-financial assets, principally the Group's property portfolio, IT assets and goodwill.

The Group's trading performance and evidence of the market value for properties and sites are considered by the Group as part of the annual impairment review. Management estimates the recoverable amount of assets to determine the extent of any impairment charge or whether a reversal of a previous impairment charge is applicable. This assessment resulted in a reversal of previous impairment on certain cash generating units and an impairment charge being recognised on others, as disclosed in note 3.3 of the financial statements.

The Committee reviewed the Group's assessment of recoverable value and reassessed the key assumptions and judgements made in the light of current market conditions and trading performance. The Committee also considered how management had assessed the potential impact of the uncertain economic conditions and the impact of an exit from the EU in the impairment review. The Committee has reviewed management's key assumptions including the market valuation of the store portfolio. It has also understood the methodology and approach to forecast

store cash flows, which remains consistent with the prior year.

In addition, property contracts where the expected future cash flows are less than the future contract commitments, an onerous contract provision should be recognised. The Committee reviewed the key judgements and understood the reasons for year-on-year movements.

The Committee reviewed the sensitivity of key assumptions along with their impact on the impairment and onerous contract provisions and is satisfied the assumptions applied by management are appropriate.

#### Commercial income

Commercial income is a deduction from the cost of purchase, and it is recognised in accordance with signed supplier agreements, with most income subject to little or no subjectivity or judgement.

The Group's definition of commercial income is disclosed in note 1.1 of the financial statements and is consistent with the definition in the prior year.

Commercial income continues to be an area of focus for the Committee. During the year, the Committee has considered the policies applied with regard to commercial income, the key judgements, the level of income recognised and the financial statement disclosure. The Committee has been updated on the Group's initiative to simplify trading arrangements and understood the impact this has had on commercial income during the year.

In considering the appropriateness of commercial income recognised in the year and the financial position at the year end, the Committee has reviewed reports from management and Internal Audit outlining the accounting judgements and the control environment. The Committee understood the key judgements in this area and considers them to be appropriate.

The Group continues to seek to provide transparency of disclosure surrounding commercial income. The Committee also reviewed the key messages from the FRC lab case study highlighting the good practice in the Group's approach to commercial income disclosure. The Committee remains supportive of the level of disclosure made in this area.

#### Stock

Stock is a material balance in the Group's financial statements, with stock held across a large number of locations. Stock count procedures have remained consistent with the prior year.

Judgement is required in determining provisions for shrinkage and valuation and the Committee reviews these judgements as part of the annual accounting policy review.

The Committee has reviewed the level of stock provision and key assumptions underpinning the provisions and considers these to be appropriate.

#### Pensions

The Group operates a number of defined benefit pension schemes. Accounting for defined benefit pension schemes requires the application of a number of assumptions which have an impact on the valuation of the schemes' assets and liabilities. The IAS 19 valuations are performed by an independent actuary.

The Committee has reviewed the assumptions used in the schemes' valuations. The Committee has considered the appropriateness and sensitivity of the assumptions used by the independent actuaries in the valuation. The Committee has concluded that the assumptions are appropriate.

The Committee reviewed the legal advice the Group has obtained with regard to the recognition of a pension surplus for the Group's defined benefit pension schemes and considered the treatment appropriate.

The Committee reviewed management's assessment of the accounting treatment resulting from the set-up of the new defined contribution scheme and agreed with Management's treatment.

The Committee also instigated an update at the Board regarding the outcomes of the triennial valuation as part of understanding the Group's pension position.

#### Internal control and risk management

The Board has overall accountability for ensuring that risk is effectively managed across the Group. Risks are reviewed by the Executive Committee for all functions twice annually and results are brought to the Board. On behalf of the Board, the Audit Committee has responsibility for reviewing the effectiveness of internal control including financial, operational and compliance controls.

The Group's principal risks are set out on pages 17 to 19.

In order to do this, as a matter of course in any one year, the Committee:

- receives and agrees appropriate actions in response to regular reports from the Risk and Internal Audit function on:
  - the status of internal control and risk management systems across the Group;
  - the department's findings, annual plan and the resources available to it to perform its work; and
  - any concerns expressed by colleagues about possible malpractice or wrongdoing;

## Corporate governance report continued

- reviews financial whistle-blowing reports from colleagues;
- reviews the external auditor's management letter on internal financial control;
- seeks reports from senior management on the effectiveness of the management of key risk areas; and
- monitors the adequacy and timeliness of management's response to identified audit issues.

These systems and processes have been in place throughout the period and up to the date of approval of this Annual Report.

The main features of the Group's internal control and risk management systems relating to the accuracy and reliability of financial reporting, including the process for preparing consolidated accounts, are:

- recruitment of suitably qualified and experienced finance colleagues;
- segregation of duties, clear lines of accountability and delegation of authority;
- policies and procedures that cover financial planning and reporting, preparation of financial information, and capital expenditure;
- a robust period end review process including review and commentary from process owners;
- a tiered review process for external financial reports involving internal stakeholders from relevant areas of the business;
- information and data security policies and procedures; and
- self certification by each section of the business.

The Committee regularly reviews the Group's process for risk management and internal control and annually conducts a formal review of these processes. No significant failings or weaknesses of internal control were identified during these reviews. Limited weaknesses and areas where controls could be further automated were identified. Clear action plans are in place to address these weaknesses and are captured as part of functional risk registers with defined management responsibility. The Committee understands the importance of a robust risk management process and control environment and looks to progressively strengthen it over time.

### Viability statement

The Group's business model and strategy, as outlined on pages 8 and 9, are central to an understanding of its future viability. The Group continues to progress against the current turnaround strategy, focusing on strengthening the core supermarkets and delivering capital light growth whilst maintaining discipline and control in relation to costs and upholding a strong balance sheet.

The Directors have assessed the viability of the Group over a three year period to January 2020. The Group's business model is not dependent on any particular contract or resource with fixed end dates; the period was selected because the Group's forecasts associated with the detailed strategic and financial plans are prepared over this period and were considered to be the most robust and appropriate means to support its Viability statement.

The Board assesses the Group's prospects primarily through the strategic planning process. The latest strategic planning update with the Board was held in November 2016 with involvement of all relevant functions across the business.

As part of the strategic planning process, the Directors make a number of assumptions about business performance and the ability of the Group to raise debt financing. The Group carefully plans and reviews the maturity profile of debt facilities to avoid coterminous maturity dates, and liquidity forecasting gives visibility of headroom under committed facilities over the period of the financial plans.

Key metrics in the plan, such as cash flow, interest cover, liquidity and the ability to raise debt financing, were subject to sensitivity testing by flexing a number of the main financial assumptions in order to assess the impact of principal risks in severe but plausible scenarios.

All principal risks were considered as part of the testing but particular focus was given to:

- business interruption;
- competitiveness;
- customer;
- data; and
- financial and treasury.

Scenarios tested included measuring the impact of a downturn in sales, an increase in costs, or a business interruption event. Furthermore, reverse stress testing was performed to understand the level of performance decline that the Group could withstand.

Based on this assessment, and taking into account the Group's current position, the Directors have a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over the three year period of their assessment.

### Effectiveness and independence of the external auditor

The Committee considered the effectiveness of PricewaterhouseCoopers LLP (PwC) as auditor during the year. In making this assessment the Committee considered the output of an effectiveness survey completed by the Directors and management, the information presented by the auditors, management responses to the auditor's findings, including any adjustments, and the level of non-audit fees.

The Committee holds meetings with the auditor without management present. The purpose of these meetings is to understand the auditor's views on the control and governance environment and management's effectiveness within it. To fulfil its responsibilities in respect of the independence and effectiveness of the external auditor, the Committee reviewed:

- the terms, areas of responsibility, duties and scope of work of the external auditor as set out in the engagement letter;
- the audit work plan for the Group;
- the detailed findings of the audit, including a discussion of any major issues that arose during the audit;
- the letter from the external auditor confirming its independence and objectivity; and
- the audit fee and the extent of non-audit services provided during 2016/17.

The policy on the engagement of the external auditor to supply non-audit services is set out in the investor relations section of the Group's website (see [www.morrison-corporate.com](http://www.morrison-corporate.com)).

PwC has continued to provide certain non-audit services throughout the year. In the year the non-audit services work provided by PwC was in line with the policy and the ratio of audit to non-audit services was within the 1:0.7 limit set in the policy.

The Committee is satisfied that this non-audit activity carried out by the statutory auditors is subject to safeguards to avoid a threat to the auditor's independence or objectivity. These safeguards include separate teams for audit versus non-audit work.

### External audit tender

As noted in last year's Annual Report, the Board appointed PwC as external auditor in June 2014. The Group confirms that it has complied with the provisions of the Competition and Markets Authority's Order in respect of The Statutory Audit Services for Large Companies Market Investigation (Mandatory Use of Competitive Tender Processes and Audit Committee Responsibilities) Order 2014 – statement of compliance.



## Corporate Compliance and Responsibility (CCR) Committee

### Members<sup>1</sup>

Neil Davidson (Chair), Andrew Higginson, David Potts, Rooney Anand, Belinda Richards, Paula Vennells, Darren Blackhurst, Andrew Clappen<sup>2</sup>

### Key objectives

Development and implementation of the Group's policies on corporate compliance and corporate responsibility. Reviewing and ensuring compliance with these policies and ethical and governance standards.

### Responsibilities

Oversight that the business is doing the right thing in areas of corporate responsibility, including:

- GSCOP;
- food safety and food integrity;
- health and safety;
- gender pay gap;
- cyber security;
- ethical trading;
- modern slavery;
- environmental and competition compliance;
- data protection;
- governance and reputation; and
- the Morrisons Foundation.

Generally ensuring that the Group is acting as a good corporate citizen.

<sup>1</sup> Irwin Lee stepped down from the Committee on 31 August 2016. Mark Amsden stepped down from the Committee on 15 February 2017.

<sup>2</sup> Andrew Clappen is the Group Corporate Services Director. Andrew joined Morrisons in 2012 and is responsible for the Corporate Affairs and Policy, CSR & Ethical Trading, Agriculture and Technical Services (Food and General Merchandise Technology, Safety, Quality, Compliance and Health & Safety) of the Group. Prior to Morrisons, Andrew was the Senior Vice President responsible for Food Safety, Quality Assurance & Regulatory Affairs at Loblaw Companies Ltd in Canada.

### CCR Committee's activities in 2016/17

The Committee's focus in this financial year was a review of:

- GSCOP compliance including training and results of internal reviews;
- cyber and IT security risk;
- health and safety incidents and actions taken and progress of health and safety initiatives;
- energy strategy and carbon reduction measures;
- ethical trading;
- redistribution of food waste;
- food safety and improvements;
- food integrity and testing; and
- non-financial whistle-blowing reports.

### Remuneration Committee report

The report from the Remuneration Committee is contained in the Directors' remuneration report on pages 33 to 46.

## Nomination Committee report

### Members<sup>1</sup>

Andrew Higginson (Chair), Rooney Anand, Neil Davidson, Belinda Richards, Paula Vennells

### Key objectives

Advice to the Board on Board and senior management appointments and succession planning; monitoring of the composition of the Board and its Committees.

### Responsibilities

- Evaluating the current and required mixture of skills and experience on the Board;
- Sourcing and selecting candidates;
- General oversight of people and capability within the business;
- Oversight and understanding of the Group's leadership and succession plans; and
- Oversight of the Group's plans on diversity and inclusion.

<sup>1</sup> Irwin Lee stepped down from the Committee on 31 August 2016.

### Nomination Committee's activities in 2016/17

#### Selection process

The Nomination Committee is responsible for succession planning and the recommendation of Director appointments to the Board. The Committee considers the size and composition of the Board on an ongoing basis.

The Committee will consider the skills of outgoing and remaining Board members to assess any gaps and develop a candidate profile. The Board uses external search consultancies to source suitable candidates. The Committee recommends appointments on merit against the criteria applied in developing the candidate profile and taking into account the mix of skills, experience and diversity on the Board.

#### Diversity

The Committee recognises the benefits of a diverse colleague base across the Group and is supportive of initiatives with the business to improve diversity at all levels.

The Group wishes to increase female representation in the Leadership team to at least 30%. This target has not yet been achieved. The Leadership team currently has 18% female representation and the Committee recognises that more work is needed in this area. Recruitment and promotion policies have been reviewed with a view to

#### Gender diversity

	Female representation	Female representation %	Male representation	Male representation %	Total
Board	2	29%	5	71%	7
Senior management	14	18%	65	82%	79
<b>Total</b>	<b>16</b>	<b>19%</b>	<b>70</b>	<b>81%</b>	<b>86</b>

attracting candidates with a wide range of backgrounds and experience, ensuring that the best individual for the role is appointed. Specific targets have not been set as it is considered that they may drive the wrong behaviours. However, guidelines are in place to ensure that the long list for any particular vacancy at management level includes a balanced profile of candidates.

Particular focus continued throughout the year on increasing female representation in the Retail team. Six of the 20 most senior retail field team are now female, up from two just over a year ago, an increase from 9% to 30%. An additional ten female store managers were appointed during the year, meaning that 10% of our store managers are now female.

Progress on the diversity agenda is measured through regular functional talent reviews. These reviews consider the ethnicity, gender, age and length of service of all colleagues at Morrisons.

At the end of the 2016/17 financial year the Board included two women members, 29% of its total composition. The Board's policy is that female representation should be maintained at not less than 20% and aspires that this should be higher than 30%. This policy will continue to be considered as part of the Committee's regular review of the Board's composition and skills.

#### Stability and diversity

Following the decision for the UK to leave the EU, the Committee and Board have worked hard to reassure, engage and support our colleagues from the EU. The Committee and Board are confident that our multi-cultural sites and stores will offer all our colleagues the same commitments of respect, opportunity, training and fair pay. The Group has improved our ways of working to make our business accessible for our EU colleagues through better English language training, translation support, simplified processes and more opportunities to progress.

#### Other areas of focus

The Committee also spent time reviewing succession planning for both the Board and Executive Committee as well as of the talent pool for levels below Executive Committee.

## Corporate governance report continued

### The Groceries Supply Code of Practice (GSCOP)

GSCOP applies to designated grocery retailers in the UK with an annual turnover in excess of £1bn. This code of practice adds specific regulations into the trading relationships between the designated grocery retailers and their suppliers.

We actively engage with the relevant regulatory bodies, the Office of the Groceries Code Adjudicator (GCA) and the Competition and Markets Authority (CMA), to build best practice in relation to the Code. We have regular meetings with the GCA and provide updates on our activity and details on specific areas of interest for the Adjudicator.

In June 2016 the GCA published a case study providing clarification on activity Morrisons had undertaken in July 2015. The GCA determined that Morrisons had breached paragraph 3 of GSCOP, Variation of Supply Agreements by indirectly requiring suppliers to pay lump sums that were not provided for in the relevant supply agreement. The GCA acknowledged that we had responded immediately when alerted to the issue, had conducted an extensive internal investigation and no further action was required to be taken.

In response to the GCA's case study, and supplier and buyer feedback, we enhanced and extended our training programme for all supplier-facing colleagues. This training covered all colleagues in the Trading teams together with bespoke training for colleagues in our Supply Chain and Finance teams who work closely with the Trading function. Over 1,000 colleagues have been through the programme.

In addition, we strengthened our overarching governance in this area with the establishment of a governance group comprising of senior leadership team members across the Trading, Supply Chain, Finance, Legal and Compliance functions. This group undertook a detailed review of current activity and compliance with the GCA's sector-wide priority areas and supplier relationship development. Routine reports and updates are provided to our Executive Committee and CCR Committee, on activity and all relevant aspects of GSCOP including developments about its operation or regulation. We formally report details of activity over the year and specific complaints made by the suppliers to our Code Compliance Officer (CCO), and to the GCA and the CMA at the financial year end.

Enquiries from suppliers on GSCOP related matters are dealt with in accordance with the regulations. Any matter not resolved directly with a buyer is escalated to the relevant Category Director and, if requested, to our appointed CCO. During 2016/17 we successfully worked with suppliers to resolve any GSCOP complaints through the commercial escalation process or with the intervention of our CCO.

Contact details and further information can be found at [www.morrisons.co.uk/gscop](http://www.morrisons.co.uk/gscop).

### Relations with shareholders

The Board is committed to communicating the strategy to analysts, investors and shareholders on a regular basis through a planned programme.

The Investor Relations programme includes:

- formal presentations of full and half year results;
- interim management statements;
- regular meetings between institutional investors, the CEO, the CFO and the Investor Relations team in the UK and overseas following the full and half year results;
- regular meetings between the Chairman and major shareholders to discuss any aspect of the Group or its governance arrangements;
- attending key investor conferences;
- communication between the Chairman of the Remuneration Committee and major shareholders on remuneration policy and significant changes in remuneration arrangements;
- responding to enquiries from shareholders and analysts through the Investor Relations team; and
- dedicated shareholder and investor sections on the corporate website.

In addition, the Investor Relations team provides a regular update to the Board and feedback from meetings held between executive management and institutional shareholders. The Group's brokers seek independent feedback from analysts and investors following the full and half year results meetings which is reported to the Board.

### Matters dealt with elsewhere in the Strategic report or Directors' report

The way the Group generates value and the Board's strategy for delivering the Group's objectives are described in our business model on pages 8 and 9, and in our six priorities section on pages 6 and 7. The information regarding the Takeover Directive disclosures are on page 48. The consideration of going concern is described on page 47.

### Annual General Meeting (AGM)

All Executive Directors and Non-Executive Directors attend the AGM unless unable to do so due to circumstances outside of their control.

Notice of the 2017 AGM of the Group is to be sent to shareholders with an accompanying letter from the Chair. The AGM will be held at the Group's headquarters at Gain Lane in Bradford on 15 June 2017. Format of the meeting:

- a summary presentation of results is provided before the Chairman deals with the formal business;
- all shareholders present can question the Chairman, Chairmen of the Committees and the Board during the meeting and informally afterwards;
- the Board encourages participation of individual investors at the AGM; and
- following the meeting, details of the voting on the resolutions will be made available on the website at [www.morrisons-corporate.com/Investor-centre/generalmeetings/](http://www.morrisons-corporate.com/Investor-centre/generalmeetings/).

The Directors recommend shareholders vote in favour of each resolution, believing them to be in the best interests of the Group. Shareholders will be notified of the availability of the Annual Report and Financial Statements on the website unless they have elected to receive a printed version.

Directors' remuneration report

# How our Directors are rewarded

Annual statement by the Senior Independent Director, on behalf of the Remuneration Committee

Rooney Anand  
Senior Independent Director



The first full year of delivering a sustainable turnaround, against the backdrop of a very competitive market

### Dear Shareholder

On behalf of the Remuneration Committee and the Board, I am pleased to present the Directors' remuneration report for the financial year 2016/17.

### Business context – performance for 2016/17

The Committee is pleased with the progress made in the first full year of the Fix phase of the turnaround. David and the team have been able to improve the business faster than expected by listening to customers and colleagues, and responding to their feedback, to improve the shopping experience. The business has also continued its strong capital discipline, continuing to improve free cash flow and strengthen the balance sheet.

In a highly competitive market, like-for-like (LFL) sales have grown and more customers are choosing to shop with us. We have reduced prices for customers without compromising on quality, as shown by us winning a number of prestigious awards, including Meat & Fish Retailer of the Year and International Wine Challenge Supermarket of the Year for the second year running.

We have also started to realise the profit opportunity from the business which will power the Rebuild and Grow phases of the turnaround – wholesale, online, popular and useful services. We continue to explore capital light growth opportunities.

### Key financial highlights

- Underlying profit before tax (UPBT) for 2016/17 of £337m (an increase of 11.6% on 2015/16 before restructuring costs).
- LFL sales growth (excluding fuel) of 1.7%.
- Exceeded £2bn three-year free cash flow target six months early and have continued to reduce net debt.

### New remuneration policy – summary

- No material change to the remuneration policy
- Increase to shareholding requirement
- Change of level of normal LTIP grant to reflect turnaround opportunity

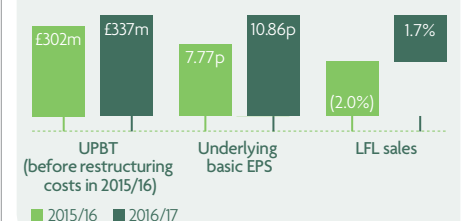
In addition, we are pleased with the progress we are making across the business for all colleagues to share in the success of the business going forward:

- In 2016/17, we paid the highest hourly rate for store colleagues of the big four grocers.
- In 2016/17 we made a significant investment in-store colleagues' hourly pay and paid a bonus to colleagues equivalent to around 9% of UPBT.
- Performance based Long Term Incentive Plans (LTIPs) have been rolled out to store manager level and above across the business.

The new remuneration policy presented later in the report reflects feedback from shareholders and the policy changes aim to increasingly link Director and shareholder experience.

### Key Measures

#### Business performance



## Directors' remuneration report continued

### Incentive out-turns for 2016/17

#### Annual bonus

The bonus for 2016/17 was based 50% on UPBT, 30% on a strategic scorecard of measures and 20% on personal objectives.

- UPBT of £337m resulted in 100% of this part of the bonus paying out.
- LFL sales growth of 1.7%, and relevant cost/productivity savings of £269m were achieved in 2016/17. Both elements of the strategic scorecard measure achieved 100% against their respective targets, resulting in 100% achievement against the strategic scorecard measure.

The result of the above measures combined with achievement against personal objectives resulted in bonus payouts of 100% of maximum for both the CEO and CFO.

#### LTIP

The LTIP award granted in June 2014 and vesting in June 2017 was based 50% on cumulative free cash flow, 30% on underlying EPS and 20% on total sales (excluding fuel and VAT) for 2016/17.

- Cumulative free cash flow of over £2bn over the period resulted in 100% of this part of the LTIP vesting.
- The underlying EPS growth and total sales targets were not met and therefore none of this part of the award will vest.

The LTIP will vest at 50% of the maximum.

### Key actions during 2016/17

#### Shareholder engagement

During the year, the Committee engaged with our largest investors to obtain their views on our current remuneration policy and the proposed changes in the new policy.

Key feedback included:

- support for the principle of higher reward for stretching targets;
- continued support for free cash flow measure, but at lower weighting; and
- support for a long term incentive plan that locked in the management team and incentivised turning around the business and delivering further growth.

We considered and incorporated the views of our investors in the development of our new policy as follows:

- stretching performance targets which reflect the financial objectives of the business over the next three to four years and reward achievement of those objectives in a way that is 'self funding';
- increasing the shareholding requirement to drive alignment within the investor experience; and
- continued focus on cash but at lower weighting than previously.

#### New remuneration policy

We intend to present our new remuneration policy for shareholder approval at the June 2017 AGM.

- No changes to policy on pay, annual bonus, benefits or pensions.
- Individual LTIP awards rising to 300% (in line with current policy), with associated stretching targets.
- Increase in shareholding requirement to 250% which represents a sector leading requirement.

A detailed summary of the new remuneration policy is set out on pages 37 to 40.

#### Implementation in 2017/18

- No change to policy on base pay, benefits, pensions or annual bonus; and
- David Potts has again waived the pay rise offered by the Committee.

### 2017-2020 LTIP

The material change to the operation of the policy is the LTIP award.

The plan has been designed with the following two goals in mind:

#### Goal 1

Flexibility to motivate and reward achievement of the business turnaround

#### Current LTIP

Performance targets driving market typical levels of growth

#### New LTIP

Stretching performance targets driving further growth

Increased normal grant levels and associated stretching targets to drive performance (self funding)

#### Goal 2

Greater alignment with investors

#### Current LTIP

Financial targets

Three year performance period

#### New LTIP

Increased shareholding requirement

#### Structure of the full Directors' Remuneration Report

- **At a glance** – Overview of performance and comparison of 2014 and 2017 policies.
- **Remuneration policy** – New remuneration policy. Subject to binding shareholder vote at the 2017 AGM in June.
- **Annual report on remuneration** – Implementation of remuneration policy during 2016/17 and proposed implementation of the new policy in 2017/18. Subject to shareholder vote at the 2017 AGM in June.

#### Rooney Anand

Senior Independent Director

The Group is required to prepare a Directors' remuneration report for the 52 weeks ended 29 January 2017. The report has been prepared in accordance with the Companies Act 2006 and the Large and Medium-sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013.

# At a glance – how we have performed

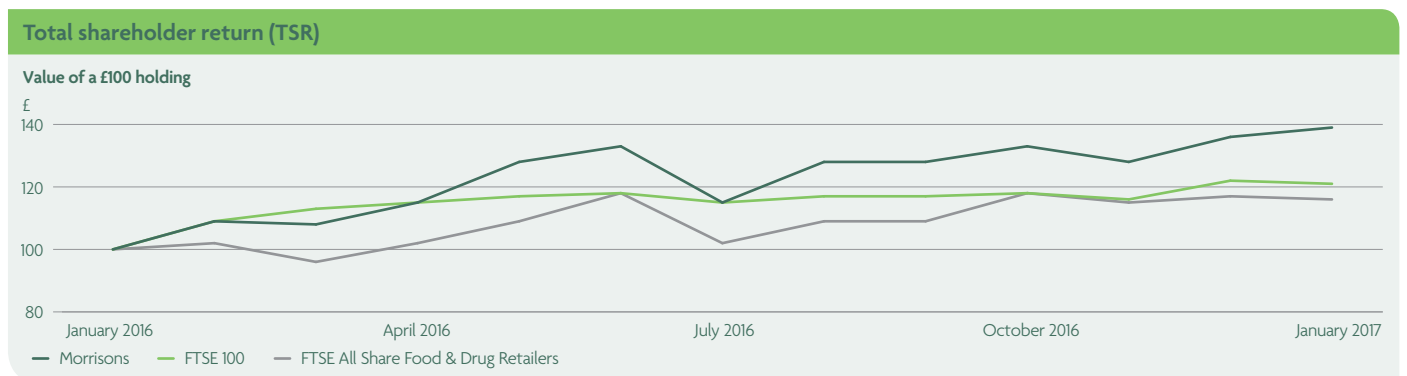
*Rewarding a year of strong financial performance and achievement of our customer measures*

## Key business performance indicators

Measure <sup>1</sup>	2016/17	2015/16
UPBT (before restructuring costs in 2015/16)	£337m	£302m
Underlying basic EPS	10.86p	7.77p
LFL sales (%)	1.7%	(2.0%)
Cumulative free cash flow (2014/15 onwards)	£2,304m	£1,639m

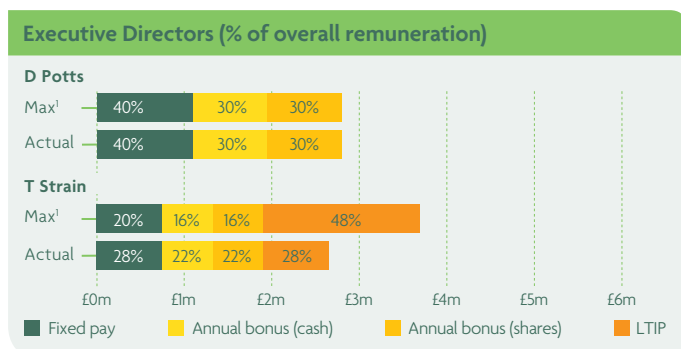
<sup>1</sup> For definitions of these measures, see the Glossary on page 122.

## Key shareholder performance indicators



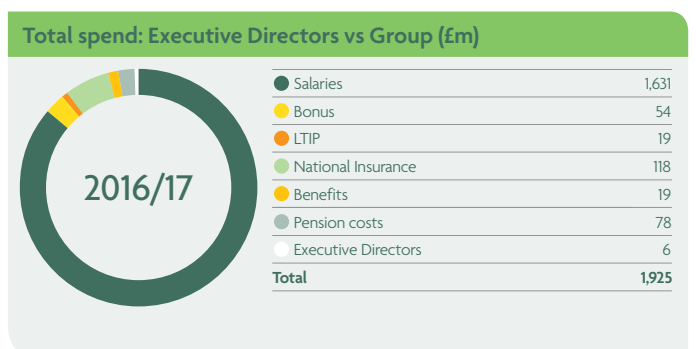
The graph above shows the Group's total shareholder return (TSR) compared with the TSR of the FTSE 100 and FTSE All Share Food & Drug Retailers indices over the 12 month period to 29 January 2017.

## How we have been rewarded in 2016/17



The above shows the proportion of the Executive Directors' remuneration in 2017 that was at risk in the form of annual bonus and LTIP arrangements, meaning 77% of their remuneration was linked to the achievement of short and long term objectives.

<sup>1</sup> Reflects the maximum that the individual could earn under the current policy. D Potts first LTIP award was 2015-2018, therefore he had no LTIP vesting in 2016/17.



The Group's total spend on colleague reward is illustrated in the above chart. This indicates that the spend on Executive Director pay is a small proportion of the total investment in overall remuneration, and that our colleagues are rewarded for their contribution to the Group's success.

Directors' remuneration report continued

# Changes to our Directors' remuneration policy

We are evolving our policy to support our six priorities

## Consideration of shareholder views and policy review process

### Consideration of shareholder views

As well as normal ongoing dialogue with shareholders, the Group has undertaken a series of consultative meetings to shape the development of the new policy, as well as meeting with institutional investor representative bodies. The design of the LTIP was amended specifically in response to shareholder feedback.

How we went about the policy review:

- Met with our major shareholders to discuss views on remuneration in the context of Morrisons
- Reviewed our current policy against our strategic priorities and identified areas of misalignment
- Developed alternative proposals for consideration before identifying a preferred approach
- Presented detailed proposals to our major shareholders with further meetings to discuss rationale
- Proposal further refined following shareholder feedback
- Remuneration Committee approve changes and present to shareholders for approval

## Summary of policy changes

### The principles underpinning our policy

<b>1</b> Doing what is right for the business for the long term	<b>2</b> Ensuring lock-in of Directors as we start to deliver Fix, Rebuild and Grow	<b>3</b> Continuing to deliver sector superior returns to shareholders	<b>4</b> Providing clear alignment between Directors and shareholders over the policy period and beyond	<b>5</b> Maintaining pay fairness in what is a talent competitive industry
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### Summary of policy changes

	PAY ELEMENT	POLICY GOALS	HOW POLICY IS EVOLVING TO FURTHER SUPPORT OUR STRATEGY <sup>1</sup>
<b>Fixed</b>	<b>Base salary</b>	<ul style="list-style-type: none"> <li>• Ability to recruit and retain our top talent</li> </ul>	<ul style="list-style-type: none"> <li>• Maintain policy of providing market competitive base pay, benefit and retirement provisions</li> <li>• Maintain limit on increases in base salary for Directors to those of the wider workforce<sup>2</sup></li> </ul>
	<b>Benefits</b>	<ul style="list-style-type: none"> <li>• Provide market competitive levels of fixed pay in a competitive industry</li> </ul>	
	<b>Pension</b>	<ul style="list-style-type: none"> <li>• Provide for a sense of fairness amongst wider colleagues</li> </ul>	
<b>Variable</b>	<b>Annual bonus</b>	<ul style="list-style-type: none"> <li>• A focus on doing what is right for the business over the long term</li> <li>• Clear alignment between Director and investor interests</li> <li>• A strong and rigorous performance culture</li> </ul>	<ul style="list-style-type: none"> <li>• Maintain incentive focus on key business metrics of UPBT, LFL sales, free cash flow and EPS</li> <li>• Maintain current annual bonus framework to include a 50% deferral into shares for three years<sup>3</sup></li> <li>• Increase in share ownership guidelines to 250% – a sector leading requirement</li> </ul>
	<b>LTIP</b>	<ul style="list-style-type: none"> <li>• A remuneration package weighted towards performance-related pay</li> <li>• Transparency in targets set and performance measurement</li> </ul>	

<sup>1</sup> Full policy is set out on pages 37 to 40. <sup>2</sup> Policy will permit increases of a higher amount in exceptional circumstances such as change in role or promotion. <sup>3</sup> The Committee have the discretion to adjust the clawback and malus periods as they deem appropriate. <sup>4</sup> Although outgoing policy already permits LTIP awards of this amount, the intention is for normal award limits to be increased to 300% from 240% subject to achievement of 'stretching' targets.

**The Committee is committed to ongoing dialogue and consultation with shareholders and their representative bodies.**

**Policy change rationale**  
 In reviewing our policy, we have reflected the shareholder feedback from consultation,

alongside the principle of working with the existing policy. The outcome of this review resulted in two changes:

**Normal LTIP grant levels**  
 The normal LTIP grant levels have been increased in response to the feedback that

shareholders liked the principle of the potential for higher reward, if linked to stretching targets.

**Weightings of performance levels**  
 Investors also told us they particularly liked our focus on cash and wanted to see this retained as a measure, albeit at lower weighting.

# Our new Directors' remuneration policy

*A remuneration policy that will drive long term sustainable value creation for shareholders*

As outlined on page 34, the Directors' remuneration policy will be subject to a vote at the 2017 AGM. If approved, the changes will take effect following the AGM. The current policy, as approved at the 2014 AGM, can be found at [www.morrisons-corporate.com](http://www.morrisons-corporate.com). In designing and setting the policy on Directors' remuneration, the Committee has considered the reward structure, market levels of pay and general pay increases throughout the Group.

### Pay and conditions in the wider Group

The new policy covers a period of turnaround for the Group, and consequently we are seeking to attract, motivate and retain the best talent at all levels of the market. For store colleagues, during 2016/17 we paid the highest hourly rate of the big four grocers. We have also introduced a performance-related colleague bonus scheme which for 2016/17 performance will pay out nearly double what the previous 'profit share' arrangement used to.

Although colleagues are not formally consulted on Directors' remuneration policy, colleagues views on pay form part of our Engagement Survey and colleague 'Your Say' forums. The results of the survey are communicated to the Board, and Executive Directors attend the national 'Your Say' forum.

The only changes are to the LTIP (as outlined on page 34). The policy is summarised below:

### Remuneration policy table – new policy 2017

#### Executive Directors

ELEMENT AND HOW IT SUPPORTS STRATEGY	OPERATION	OPPORTUNITY	PERFORMANCE MEASURES AND PERIOD
<p><b>Base salary</b></p> <p>The Committee's policy is to set base salaries competitively to attract and retain the best talent, which is critical to the Group's success and delivery of the strategy.</p> <p>Base salary is part of a total remuneration package which rewards stretching performance aligned to the Group's strategy.</p>	<p>Base salaries are set by the Committee on appointment and then normally reviewed annually.</p> <p>In setting and reviewing salary levels, the Committee considers the responsibilities of the role, progression in the role, individual performance (including any change in responsibilities), skills, experience, and pay levels and structure throughout the Group.</p> <p>The Committee also has regard to rates for similar roles in comparator companies, both in FTSE 100 retailers and UK-based companies of a similar size and complexity, but seeks to avoid the automatic ratcheting effects of following benchmark levels of salary.</p>	<p>Salary increases will ordinarily be in line with salary increases across the Group. The Committee may award increases above this level where this is warranted due to a change in the scope or responsibilities of the role, to reflect progression in the role (e.g. staged increases for a recent appointment) or to remain competitive in the market.</p> <p>Current base salary levels are disclosed on page 42.</p>	<p>Not applicable.</p>
<p><b>Benefits</b></p> <p>The Group provides a market competitive benefits package for Executive Directors to support in the ability to recruit and retain the best talent.</p>	<p>Executive Directors are entitled to a car allowance (or other car benefit), transport costs, private health provision, life assurance and normal colleague discount entitlement. Executive Directors are also entitled to participate in the all colleague Share save schemes (and any other all colleague share plan which the Group may operate) on the same terms as all other UK-based colleagues. The Committee reviews benefit provision from time-to-time and retains flexibility to add or remove benefits if necessary to ensure that benefit provision remains market competitive or to meet the operational needs of the business (for example, through the payment of relocation expenses).</p>	<p>The maximum car allowance is currently £24,000. The cost to the Group of providing other benefits depends on the nature of the benefit and can vary from year-to-year. Benefit provision will be maintained at a level which is competitive.</p>	<p>Not applicable.</p>

## Directors' remuneration report continued

ELEMENT AND HOW IT SUPPORTS STRATEGY	OPERATION	OPPORTUNITY	PERFORMANCE MEASURES AND PERIOD
<p><b>Pension benefits</b></p> <p>The Group provides a market competitive retirement provision for Executive Directors which is aligned with retirement benefits available throughout the Group.</p>	<p>Executive Directors are entitled to membership of the Group's cash balance pension arrangement known as the Morrisons Retirement Saver Plan. Individuals contribute 5% of capped base salary and all new eligible colleagues are automatically enrolled into this arrangement. A 10% cash salary supplement in lieu of Group pension contributions applies on base salary above the capped amount.</p> <p>A cash alternative to pension provision is provided where the Group's standard pension provision is not appropriate, for example, where an Executive Director has reached the Lifetime Allowance. Executive Directors may elect to receive this cash salary supplement in lieu of pension of broadly the same value as would accrue on an annual basis in the pension plan.</p>	<p>The Morrisons Retirement Saver Plan guarantees a value of the cash balance in the plan of 24% of pensionable pay (assuming retirement at age 65 years) adjusted for inflation capped at 2% p.a.</p> <p>A maximum 10% cash salary supplement applies above capped base salary.</p> <p>Where an Executive Director receives a cash salary supplement only, the maximum supplement payable is 25% of salary.</p>	<p>Not applicable.</p>
<p><b>Annual bonus</b></p> <p>Annual bonus awards are designed to incentivise and reward achievement of the Group's short term financial and strategic objectives and personal performance objectives.</p> <p>Compulsory deferral is designed to encourage retention and further align the interests of the Executive Directors with shareholders.</p>	<p>Bonus awards are made annually subject to a mix of financial and non-financial performance measures. Achievement of each performance element is assessed independently and the level of payout is determined by the Committee after the end of the relevant financial year.</p> <p>50% of any bonus payable is paid in cash with the other 50% deferred in shares under the deferred share bonus plan (DSBP), normally for a period of three years. The Committee has discretion to allow a higher level of deferral.</p> <p>Dividend equivalents accrue over the vesting period and are paid at the time of vesting on the number of shares that vest.</p>	<p>The maximum bonus potential for Executive Directors is 200% of base salary.</p> <p>The number of shares subject to the deferred award is determined by reference to the bonus and the share price on the date of award.</p>	<p>Annual bonus awards are subject to the following performance measures:</p> <ul style="list-style-type: none"> <li>• 50% is based on underlying profit before tax performance;</li> <li>• 30% is linked to achievement of a number of strategic scorecard measures; and</li> <li>• 20% is linked to achievement of personal objectives.</li> </ul> <p>The measures and weightings are set by the Committee on an annual basis, and may be changed if the Committee decides this is appropriate to support delivery of the Group's strategy. Each element is assessed independently at the end of each year. Achievement of threshold performance will result in a payout of 20% of the underlying profit element (i.e. 10% of the maximum bonus potential).</p> <p>Achievement of one of the strategic scorecard measures or one of the personal objectives is regarded as threshold performance for that element.</p> <p>Deferred share awards are not subject to any further performance conditions. Awards will normally vest three years after the date of award but may be forfeited if the individual leaves employment before the vesting date. The Committee has discretion to award 'good leaver' status.</p>
<p><b>LTIP</b></p> <p>Awards under the LTIP are designed to incentivise and reward achievement of the Group's long term strategic objectives and creation of sustainable value for shareholders through execution of the strategy.</p>	<p>Awards are made annually subject to performance measures set by the Committee, which are aligned with business strategy and the Group's stated KPIs. The Committee has the discretion to change the weightings of measures, remove measures or introduce new measures to support delivery of the Group's objectives and strategy.</p> <p>Achievement of each element is assessed independently.</p> <p>Awards will normally vest three years after the award is made. The Committee retains discretion to introduce a holding period which would apply after the award has vested.</p> <p>Dividend equivalents accrue over the performance period and are paid at the time of vesting on the number of shares that vest.</p>	<p>The maximum annual individual award level under the plan is 300% of salary.</p> <p>The annual award level for Executive Directors is 300% of salary.</p>	<p>LTIP awards are subject to the following performance measures:</p> <ul style="list-style-type: none"> <li>• 40% is based on cumulative free cash flow;</li> <li>• 40% is based on total sales (excluding fuel and VAT); and</li> <li>• 20% is based on underlying EPS growth.</li> </ul> <p>Achievement of threshold performance will ordinarily result in vesting of 25% of each element with 100% vesting for maximum performance. However, the Committee has discretion to reduce the level of vesting at threshold.</p> <p>A return on capital employed (ROCE) underpin applies to the vesting of the total LTIP award.</p> <p>For all awards, the Committee has the discretion to adjust the vesting calculations as set out in these notes.</p>



**Notes to Policy table**

**Annual Bonus Plan and Deferred Share Plan**

Annual Bonus Plan is measured over the financial year. The current measures are underlying profit before tax (50%), strategic measures (30%) and personal performance (20%). The weightings are reviewed each year to ensure strategic alignment and the Committee has the flexibility to adjust weightings and measures to ensure alignment to the strategy and our six priorities. Weightings for each year are disclosed in the statement of implementation.

Underlying profit before tax is a widely accepted measure of Group and Director performance. Directors are able to impact it within the year, and it is directly aligned to shareholder experience. The Committee has the discretion to adjust for material exceptional events or actions which were not contemplated at the time of target setting, to ensure that vesting is accurate and fair. As a point of principle, the Committee has decided that the threshold for profit targets will always be higher than actual profit achieved in the previous financial year.

Strategic scorecard measures are set annually in line with the Group's strategy and key objectives for the financial year. The Committee uses objective measures where possible (for example, achievement of cost/productivity savings), and exercises its judgement to assess the outcome of each element at the end of the year.

Personal objectives for the CEO are set by the Chairman, in line with objectives for the

next 12 months and the longer term Group strategy. The CEO sets objectives for the other Executive Director(s). The Committee assesses performance against objectives and personal bonus achievement at the end of each year.

Deferred share awards are not subject to any further performance conditions.

**LTIP**

The Committee believes the mix of measures and weightings are correct for the Group's current strategy and aims. The current measures are:

- total sales (excluding VAT and fuel) (40%);
- free cash flow (40%); and
- underlying EPS growth (20%).

The Committee has the discretion to amend the weightings, introduce new measures and exclude measures in order to best align to long term shareholder interests.

Targets are determined by the Committee at the time of grant, and are based on the internal financial plan, external expectations and the need to ensure we incentivise long term sustainable value creation for shareholders.

Total sales growth is the change in total sales (excluding VAT and fuel).

Free cash flow is operating cash flow<sup>1</sup> plus net proceeds from sale of properties (excluding store sale and leasebacks) less capital expenditure (excluding onerous capital payments)

<sup>1</sup> Operating cash flow is EBITDA plus movements in operating working capital adjusted for non-cash charges as set out in the notes to the financial statements.

Underlying EPS is based on underlying profit before tax adjusted for a normalised tax charge.

The Committee uses a ROCE underpin to ensure that ROCE exceeds weighted average cost of capital for the performance period. The calculation of ROCE is as described in the Glossary on page 122.

The Committee has discretion to amend the calculation for free cash flow in the interests of fairness and accuracy. In this event, a full disclosure will be given in the Directors' remuneration report.

**Remuneration for the wider Group**

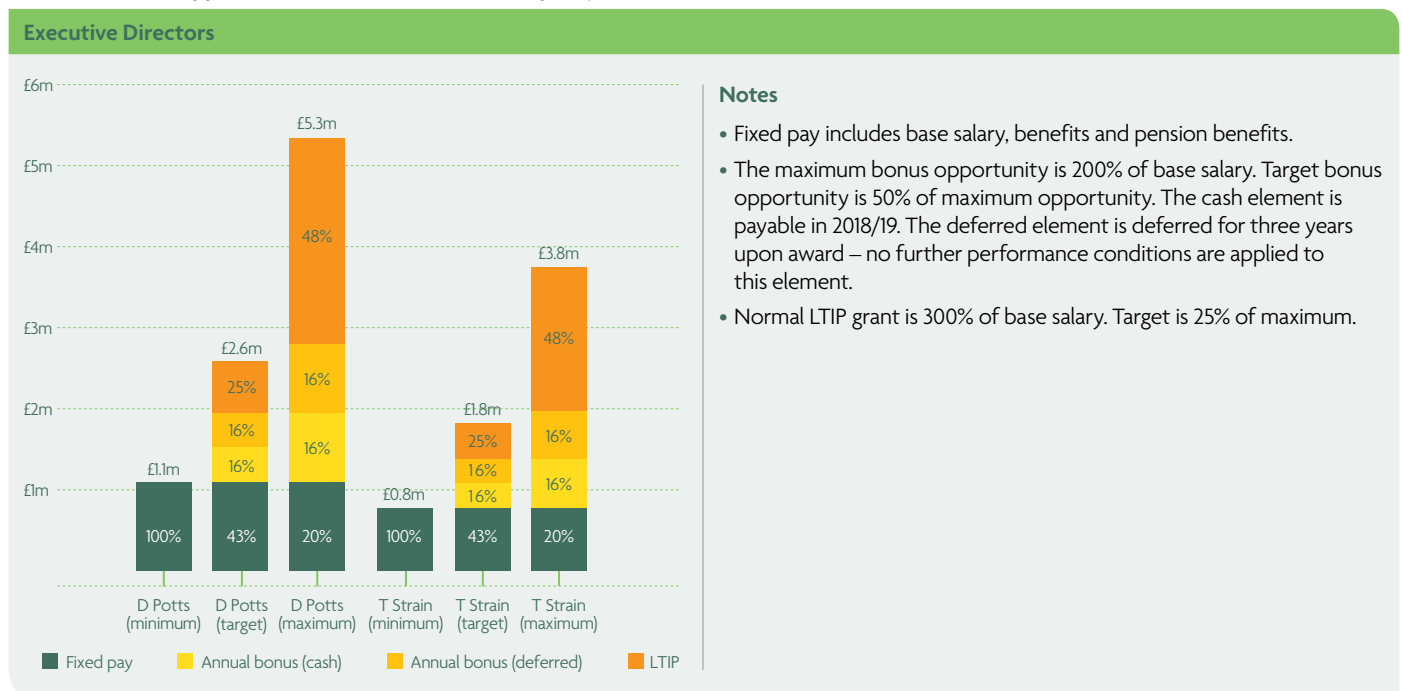
Everyone at store manager level and above participates in the Annual Bonus Plan, with the same measures and targets as the Executive Directors. The same population participate in the LTIP, again with the same measures and targets. This alignment within the organisation is an important part of 'Teamwork', one of our five ways of working.

**Approach to new hires**

Prior to appointment, the Committee will apply the following principles in agreeing the remuneration of Executive Directors:

- The overall package will be sufficient to attract and retain the best talent to effectively deliver the Group's strategy, taking into account similar positions in the market, experience of the candidate and current remuneration.
- The Committee will look to align the base salary, benefits, pension benefits, annual bonus and LTIP, in line with the remuneration

**Illustration of the application of the new remuneration policy**



**Notes**

- Fixed pay includes base salary, benefits and pension benefits.
- The maximum bonus opportunity is 200% of base salary. Target bonus opportunity is 50% of maximum opportunity. The cash element is payable in 2018/19. The deferred element is deferred for three years upon award – no further performance conditions are applied to this element.
- Normal LTIP grant is 300% of base salary. Target is 25% of maximum.

## Directors' remuneration report continued

policy whilst taking into account the individual circumstances (including compensation for loss of remuneration from a previous employer) of candidates and existing Executive Directors.

- The maximum variable pay opportunity will be 500% of salary. Up to 200% may be earned under the Annual Bonus Plan, and up to 300%

may be granted under the LTIP. This would be separate to arrangements required to recruit the preferred candidate.

### Directors' service contracts, notice periods, termination payments and change of control

Our policy is for Executive Directors to have rolling service contracts with a notice period of

12 months. On an exceptional basis, to complete external recruitment, a longer initial period reducing to 12 months might be used.

At its discretion, the Group may pay in lieu of notice. Payment in lieu of notice could potentially include up to 12 months base salary, benefits and pension, but is payable in instalments and subject to mitigation.

### Termination payments

The table below sets out the treatment of elements of remuneration that would normally apply for Executive Directors whose service with the Group terminates:

CIRCUMSTANCES OF TERMINATION	SALARY AND CONTRACTUAL BENEFITS	ANNUAL BONUS PLAN	UNVESTED DEFERRED SHARES	UNVESTED LTIP AWARDS
Resignation or gross misconduct	Paid to date of termination	No bonus paid for year of termination	Award lapses when employment ends	Award lapses when employment ends
Injury/ill health, disability, death, retirement (with agreement of the Group)	Paid to date of termination	Eligible to be considered for a bonus, calculated on a time pro-rata basis for service in the relevant financial year. Subject to meeting performance targets	Deferred shares are retained and will typically vest on the normal three year cycle. The Committee has discretion to bring forward vesting in exceptional circumstances	Eligible to be considered for good leaver status, which gives entitlement to retain the award granted calculated on a time pro-rata basis. Vesting of any pro-rata award is subject to performance conditions. Malus provisions will continue to apply to unvested awards
Negotiated termination at the discretion of the Committee	Paid to date of termination	Eligible to be considered for a bonus, calculated on a time pro-rata basis for service in the relevant financial year. Subject to meeting performance targets	Deferred shares are retained and will typically vest on the normal three year cycle. The Committee has discretion to bring forward vesting in exceptional circumstances	At the Committee's discretion, may be eligible to be considered for good leaver status, which gives entitlement to retain the award granted calculated on a time pro-rata basis. Vesting of any pro-rata award is subject to performance conditions. Malus provisions will continue to apply to unvested awards

Under the Annual Bonus and LTIP scheme rules, the Committee has discretion in relation to termination of employment, including:

- whether a bonus payment is made;
- whether unvested deferred shares and LTIP awards are retained or not;
- level of vesting; and
- timing of any payment arising from vesting.

In exercising discretion, the Committee will take into account factors such as personal performance and conduct, overall Group performance and the specific circumstances of the departure (including but not limited to whether it is by mutual agreement). The Committee may take into account payments it considers reasonable in consideration of potential legal claims, including reasonable reimbursement of legal fees. The Committee may also consider providing support related to the ending of employment, including outplacement support, continuation of benefits for a limited period or reimbursement of repatriation costs.

### Change of control

In the event of a change of control, deferred share awards vest immediately. Annual bonus and LTIP awards vest to the extent that any performance conditions have been met and, unless the Committee decides otherwise, with

a pro-rata reduction to reflect the performance period not yet completed.

### Clawback and malus

As noted in the 2014/15 Directors' remuneration report, the Committee has incorporated clawback into the Group's incentive plans in addition to the existing malus provisions in the Group's DSBP (Deferred Share Bonus Plan) and LTIP.

Annual cash bonus and DSBP awards made in respect of 2016/17 are therefore subject to clawback and malus provisions. Clawback and malus provisions apply to LTIP awards granted from April 2015 onwards.

Clawback provisions will apply for three years following payment of a cash bonus (malus already applies to the deferred share element for a three year period) and two years following vesting of an LTIP award (i.e. five years from grant). Awards may be clawed back in the following circumstances:

- material misstatement of results;
- gross misconduct;
- reputational damage; and/or
- performance assessment error.

The Committee can adjust clawback and malus periods as they deem appropriate.

### Policy on remuneration for Non-Executive Directors

#### Fees

Fees for the Non-Executive Directors (NEDs) are determined by the Chairman and the Executive Directors, and are reviewed from time-to-time with regard to the necessary time commitment, and the level of fees in comparable companies. The Chairman's fee is determined by the Remuneration Committee and the Board, and is reviewed on the same basis.

Fees for the NEDs are made up of a base fee, plus additional fees for Committee chairmanship, Committee membership and for the appointed Senior Independent Director. The Chairman receives a single fee only. Current fee levels are disclosed on page 42. There are no additional fees for other duties to the Group.

#### Benefits and other items in the nature of remuneration

The Chairman has use of a car and driver and receives private health provision. The Chairman and NEDs are entitled to normal colleague discount. Neither the Chairman nor any of the NEDs participate in any Group incentive scheme.

## Implementation of remuneration policy in 2017/18

### Base salary

Annual base salaries for the Executive Directors are set out below:

	2017/18 £000	2016/17 £000
D Potts	850	850
T Strain	596	575

David Potts was appointed as CEO on 16 March 2015 on a base salary of £850,000. In 2016/17, David waived the increase awarded by the Committee. For 2017/18, the Committee offered a rise equivalent to store colleagues, but David again waived the increase awarded, and his salary remains unchanged.

Trevor Strain was promoted to the role of CFO in April 2013 on a base salary significantly below market rate. In 2014/15 he assumed responsibility for Property, Fuel, Online, Popular and Useful Services, and Strategy. In 2015/16 he was given responsibility for the growing wholesale business, including our partnership with Amazon and our petrol forecourt initiatives. He has also taken on responsibility for the Legal and Company Secretary functions. The Committee therefore felt it appropriate to award a salary increase in line with store colleagues, taking his salary to £596,000, effective 1 February 2017.

The Committee took this decision in light of the fact Trevor Strain was appointed on a salary with the intention of stepping it up over time as he developed in role. He has proved to be pivotal in the performance and turnaround of the business. Given his contribution, his additional responsibilities and his marketability, the Committee did consider whether a higher increase would be appropriate; however, it decided to keep in line with increases in the wider business.

### Benefits and pension

The Executive Directors will receive benefits and a pension salary supplement in line with the current policy. David Potts and Trevor Strain receive a pension salary supplement of 25% and 24% of base salary, respectively.

### Annual bonus

The structure of the bonus, including maximum potential (200% of salary) and the requirement to defer 50% of any bonus in shares under the DSBP, is in line with the Directors' remuneration policy (policy set out on pages 37 to 40).

The performance measures and weightings for the Executive Directors are as follows:

	Weightings (% of maximum bonus opportunity)
Underlying profit before tax	50%
Strategic scorecard	30%
Personal objectives	20%

Underlying profit before tax targets are set by reference to internal budgets.

Scorecard measures for 2017/18 will focus on strategic objectives in the areas of like-for-like sales (20%) and productivity/cost reduction (10%).

Personal objectives will be underpinned by the Group's strategic objectives.

Detail on the performance targets is regarded by the Directors as commercially sensitive at this time and cannot be disclosed here. Subject to being considered no longer commercially sensitive, targets will be disclosed in a future remuneration report.

### LTIP

The LTIP awards for David Potts and Trevor Strain for 2017 will be 300% of salary. The reason for awarding at the maximum of the range is to align the Directors with the turnaround opportunity. All leaders from store managers and above were granted an exceptional 'teamwork' award (LTIP) in 2016, in recognition of the size of the turnaround opportunity and the work required. Only the Executive Directors did not get a higher than usual grant. Given that shareholders expressed support for the principle of higher reward for value creation, and the Chief Executive is already two years in role, with a significant track record of achievement, the Committee felt it appropriate to align the incentives to stretch beyond the financial plan.

The performance measures, weightings and targets attached to LTIP awards due to be made in April 2017 are as follows:

Measure	Weighting (% of maximum award)	Targets <sup>4</sup>
Sales <sup>1</sup>	40%	£400m to £750m
Free cash flow <sup>2</sup>	40%	£600m to £800m
Underlying EPS growth <sup>3</sup>	20%	5% to 10% per annum

<sup>1</sup> The change in total sales (excluding VAT and fuel).

<sup>2</sup> Operating cash flow plus net proceeds from sale of properties (excluding store sale and leasebacks) less capital expenditure (excluding onerous capital payments).

<sup>3</sup> See the Glossary on page 122.

<sup>4</sup> Vesting is on a straight-line basis between points.

The Committee will take account of the Group's ROCE over the performance period. If the Committee is not satisfied with ROCE performance over the period it will retain discretion to adjust outcomes downward.

For the sales targets, as set out in the Directors' remuneration policy, the Committee will retain the discretion to adjust the targets in the event of material disposals or store closures during the performance period which were not taken into account in setting the target range.

The Committee has discretion to adjust these calculations for material exceptional events or actions (which may include strategic changes to capital expenditure approved by the Board and material acquisitions or disposals) which were not in the contemplation of the Committee at the time the targets were set and which might otherwise materially distort the outcome, in order to ensure that vesting of the LTIP is an accurate and fair reflection of performance. If the Committee exercises its discretion to amend the calculation, a full disclosure of the reason for the amendment and an explanation of the impact will be given in the relevant Annual report on remuneration.

### Chairman and Non-Executive Director fees

Base fees for Non-Executive Directors have not been reviewed since 2008, and are therefore being increased by 2% to £61,200. Fees for subcommittee membership (last reviewed in 2013) have been increased to £7,000. The fees for subcommittee chair roles are unchanged. The fee for the Senior Independent Director is also unchanged at £20,000. The base fee for the Chairman is unchanged at £400,000.

## Directors' remuneration report continued

# Annual report on remuneration

### Audited information

#### Single total figure of remuneration

The table below sets out the single total figure of remuneration and breakdown for each Director for 2016/17 and the comparative figure for 2015/16.

	2016/17					2015/16						
	Salary/fees £000	Benefits <sup>1</sup> £000	Annual bonus <sup>2</sup> £000	LTIP <sup>3</sup> £000	Pension benefits <sup>4</sup> £000	Total £000	Salary/fees £000	Benefits <sup>1</sup> £000	Annual bonus <sup>2</sup> £000	LTIP £000	Pension benefits <sup>4</sup> £000	Total £000
<b>Executive Directors</b>												
D Potts <sup>5</sup>	850	31	1,700	–	213	2,794	747	226	1,092	–	187	2,252
T Strain	575	35	1,150	783	138	2,681	525	35	763	–	126	1,449
D Philips <sup>6</sup>	–	–	–	354	–	354	39	1	–	–	10	50
<b>Non-Executive Directors</b>												
A Higginson	400	15	–	–	–	415	400	1	–	–	–	401
R Anand <sup>7</sup>	92	–	–	–	–	92	7	–	–	–	–	7
P Vennells <sup>7</sup>	76	–	–	–	–	76	5	–	–	–	–	5
I Lee <sup>8</sup>	54	–	–	–	–	54	32	–	–	–	–	32
N Davidson <sup>9</sup>	92	–	–	–	–	92	25	–	–	–	–	25
B Richards <sup>10</sup>	92	–	–	–	–	92	33	–	–	–	–	33
P Cox <sup>11</sup>	–	–	–	–	–	–	102	–	–	–	–	102
P Hughes <sup>11</sup>	–	–	–	–	–	–	84	–	–	–	–	84
R Gillingwater <sup>12</sup>	–	–	–	–	–	–	26	–	–	–	–	26
J Waterous <sup>13</sup>	–	–	–	–	–	–	92	–	–	–	–	92

1 Taxable benefits for the Executive Directors include a car allowance (or other car benefit), transport costs and private health provision. The Chairman has use of a car and driver for Group business and receives private health provision. All Directors receive the Group's normal staff discount entitlement which is not taxable. The value of any new Sharesave awards granted in 2016/17 is also included in this figure. The Group has been advised that for the Chairman, CEO and CFO, certain expenses in relation to travel should be treated as a taxable benefit. The table above includes these travel expenses and the corresponding tax contributions.

2 50% of the annual bonus is deferred in shares for a period of three years. There are no performance conditions attached to this deferred element.

3 Awards granted under the LTIP in June 2014 are scheduled to vest in June 2017. The performance conditions, relating to the 2014-2017 LTIP award, ended on 29 January 2017. The figures stated also include the number of dividends accrued on the 2014-2017 LTIP award at the time of vesting.

4 D Potts received a salary supplement equal to 25% of base salary. T Strain received a salary supplement of 24% of base salary. None of the Executive Directors have a prospective entitlement to a defined benefit pension by reason of qualifying services.

5 D Potts was appointed to the Board on 16 March 2015. The figures disclosed for 2015/16 are for the period following appointment to the Board.

6 D Philips stepped down from the Board on 16 February 2015. The figures disclosed for 2015/16 are for the period prior to him stepping down. Loss of office payments were disclosed in the 2015/16 remuneration report.

7 R Anand and P Vennells were appointed to the Board on 1 January 2016. The figures disclosed for 2015/16 are for the period following appointment to the Board.

8 I Lee was appointed to the Board on 1 September 2015. The figures disclosed for 2015/16 are for the period following appointment to the Board. I Lee retired from the Board on 31 August 2016.

9 N Davidson was appointed to the Board on 1 October 2015. The figure disclosed for 2015/16 is for the period following appointment to the Board.

10 B Richards was appointed to the Board on 1 September 2015. The figures disclosed for 2015/16 are for the period following appointment to the Board.

11 P Cox and P Hughes stepped down from the Board on 31 December 2015. The figures disclosed for 2015/16 are for the period prior to them stepping down.

12 R Gillingwater stepped down from the Board on 4 June 2015. The figure disclosed for 2015/16 is for the period prior to him stepping down.

13 J Waterous retired from the Board on 31 January 2016.

#### Annual bonus

The table below provides a summary of the performance achieved under the annual bonus for 2016/17:

Director	Maximum bonus opportunity (% of salary)	Actual bonus (% of salary)	Actual bonus (£000)	Bonus deferred into shares (% of award)	Bonus paid in 2017 (£000)
D Potts	200%	200%	1,700	50%	850
T Strain	200%	200%	1,150	50%	575

## Group financial and strategic scorecard

 Actual performance achieved

Performance measure	Weighting (as a % of total annual bonus opportunity)	Achieved as a % of maximum			Actual achievement	Payout (as a % of total annual bonus opportunity)
		Threshold	Target	Maximum		
<b>Group financial</b>		20% payout	60% payout	100% payout		
Underlying profit before tax	50%	£302m	£316m	£330m	£337m	50%
<b>Strategic scorecard</b>		20% payout	50% payout	100% payout		
Cost reduction/productivity	10%	£170m	£180m	£190m	£269m	10%
Like-for-like sales	20%	(2%)	(1%)	0%	+1.7%	20%
Personal objectives	20%					

## Personal measures

Director	Weighting (as a % of total annual bonus opportunity)	Objective	Commentary
D Potts	20%	Deliver key actions against the six priorities	<ul style="list-style-type: none"> <li>Fresh Look store refurbishment programme met targets</li> <li>Improvements in store standards, product quality and supply chain</li> <li>Launch of the 'Best' premium range</li> <li>Automated store ordering system delivered to every store</li> <li>Work led to increased like-for-like sales</li> </ul>
		Develop capability	<ul style="list-style-type: none"> <li>Executive Committee stabilised</li> <li>Senior leadership team enhanced</li> <li>84 new store managers hired</li> <li>All store managers and regional managers attended five day leadership development programme designed to improve store standards, colleague engagement and customer satisfaction</li> </ul>
		Strengthen GSCOP compliance, processes and culture	<ul style="list-style-type: none"> <li>Significant strengthening of internal GSCOP processes, including governance and control framework, improving the compliance culture and the way we treat suppliers</li> </ul>
		Develop and start to implement a strategy for growth post the Rebuild phase of the turnaround	<ul style="list-style-type: none"> <li>Development of Popular and Useful Services</li> <li>Development of Wholesale business (including Amazon partnership, petrol forecourts and re-launch of the Safeway brand)</li> </ul>
T Strain	20%	Build capacity in his functions	<ul style="list-style-type: none"> <li>Completed talent and succession review for function</li> <li>Hired new CIO</li> <li>Built talent pipeline by Teamwork moves across functions</li> </ul>
		Cost reduction and Group simplification programme	<ul style="list-style-type: none"> <li>Group has exceeded cost/productivity savings target</li> </ul>
		Develop and execute plans for non-core/non-strategic assets	<ul style="list-style-type: none"> <li>Disposal of investment in Fresh Direct Inc. at a profit</li> </ul>
		Deliver cash improvement programmes and Group cash flow targets	<ul style="list-style-type: none"> <li>Free cash flow targets exceeded</li> <li>Net debt reduced by £552m</li> </ul>
		Lead the process to identify and implement the actions required to deliver our strategy	<ul style="list-style-type: none"> <li>Leads Wholesale business, Online, and Popular and Useful Services. Significant progress made across all including Amazon partnership, petrol forecourts and re-launch of the Safeway brand</li> </ul>

## Performance summary

As well as performance against individual objectives (which have been completed in full), the Committee considered the wider performance of the Group. The Committee concluded that management were making substantial progress against the Fix phase of the turnaround, as well as laying the foundations for Rebuild and Grow. The financial performance resulting from the contribution of the Executive Directors has exceeded maximum. The Committee therefore decided to award them each the maximum 20%.

50% of any bonus payable is deferred in shares under the DSBP which vest three years after the date of award. Dividend equivalents will accrue and be paid on the shares that vest. Deferred shares are normally forfeited if the individual leaves the Group before they vest.

## Directors' remuneration report continued

### LTIP awards

Awards granted under the LTIP in June 2014 are scheduled to vest in June 2017. The performance period relating to these awards ended on 29 January 2017. Details of the performance conditions and the extent to which they have been satisfied are set out below:

	Weighting	(25%) Threshold performance required	(100%) Maximum performance required	Actual outcome	Actual LTIP vesting (% of maximum)
<b>Performance condition<sup>1</sup></b>					
Cumulative operating cash flow from 2014/15 to 2016/17 inclusive	50%	Achievement of cumulative free cash flow of £1bn over the three year performance period	Achievement of cumulative free cash flow of £2bn over the three year performance period	£2bn	50%
Underlying basic EPS for 2016/17	30%	17p	23p	10.86p	0%
Total sales (excluding VAT and fuel) for 2016/17	20%	£14bn	£15bn	£12.9bn	0%
LTIP vesting (% of maximum)					50%

<sup>1</sup> Vesting is on a straight-line basis between threshold and maximum.

### Share awards granted in 2016/17

The table below sets out the share awards made to the Executive Directors during 2016/17 under the Group's LTIP:

	Grant date	Award type	Basis on which award made	Face value of award (£000) <sup>1</sup>	Percentage of award vesting at threshold performance	Performance period end date	Performance conditions
D Potts	6 April 2016	Conditional award	240% of salary	2,040	25%	3 February 2019	See table below
T Strain	6 April 2016	Conditional award	240% of salary	1,380	25%	3 February 2019	See table below

<sup>1</sup> The face value in the table above has been calculated by multiplying the maximum number of shares that could vest by the average share price used to determine the number of shares awarded. The average share price used was £2.004 and this was calculated over a period of five business days prior to the date of grant.

The table below sets out the performance conditions attached to the awards made during the year. These awards were granted in April 2016.

Measure <sup>1</sup>	Period over which the measure applies	Weighting (% of maximum award)	Threshold (25%)	Maximum (100%)
Cumulative free cash flow	Three year performance period (2016/17 – 2018/19)	60%	£620m	£1,340m
Underlying basic EPS	Three year performance period (2016/17 – 2018/19)	20%	6% p.a.	13% p.a.
Total sales (excluding fuel and VAT)	Final year of the performance period (2018/19)	20%	£12.7bn <sup>2</sup>	£13.2bn <sup>2</sup>

<sup>1</sup> For further detail on the definition of these measures, see page 39.

<sup>2</sup> In line with the policy, the maximum target has been adjusted for the impact of closures of stores during the year.

The Committee will take account of the Group's ROCE over the performance period. If the Committee is not satisfied with ROCE performance over the period it will retain discretion to adjust outcomes downward.

For the free cash flow measure, the Committee has set minimum and maximum 'guardrails' for maintenance expenditure and cumulative net proceeds from property sales over the performance period. When considering vesting against the free cash flow measure, the Committee will review and adjust as appropriate in the event of operation outside the agreed parameters. The Committee will disclose these parameters and any decision taken to adjust outcomes retrospectively in the relevant Annual report on remuneration. It should be noted that decisions in relation to material property sales and expenditure on maintenance and infrastructure are taken by the Board as a whole.

For the revenue targets, as set out in the Directors' remuneration policy, the Committee will retain the discretion to adjust the targets in the event of material disposals or store closures during the performance period which were not taken into account in setting the target range. For the avoidance of doubt, the revenue targets in the table above exclude M Local convenience stores.

The Committee has discretion to adjust these calculations for material exceptional events or actions (which may include strategic changes to capital expenditure approved by the Board and material acquisitions or disposals) which were not in the contemplation of the Committee at the time the targets were set and which might otherwise materially distort the outcome, in order to ensure that vesting of the LTIP is an accurate and fair reflection of performance. If the Committee exercises its discretion to amend the calculation, a full disclosure of the reason for the amendment and an explanation of the impact will be given in the relevant Annual report on remuneration.

### Payments to past Directors and loss of office payments

As disclosed in the 2014/15 Annual Report, Dalton Philips was granted good leavers status when he left the business in 2015. His 2014-2017 LTIP therefore vests on a pro-rata basis, in line with the achievement of performance conditions, as outlined above, to the value of £353,558.

No other payments (including loss of office payments) have been made during 2016/17 to any individual who was previously a Director of the Group.

## Statement of Directors' shareholding

The Group has share ownership guidelines for Executive Directors of 200% of salary. Under the guidelines, Executive Directors are expected to retain 50% of vested share awards (net of tax), including shares from the deferred element of the annual bonus, until the guideline is reached. Shares held under the deferred share bonus plan (calculated on a post-tax basis) which are subject only to a continuing service requirement, will be included in assessing the level of shareholding. The shareholding guideline should be reached within five years of appointment to the Board. The Group has share ownership guidelines for Non-Executive Directors of 50% of base fees. This guideline should be reached within three years of appointment to the Board or three years after the date of adoption of the policy for incumbent Directors.

David Potts has now met his shareholding requirement. Trevor Strain has not yet met the 200% shareholding guideline but is within the five year period permitted to build up his shareholding.

## Directors' shareholdings – Executive Directors

	Shareholding requirement (% salary)	Shareholding as at 27 January 2017 (% salary) <sup>1,2</sup>	Shares owned outright	Deferred shares not subject to performance	Share save options not subject to performance	LTIP shares subject to performance <sup>3</sup>	Total interests in shares
<b>Executive Directors</b>							
D Potts	200%	265%	1,002,881	270,306	7,411	2,311,329	3,591,927
T Strain	200%	117%	97,794	385,670	7,682	1,904,691	2,395,837

<sup>1</sup> Includes shares held under the DSBP on an after tax basis.

<sup>2</sup> For the purpose of calculating the shareholding as a percentage of salary, the share price of £2.381 as at 27 January 2017 (the last trading day of the financial year ended 29 January 2017) has been used (other than for shares purchased in the market which are valued at the acquisition price).

<sup>3</sup> 576,995 shares represent the LTIP award granted to T Strain in June 2014 which is due to vest in June 2017. 50% of the award is linked to cumulative free cash flow targets. 25% of this element vests for achieving cumulative free cash flow of £1bn over the three year performance period and 100% vests for achieving £2bn over the three year performance period. 30% of the award is linked to underlying earnings per share (EPS) targets. 25% of this element vests for achieving underlying EPS of 17p for the financial year 2016/17 and 100% vests for achieving underlying EPS of 23p for the financial year 2016/17. 20% of the award is linked to total sales (excluding VAT and fuel). 25% of this element vests for achieving total sales of £14bn for the financial year 2016/17. 50% vests for achieving total sales of £14.4bn for the financial year 2016/17 and 100% vests for achieving total sales of £15bn for the financial year 2016/17. Vesting is on a straight-line basis between each of the points. 1,293,365 shares and 639,074 shares represent LTIP awards granted to D Potts and T Strain respectively in April 2015 which are due to vest in April 2018. 60% of the award is linked to cumulative free cash flow targets. 25% of this element vests performance period and 100% vests for achieving cumulative free cash flow of £1.6bn over the three year period. 20% of the award is linked to an underlying earnings per share (EPS) target. 25% of this element vests for achieving underlying EPS of 10p for the financial year 2017/18 and 100% vests for achieving underlying EPS of 15p for the financial year 2017/18. 20% of the award is linked to total sales (excluding VAT and fuel). 25% of this element vests for achieving total sales of £12.7bn for the financial year 2017/18. 100% vests for achieving total sales of £13.2bn for the financial year 2017/18. Vesting is on a straight-line basis for the cumulative free cash flow and total sales (excluding VAT and fuel) measures. Intermediate vesting applies for the underlying earnings per share measure: 10p (25%), 12p (60%), 15p (100%), with straight-line vesting between each point. Performance targets for the 1,017,964 and 688,622 shares granted to D Potts and T Strain respectively represent LTIP awards made in April 2016 which are due to vest in April 2019. Performance targets for these awards are disclosed in the section headed 'Share awards granted in 2016/17' on page 44.

## Directors' shareholdings – Non-Executive Directors

All Non-Executive Directors are still within the three year period allowed to build up their shareholding. Shareholdings as at 29 January 2017 (or date of stepping down from the Board in the case of I Lee) are set out in the table below.

	29 January 2017 Total (owned outright)
A Higginson	266,209
R Anand	12,500
N Davidson	–
I Lee	–
B Richards	–
P Vennells	–

There have been no changes in the Directors' interests since the year end.

The table below sets out the total remuneration figure for the CEO over the same eight year period, valued using the methodology applied to the single total figure of remuneration.

	Chief Executive	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16 <sup>3</sup>	2016/17
Total remuneration (£000)	D Potts	–	–	–	–	–	–	2,252	2,794
	D Philips	–	3,328 <sup>2</sup>	2,502	1,089	1,089	2,101	50	354
	M Bolland	1,159	304	–	–	–	–	–	–
Annual bonus payment (% of maximum opportunity)	D Potts	–	–	–	–	–	–	73%	100%
	D Philips	–	70%	90%	0%	0%	60%	–	–
	M Bolland	0% <sup>1</sup>	–	–	–	–	–	–	–
LTIP vesting level achieved (% of maximum opportunity)	D Potts	–	–	–	–	–	–	–	–
	D Philips	–	–	–	0%	0%	0%	0%	50%
	M Bolland	–	–	–	–	–	–	–	–

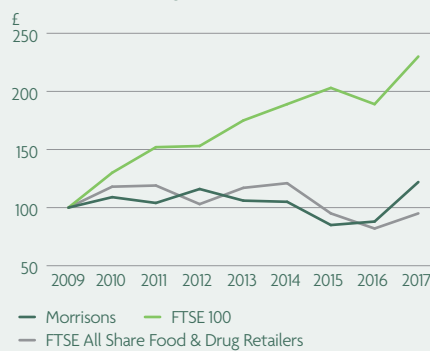
<sup>1</sup> M Bolland was not treated as a good leaver and therefore did not receive a bonus in 2009/10.

<sup>2</sup> Total remuneration includes value of unrestricted share award over 319,401 shares and restricted share award over 120,965 shares granted on recruitment.

<sup>3</sup> D Potts was appointed on 16 March 2015 and D Philips stepped down from the Board on 16 February 2015.

## Performance graph and table

### Value of a £100 holding



The graph shows the Group's total shareholder return (TSR) compared with the TSR of the FTSE 100 and FTSE All Share Food and Drug Retailers indices over the eight year period to 29 January 2017. These indices have been selected as being appropriate in giving a broad equity view and given that the Group is or has been constituent of these indices over the period.

TSR is a measure of the returns that a company has provided for its shareholders, reflecting share price movements and assuming reinvestment of dividends.

## Directors' remuneration report continued

### Change in remuneration of CEO compared to Group employees

The table below sets out the change in total remuneration paid to the CEO from 2015/16 to 2016/17 and the average percentage change from 2015/16 to 2016/17 for employees of the Group as a whole.

	% increase in element between 2015/16 and 2016/17		
	Salary and fees	Taxable benefits <sup>3</sup>	Annual bonus
D Potts	0%	0%	55.7%
All Group employees <sup>1</sup>	5.4%	0%	31% <sup>2</sup>

<sup>1</sup> Reflects the change in average pay for all Group employees employed in both the financial year 2015/16 and the financial year 2016/17.

<sup>2</sup> Reflects the increase in the average bonus payout for eligible employees.

<sup>3</sup> Change in taxable benefits for D Potts excludes relocation costs in 2015/16.

### Relative importance of spend on pay

The table below sets out the total spend on remuneration in the 2015/16 and 2016/17 financial years compared with distributions to shareholders.

	2016/17 £m	2015/16 £m	Difference £m
Total spend on remuneration for all Group employees	1,925	1,944	(19)
Profit distributed by way of dividends	118	260	(142)

### The Committee and its advisers

During the year, the following individuals were members of the Remuneration Committee:

Name of Director	Membership	
	From	To
I Lee (Chairman until departure)	2 Sep 2015	31 Aug 2016
R Anand	21 Jan 2016	To date
N Davidson	3 Nov 2015	To date
A Higginson	22 Jan 2015	To date
B Richards	2 Sep 2015	To date
P Vennells	21 Jan 2016	To date

The CEO, the Group People Director and other HR representatives also attend meetings (other than where their own remuneration is being discussed) by invitation. The Company Secretary acts as secretary to the Committee.

Deloitte LLP (Deloitte) were appointed in July 2014 and served as independent advisers until August 2016. In August, Willis Towers Watson were appointed by the Committee, following a competitive tender process, to provide independent external advice on market practice and Executive and Non-Executive remuneration. Fees are agreed by the Committee according to services provided. Total fees paid during 2016/17 to Deloitte for material advice and assistance in relation to remuneration matters were £86,000, on a time and expense basis. Total fees paid to Willis Towers Watson were £92,427, also on a time and expense paid basis.

### Statement of voting at 2014 AGM

As disclosed in previous Annual Reports, the table below shows the voting outcome at the June 2014 AGM for approval of the remuneration policy:

	Votes for	For as a % of votes cast	Votes against	Against as a % of votes cast	Abstentions	Total
Remuneration policy	1,142,938,356	73.46	412,940,651	26.54	35,276,870	1,591,155,877

### Statement of voting at 2016 AGM

The table below shows the voting outcome at the June 2016 AGM for approval of the 2015/16 remuneration report:

	Votes for	For as a % of votes cast	Votes against	Against as a % of votes cast	Abstentions	Total
Remuneration report	1,371,795,348	83.04	280,146,204	16.96	50,092,032	1,702,033,584

### Rooney Anand

Senior Independent Director  
8 March 2017



## Directors' report

# Statutory disclosures

The following disclosures have been included elsewhere within the Annual Report and are incorporated into the Directors' report by reference.

Disclosure	Page
Financial instruments	91 to 94
Financial risk management	92
Future developments	2 to 22
Dividends	71
Greenhouse gas emissions	22
Corporate governance report	23 to 32
Directors of the Group	24 and 25
Employee involvement	12

Disclosures required pursuant to Listing Rule 9.8.4R can be found on the following pages:

Disclosure	Page
Interest capitalised	76 to 79
Long term incentive schemes	100
Waiver of Directors' emoluments	34

### Political donations

No political donations were made in the financial year, which is Group policy.

### Going concern

The Directors' assessment of the Group and the Company's ability to continue as a going concern is based on cash flow forecasts for the Group and the committed borrowing and debt facilities of the Group. These forecasts include consideration of future trading performance, working capital requirements, retail market conditions and the wider economy.

The Group remains able to borrow cash at competitive rates. The Group has negotiated, and has available to it, committed, competitive facilities that will meet the Group's needs in the short and medium term.

Having assessed the principal risks as set out on pages 18 and 19 and the other matters discussed in connection with the Viability statement on page 30, the Directors considered it appropriate to adopt the going concern basis of accounting in preparing the financial statements.

### Forward-looking statements

The Strategic report and Directors' report are prepared for the members of the Group and should not be relied upon by any other party or for any other purpose. Where the Strategic report and Directors' report include forward-looking statements, these are made by the Directors in good faith based on the information available to them at the time of their approval of the Annual Report.

Consequently, such statements should be treated with caution due to the inherent uncertainties, including both economic and business risk factors, underlying such forward-looking statements and information.

The liabilities of the Directors in connection with the Strategic report, the Directors' remuneration report and the Directors' report shall be subject to the limitations and restrictions provided by the Companies Act 2006.

### Borrowing powers

The Articles of Association of the Group restrict the borrowings of the Group and its subsidiary undertakings to a maximum amount equal to twice the share capital and consolidated reserves.

### Relating to beneficial owners of shares with 'information rights'

Beneficial owners of shares who have been nominated by the registered holder of those shares to receive information rights under section 146 of the Companies Act 2006 are required to direct all communications to the registered holder of their shares rather than to the Group's registrar, Capita Registrars, or to the Group directly.

### Directors' and Officers' liability insurance

The Group maintains insurance cover for the protection of Directors and senior management from personal liabilities and costs which may arise in the course of fulfilling their duties. The Group also provides an indemnity to the Non-Executive Directors for such liabilities and costs to the fullest extent permitted by law.

### Substantial shareholdings

The Group has been notified by the following shareholders (excluding Directors) that they have interests in 3% or more of the total voting rights in the Group. The shares relate to the number informed by the shareholders on the notification rather than the current share register:

	As at 29 January 2017		As at 8 March 2017	
	Number of shares	% of share capital	Number of shares	% of share capital
Deutsche Bank AG	198,270,279	8.49	186,566,882	7.99
Amerprise Financial Inc	177,970,287	7.62	177,970,287	7.62
Schroders PLC	155,916,196	6.68	155,916,196	6.68
Silchester International Investors LLP	117,553,329	5.03	117,553,329	5.03
BlackRock Inc	117,232,444	5.02	117,232,444	5.02
Brandes Investment Partners, LP	117,121,738	5.01	117,121,738	5.01
Majedie Asset Management Limited	116,805,074	5.00	116,805,074	5.00
First Eagle Investment Management, LLC	114,296,273	4.89	114,296,273	4.89
Invesco Limited	111,082,524	4.76	111,082,524	4.76
Morgan Stanley	93,126,863	3.99	93,566,085	4.01
Zurich Financial Services	81,286,130	3.48	81,286,130	3.48
Eleanor Marie Kernighan	70,051,782	3.00	70,051,782	3.00

The percentage appearing above is the percentage that number represents of the issued share capital of the Group as at 29 January 2017 and 8 March 2017 respectively.

## Directors' report continued

### Additional shareholder information

Additional information for shareholders is required by the implementation of the EU Takeover Directive into UK law.

Pursuant to section 992 of the Companies Act 2006, the Group is required to disclose certain additional information. Such disclosures, which are not covered elsewhere in this report, include the following paragraphs. The disclosures set out below are in some cases a summary of the relevant provisions of the Group's Articles of Association and the relevant full provisions can be found in the Articles which are available for inspection at the Group's registered office.

### Appointment and powers of Directors

Directors are appointed by ordinary resolution at a general meeting of ordinary shareholders. The Directors have the power to appoint a Director during the year, but any person so appointed must be put up for appointment at the next AGM.

Subject to its Articles of Association and relevant statutory law, and to such direction as may be given by the Group in general meeting by special resolution, the business of the Group shall be managed by the Directors, who may exercise all powers of the Group which are not required to be exercised by the Group in general meeting.

### Articles of Association

The Group's Articles of Association may only be amended by a special resolution at a general meeting of shareholders.

### Share capital

The authorised and called-up share capital of the Group, together with details of shares allotted and cancelled during the year, are shown in note 6.5 of the Group financial statements.

At the AGM of the Group held in June 2016, a special resolution was passed to renew the authority given at the AGM held in June 2015 for the purchase by the Group of up to 233,517,658 ordinary shares, representing approximately 10% of the issued ordinary share capital at that time.

During the period, 381,043 (2016: 70,480) ordinary shares were issued to employees exercising share options and 2,733,049 (2016: 3,118,702) out of the Group's trust shares.

### Share capital and rights attaching to the Group's shares

Under the Group's Articles of Association, any share in the Group may be issued with such rights or restrictions, whether in regard to dividend, voting, return of capital or otherwise as the Group may from time-to-time by ordinary resolution determine (or, in the absence of any such determination, as the Directors may determine).

At a general meeting of the Group, every member has one vote on a show of hands and, on a poll, one vote for each share held. The notice of general meeting specifies deadlines for exercising voting rights either by proxy or present in person in relation to resolutions to be passed at a general meeting.

No member is, unless the Board decides otherwise, entitled to attend or vote either personally or by proxy at a general meeting, or to exercise any other right conferred by being a shareholder if they or any person with an interest in shares has been sent a notice under section 793 of the Companies Act 2006 (which confers upon public companies the power to require information with respect to interests in their voting shares) and they or any interested person failed to supply the Group with the information requested within 14 days after delivery of that notice. The Board may also decide that no dividend is payable in respect of those default shares and that no transfer of any default shares shall be registered. These restrictions end seven days after receipt by the Group of a notice of an approved transfer of the shares or all the information required by the relevant section 793 notice, whichever is the earlier.

The Directors may refuse to register any transfer of any share which is not a fully paid share, although such discretion may not be exercised in a way which the Financial Conduct Authority regards as preventing dealings in the shares of the relevant class or classes from taking place on an open or proper basis. The Directors may likewise refuse to register any transfer of a share in favour of more than four persons jointly. The Group is not aware of any other restrictions on the transfer of shares in the Group other than certain restrictions that may from time-to-time be imposed by laws and regulations (for example, insider trading laws).

The Group is not aware of any agreements between shareholders that may result in restrictions on the transfer of securities or voting rights.

### Other disclosures

The Group is not party to any significant arrangements which take effect, alter or terminate upon a change of control of the Group following a takeover bid.

The Group does not have any employee share schemes where the shares to which the scheme relates have rights with regard to the control of the Group which are not exercisable by employees.

### Equal opportunities for all

Integral to a high performing culture is the concept of equal opportunity for all colleagues, which we offer regardless of race, colour, nationality, ethnic origin, gender (including gender reassignment), marital or civil partnership status, disability, religion or belief, sexual orientation, age or trade union membership.

This includes applications for employment made by people with disabilities, which are given full and fair consideration. Respect underpins our behaviour towards all disabled candidates, as well as colleagues who have a disability or become disabled in any way during the course of their employment.

A full assessment of the individual's needs is undertaken and we will make reasonable adjustments to the work environment or practices in order to help people with disabilities.

All candidates and colleagues are treated equally in respect of recruitment, promotion, training, pay and other employment policies and conditions. The decisions we make are based on relevant merits and abilities.

### Health and safety policy

It is the Group's intention, so far as is reasonably practicable, to ensure the health, safety and welfare of all its employees, customers and visitors to its premises. In order to achieve this, a comprehensive health and safety manual is in place for each division of the Group and subsidiary companies within the Group. Each health and safety manual contains the policy and procedures for complying with the Health and Safety at Work Act 1974, including the provision, based on risk assessment, of safe working practices for all work activities across the Group. The Group's health and safety policy is approved by the Executive Committee. The Group has adopted the national targets set by the Health and Safety Commission for the reduction of workplace accidents and work-related ill health, and is on course to meet or exceed these targets. Health and safety performance is monitored to ensure continuous improvement in all areas.

By order of the Board

**Jonathan Burke**  
Company Secretary  
8 March 2017

## Statement of Directors' responsibilities in respect of the Annual Report and Financial Statements

The Directors are responsible for preparing the Annual Report and the Financial Statements in accordance with applicable law and regulation.

Company law requires the Directors to prepare financial statements for each financial 52 week period. Under that law the Directors have prepared the Group financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union and Group financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards, comprising FRS 101 Reduced Disclosure Framework, and applicable law). Under company law the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Group and Company and of the profit or loss of the Group and Company for that period. In preparing the financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- state whether applicable IFRSs as adopted by the European Union have been followed for the Group financial statements and United Kingdom Accounting Standards, comprising FRS 101, have been followed for the Company financial statements, subject to any material departures disclosed and explained in the financial statements;
- make judgements and accounting estimates that are reasonable and prudent; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group and Company will continue in business.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Group and Company's transactions and disclose with reasonable accuracy at any time the financial position of the Group and Company and enable them to ensure that the financial statements and the Directors' remuneration report comply with the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS Regulation.

The Directors are also responsible for safeguarding the assets of the Group and Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Directors are responsible for the maintenance and integrity of the Group and Company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

The Directors consider that the Annual Report and accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the Group and Company's position and performance, business model and strategy.

Each of the Directors, whose names and functions are listed in the Directors' report confirm that, to the best of their knowledge:

- the Group financial statements, which have been prepared in accordance with IFRSs as adopted by the European Union, give a true and fair view of the assets, liabilities, financial position and profit of the Group; and
- the Annual Report includes a fair review of the development and performance of the business and the position of the Group and Company, together with a description of the principal risks and uncertainties that it faces.

In the case of each Director in office at the date the Directors' report is approved:

- so far as the Director is aware, there is no relevant audit information of which the Group and Company's auditors are unaware; and
- they have taken all the steps that they ought to have taken as a Director in order to make themselves aware of any relevant audit information and to establish that the Group and Company's auditors are aware of that information.

### Disclosure of information to auditors

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

### Assessment of whether the Annual Report is fair, balanced and understandable

As required by the Code, the Directors confirm that they consider that the Annual Report, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the Group's position and performance, business model and strategy.

When arriving at this position the Board was assisted by a number of processes including the following:

- the Annual Report is drafted by appropriate senior management with overall coordination by the Chief Financial Officer to ensure consistency across sections;
- an extensive verification process is undertaken to ensure factual accuracy; and
- comprehensive reviews of drafts of the report are undertaken by members of the Executive Committee and other senior management; and the final draft is reviewed by the Audit Committee prior to consideration by the Board.

### Responsibility statement

We confirm that to the best of our knowledge:

- the financial statements, prepared in accordance with the applicable set of accounting standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Group and its subsidiaries included in the consolidation as a whole; and
- the Strategic report includes a fair review of the development of the business and the position of the Group and its subsidiaries included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face.

By order of the Board

**Jonathan Burke**  
Company Secretary  
8 March 2017

## Independent auditors' report

# Independent auditors' report to the members of Wm Morrison Supermarkets PLC

## Report on the financial statements

### Our opinion

In our opinion:

- Wm Morrison Supermarkets PLC's Group financial statements and Company financial statements (the financial statements) give a true and fair view of the state of the Group's and of the Company's affairs as at 29 January 2017 and of the Group's profit and cash flows for the 52 week period (the period) then ended;
- the Group financial statements have been properly prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union;
- the Company financial statements have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS Regulation.

### What we have audited

The financial statements, included within the Annual Report and Financial Statements (the Annual Report), comprise:

- the consolidated balance sheet as at 29 January 2017;
- the Company balance sheet as at 29 January 2017;
- the consolidated statement of comprehensive income for the period then ended;
- the consolidated cash flow statement for the period then ended;
- the consolidated statement of changes in equity for the period then ended;
- the Company statement of changes in equity for the period then ended; and
- the notes to the financial statements, which include a summary of significant accounting policies and other explanatory information.

Certain required disclosures have been presented elsewhere in the Annual Report, rather than in the notes to the financial statements. These are cross-referenced from the financial statements and are identified as audited.

The financial reporting framework that has been applied in the preparation of the Group financial statements is IFRSs as adopted by the European Union, and applicable law. The financial reporting framework that has been applied in the preparation of the Company financial statements is United Kingdom Accounting Standards, comprising FRS 101 Reduced Disclosure Framework (United Kingdom Generally Accepted Accounting Practice), and applicable law.

### Our audit approach

#### Overview



#### Materiality

- Overall Group materiality: £16.85m which represents 5% of underlying profit before tax.

#### Audit scope

- The Group engagement team conducted all of our audit work in the UK other than a PwC component audit team that undertook a full scope audit of a UK Manufacturing subsidiary.

#### Areas of focus

- Impairment of property.
- Onerous lease provisions and onerous property contracts.
- Commercial income and promotional funding.
- Impairment and capitalisation of intangible assets.
- Stock valuation.
- Pension accounting.

### The scope of our audit and our areas of focus

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) (“ISAs (UK & Ireland)”).

We designed our audit by determining materiality and assessing the risks of material misstatement in the financial statements. In particular, we looked at where the Directors made subjective judgements, for example in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain. As in all of our audits we also addressed the risk of management override of internal controls, including evaluating whether there was evidence of bias by the Directors that represented a risk of material misstatement due to fraud.

The risks of material misstatement that had the greatest effect on our audit, including the allocation of our resources and effort, are identified as ‘areas of focus’ in the table below. We have also set out how we tailored our audit to address these specific areas in order to provide an opinion on the financial statements as a whole, and any comments we make on the results of our procedures should be read in this context. This is not a complete list of all risks identified by our audit.

Area of focus	How our audit addressed the area of focus
<p><b>Impairment of property</b> Refer to page 64 (critical accounting judgements and estimates) and note 3.3 (property, plant and equipment).</p> <p>The Group has a large freehold store estate (£5,908m at 29 January 2017). Given the challenging trading conditions in the UK grocery retail market in recent years and the subsequent adverse impact on the market value of traditional supermarket freehold stores, the possibility of impairment of these assets is an area of focus for management, as is the possibility that previously charged impairments may need reversing where store trading conditions have improved.</p> <p>We focused on this area because of the judgemental factors involved in testing for impairment and the significant carrying value of freehold property.</p> <p>Management considers each store to be a cash generating unit (‘CGU’) and has calculated the recoverable amount of each CGU as the higher of value in use and fair value less costs of disposal.</p> <p><b>Value in use</b> Value in use is based on discounted future cash flow forecasts, requiring management to make judgements on certain key inputs including, for example, discount rates and long term growth rates.</p> <p><b>Fair value less costs of disposal</b> Fair value less costs of disposal is estimated by management based on their knowledge of individual stores, likely demand from grocers or other retailers in the event those stores were for sale and is further informed by a valuation performed by a third party valuer. The key judgements made by the Directors in this fair value calculation relate to the estimated rental values and the yields of the stores.</p> <p>Management has calculated that an impairment charge of £147m is required as at 29 January 2017. A release of impairment charged in previous years of £191m has also been calculated following an improvement in the performance of certain stores.</p>	<p><b>Value in use</b> We have obtained the Group’s approved budget (upon which forecasts underlying the value in use calculations are based). Our audit procedures included an assessment of management’s discounted cash flow models. We tested the mathematical accuracy of the calculations derived from each forecast model and assessed key inputs in the calculations, such as the discount rate of 9%, by reference to management’s forecasts, industry reports and our valuation experts. We focused on these key assumptions because small changes can have a material impact on the value in use assessment and any resultant impairment charge. We found, based on our audit work, that the key assumptions used by management were supportable and appropriate in light of the current environment.</p> <p><b>Fair value less costs of disposal</b> Management has determined its own view of estimated rental values and yields for each store used in their calculation of market values. Management derived these assumptions having considered available information such as industry data on market conditions, purchase offers recently received for properties and information from an independent third party valuer. We evaluated management’s supporting information, and assessed this using our own internal experts, with a particular focus on the assumptions and methodology used, obtaining third party evidence and market data to corroborate the assumptions.</p> <p>We also evaluated the competency, qualifications, experience and objectivity of management’s property valuation experts and noted no issues. We determined that the valuations performed by management are reasonable.</p> <p>In addition, we evaluated the adequacy of the disclosures made in note 3.3 of the financial statements, including those regarding the key assumptions and sensitivities to changes in such assumptions by comparing the disclosures against the requirements of IAS 36 ‘Impairment of assets’ and found them to be consistent.</p>

## Independent auditors' report continued

# Independent auditors' report to the members of Wm Morrison Supermarkets PLC continued

Area of focus	How our audit addressed the area of focus
<p><b>Onerous lease provisions and onerous property contracts</b> Refer to page 64 (critical accounting judgements and estimates) and note 5.5 (provisions).</p> <p><b>Onerous lease provisions</b> Accounting standards require management to assess the Group's leasehold properties to identify where the expected future benefits from a property are less than the future lease commitments which would indicate that an onerous lease provision is required. Under IAS 37 'Provisions, contingent liabilities and contingent assets' such a provision is made for the unavoidable costs of the contract, defined in the standard as the 'least net cost of exit'.</p> <p>We focused on this area because of the judgements required to be made by management in identifying those stores requiring an onerous lease provision and the assumptions used in the models, such as the discount rate and those used in developing the associated cash flow forecasts. We also note that management judgement is required to assess the level of provision for lease guarantees in respect of My Local stores previously disposed of.</p> <p><b>Onerous property contracts</b> The Group has a number of sites that it is contractually committed to purchase as well as other property related contracts. For example, where management believes that no economic benefit would result from developing the store, a provision is made. There are judgements involved in determining the expected realisable value of these sites and therefore this has been an area of focus during our audit.</p>	<p><b>Onerous lease provisions</b> Having considered the possibility of impairment in the value of freehold properties (see above), we also tested management's calculations in respect of leasehold stores where the estimated future benefits are not expected to exceed the future lease commitments, resulting in an onerous lease.</p> <p>We obtained management's onerous lease model, which includes all leased stores, and tested the accuracy and completeness of key data by agreeing inputs such as individual store cash flows. This helps provide an insight into store profitability. We agreed lease expiry dates for a sample of stores to the original signed lease agreements, noting no issues.</p> <p>We obtained the Group's approved budget (upon which forecasts are based) and assessed the principles of the Group's discounted cash flow model, noting no exceptions. We tested the mathematical accuracy of the calculation derived from each forecast model and assessed key inputs in the calculations such as revenue growth and discount rate, by reference to management's forecasts, analyst reports and our own Real Estate experts, with no issues noted. The discount rate used is consistent with the Group's cost of debt and the requirements of IAS 37.</p> <p>We obtained management's calculation of the required provision for former My Local leases which reverted back to the Group in a prior year. We assessed the principles of the model and tested key inputs such as lease commitment information and sub-let assumptions, with no issues noted.</p> <p><b>Onerous property contracts</b> In respect of onerous property contracts, we obtained original contracts and management's calculations and considered the accuracy of these provisions by performing recalculations and testing key inputs such as estimates of contract exit costs and contractual payments due. We considered the completeness of these provisions by reviewing documentation in relation to these contracts. We found no issues in this area.</p> <p><b>Disclosures</b> We read the disclosures within the Annual Report in respect of onerous lease and contract provisions, and, based on our work, determined that they are consistent with accounting standards.</p>

**Area of focus****Commercial income and promotional funding**

Refer to note 1.1 (accounting policies), page 64 (critical accounting judgements and estimates) and notes 1.6 (operating profit).

**Commercial income**

The Group has two categories of commercial income: marketing and advertising funding, and volume based rebates on purchases.

Commercial income is recognised as a deduction from cost of sales and is earned over the period of the contractual agreements with individual suppliers, as disclosed in the Group's accounting policy on page 65. The total income recognised in the income statement in a year is based on the expected entitlement earned up to the balance sheet date under each supplier agreement. It requires management to apply judgement based on the contractual terms in place with each of its suppliers, together with estimates of amounts the Group is entitled to where transactions span the financial period end.

The relative level of judgement in each category of commercial income is considered below:

**Commercial income – marketing and advertising funding**

This income is varied with regards to the nature and timing of the activity to which it relates, and is recognised in accordance with written agreements with suppliers. This income is based on specific agreements, and its recognition requires limited judgement or estimation by management in determining the amount that the Group is entitled to. Our focus was on assessing whether a written agreement for the marketing and advertising funding existed, whether the relevant marketing or advertising had taken place and whether the income recognised was recorded in the appropriate period.

**Commercial income – volume based rebates**

Volume based rebates are driven by the Group achieving purchase volume targets set by individual suppliers for specific products over a pre-determined period. There is therefore judgement involved in estimating the volume of purchases, particularly where rebate agreements span a financial period-end. In order to narrow this judgement, management endeavours to structure agreements to coincide with the Group's financial period-end, thereby reducing or eliminating the degree of estimation. In instances where the rebate agreement does not fully coincide with the period-end, the key judgement that we focused on was the estimate of commercial income to be accrued at the period end.

**Promotional funding**

The Group separately recognises promotional funding on promotions that are partially funded by suppliers.

The majority of promotional funding is an automated deduction from cost of sales, triggered when a sale is recognised. The funding is recognised when the transaction occurs in accordance with the terms of supplier agreements. The amount receivable is wholly based on sales volumes achieved, multiplied by rates agreed with each supplier up-front. There are also some elements of promotional funding which include a manual element to the calculation and invoicing. We focused on promotional funding because of the significance of the amounts to the Group's gross profit, the significant number of transactions and agreements in place with suppliers covering a range of periods and the industry-wide focus on this area of accounting. However, we note that the level of judgement and subjectivity in the calculations is lower because of the level of automation. Our focus was on whether a written agreement for the promotional funding existed, whether the relevant promotion had taken place, and whether the funding recognised was recorded in the appropriate period.

**How our audit addressed the area of focus**

Our audit work in respect of commercial income and promotional funding comprised a combination of controls testing, substantive testing of a sample of income and funding recognised during the period, testing of amounts recognised in the balance sheet and an assessment of the Group's disclosures in this area. Each element of our work is considered in more detail below.

**Controls testing**

Our controls work encompassed understanding, evaluating and testing management's key controls in respect of the recognition of both commercial income and promotional funding. These key controls included the monitoring of invoices raised and the accuracy of confirmations from suppliers. We found no significant deficiencies in these key controls, and our testing of management's key system controls contributed to our evidence in determining whether commercial income and promotional funding had been recorded appropriately and in the correct period.

**Income statement testing**

We tested a sample of commercial income and promotional funding to supporting documentation including supplier agreements. We requested confirmations directly from suppliers in respect of a sample of commercial income and manual promotional funding across a large number of suppliers. The confirmations received, and documentations reviewed, allowed us to evaluate whether commercial income or promotional funding had been appropriately recognised in the period. No exceptions arose from this work.

We also analysed commercial income and promotional funding recognised each month and compared it to the previous period to identify whether there were any unusual trends in the amounts or timing of commercial income and promotional funding recognised in each period. We used a data analytics approach to identify any unusual items in the commercial income and promotional funding populations. Where unusual items were identified these were agreed to supporting documentation without exception.

**Balance sheet testing**

We wrote to a sample of suppliers, and obtained independent evidence of the value and timing of commercial income and promotional funding to evaluate whether it had been recognised in the correct period. We also agreed a sample of accrued income to evidence of post-year end invoicing. We performed cut-off procedures and credit note testing to provide further evidence to support the timing of the recognition of both commercial income and promotional funding. Cut-off work involved testing a sample of commercial income and promotional funding recognised both pre and post the period-end and evaluating by reference to documentation from suppliers that the timing of recognition was appropriate. We found no issues as a result of our audit procedures.

Our credit note testing focused on credit notes raised after the period-end in order to identify any instances of commercial income or promotional funding being subsequently reversed. We did not identify any exceptions from this work. We tested the recoverability of invoiced commercial income and promotional funding (unsettled balances included within trade debtors in note 5.3 to the financial statements and where the Group does not have the right of offset against trade creditors). This testing was performed by assessing the ageing of both outstanding commercial income and promotional funding debtors together with understanding the details of any disputes, and obtaining explanations from management to assess whether any provisions were appropriate. We also considered management's Key Performance Indicators in this analysis. No exceptions were noted.

**Disclosures**

We read the disclosures within the Annual Report in respect of commercial income and promotional funding and, based on our work, determined that they are consistent with accounting standards and the guidance on the reporting of complex supplier arrangements issued by the Financial Reporting Council.

## Independent auditors' report continued

# Independent auditors' report to the members of Wm Morrison Supermarkets PLC continued

### Area of focus

#### Impairment and capitalisation of intangible assets

Refer to page 64 (critical accounting judgements and estimates) and note 3.2 (goodwill and intangible assets).

The Group balance sheet includes capitalised intangible assets of £445m, of which the majority relates to software development costs incurred in connection with the Group's technology improvement programme, details of which are shown on page 76 of the Annual Report. The Group has developed a proportion of its own software and systems that are used in the business.

We focused on this area because in light of the continued development of new software and systems, judgement is required to assess whether the carrying value of the existing capitalised software or systems is impaired.

In addition, some judgement is required with regards to the nature and extent of costs capitalised in assessing whether the criteria, set out in accounting standards, required for capitalisation of such costs have been met.

### How our audit addressed the area of focus

We obtained management's assessment as to whether the development of new software or systems superseded or impaired any of the existing assets on the balance sheet. We also applied our own understanding of both new and existing projects and considered whether, in our view, any existing software was no longer in use or whether its life had been shortened by development activity. We found no such items.

We re-visited the expected costs budgeted by management within the cost benefit analysis and compared them to actual outcomes in the current period and we assessed the future expected benefits of the projects, with no issues identified from our work.

We tested a sample of costs capitalised in the period to assess whether these had been appropriately treated in line with the Group's accounting policy and accounting standards, most notably IAS 38 'Intangible assets'. We met with management responsible for particular costs to obtain an understanding of the associated projects and to independently assess whether project costs met the criteria for capitalisation as set out in accounting standards. We found the explanations obtained from management to be consistent with our understanding of developments in the business and supported management's assessment that the costs met the relevant capitalisation criteria.

Where external third party contractors were used, we agreed the hours and charge out rates to the invoices issued by the contractor, and assessed whether the costs were directly related to a capital project, with no exceptions noted.

To determine whether internal employee costs were directly attributable to projects, we obtained listings of hours worked on individual projects for the employment costs capitalised. We selected a sample of the individual hours recorded and obtained an understanding of the work performed by the employee. We also checked that the hours charged equated to the value of costs capitalised by comparing the proportion of costs capitalised to the employee's salary. No exceptions were noted from this work.

We read the disclosures within the Annual Report in respect of intangible assets, and, based on our work, determined that they are consistent with accounting standards.

Overall we found that the costs capitalised were supportable and consistent with the requirements of accounting standards for capitalising such costs. No material impairment of the intangible assets was identified from our work.

#### Stock valuation

Refer to note 1.1 (accounting policies), page 64 (critical accounting judgements and estimates) and note 5.2 (stock).

The valuation of stock of £614m (2016: £616m) was focused on because of the nature of the judgements made by management when assessing the level of provisions required. As disclosed in note 5.1 to the financial statements, provisions are held against stock based on an assessment of specific risks identified within the stock balance. The most significant categories of risk include estimated losses related to shrinkage and obsolescence, a deduction for unearned commercial income (as the stock related to that commercial income and promotional funding has yet to be sold) and other specific provisions based on identified risks. When the stock is sold, the commercial income and/or promotional funding is recognised in the income statement.

As stock is counted by the Group on a cyclical basis, rather than in full at the period end date, the shrinkage provision at 29 January 2017 contains a degree of estimation.

We attended stock counts throughout the period at a sample of the Group's supermarkets, petrol forecourts, distribution centres and manufacturing locations. In addition to performing sample test counts, we assessed the effectiveness of the count controls in operation. We also evaluated the results of other cycle counts performed by management and third parties throughout the period to assess the level of count variances. We found no material variances or count control deficiencies across these sites.

We tested management's shrinkage assumptions determined by the count procedures and the comparison of this to historical data. The historical data included the results of the recent counts at each location, and our procedures did not identify any significant unusual fluctuations in the data.

The obsolescence provision is calculated by applying a judgemental percentage to the period end stock levels, with this judgement being informed by management's view of the current stock profile and expected stock life. We considered this provision by assessing the explanations provided by management on the current profile and expected stock life noting no issues.

We tested the unearned commercial income deduction by verifying the inputs of the calculation and methodology behind the provision with no issues noted.

We have assessed the other specific provisions with reference to the risks identified by management and noted no issues.

#### Disclosures

We read the disclosures within the Annual Report in respect of inventory, and, based on our work, determined that they are consistent with accounting standards.



**Area of focus****Pension accounting**

Refer to note 1.1 (accounting policies), page 64 (critical accounting judgements and estimates) and note 8 (pensions).

We have focused on the valuation of the Group's defined benefit pension schemes because of the level of judgement required in determining the year-end valuation. In addition, the size of the gross assets (£4,674m) and liabilities (£4,402m) within the schemes are significant and material.

The Group also carries a provision for backdated pension contributions related to the set-up of a new defined contribution scheme which was formed in the year ended 31 January 2016 and requires further judgement in determining the value of the provision at 29 January 2017.

**How our audit addressed the area of focus**

We obtained the IAS 19 valuation reports produced by the Group's actuaries. We used our own actuarial experts to assess the judgemental assumptions used within the reports to form the valuation of the pension schemes' liabilities, such as discount rate, inflation and mortality rates. We obtained the detailed reports underlying the valuation of the schemes' assets and agreed the valuations to third party confirmations. We assessed the membership data used in valuing the schemes' liabilities and tested any significant changes since the last valuation. We agreed a sample of contributions made by the Group to bank statements.

We have no exceptions to report as a result of this testing.

The net surplus position of the schemes at 29 January 2017 was £272m. We have reviewed management's assessment of the right to recognise the net surplus in two of the three schemes under the requirements of IFRIC 14, including inspecting updated legal advice, and are satisfied that it is appropriate to recognise the net asset on the balance sheet. The third scheme (RSP) is recognised as a net liability and therefore this aspect of IFRIC 14 is not applicable.

We obtained management's latest assessment of the backdated pension contribution provision at 29 January 2017, including evidence of discussions with stakeholders in the period. We are satisfied that the value of the provision is appropriate.

**How we tailored the audit scope**

We tailored the scope of our audit to ensure that we performed enough work to be able to give an opinion on the financial statements as a whole, taking into account the geographic structure of the Group, the accounting processes and controls, and the industry in which the Group operates.

The Group's accounting process is structured around a Group finance function at its head office in Bradford. Within the head office, supporting finance functions exist for each of the key business operating areas (Group, Supermarkets, Manufacturing and Property), and these report to the Group finance team as appropriate. The Group also maintains local finance teams at each of its key Manufacturing sites.

All work was conducted in the UK by the same Group audit team, other than Group reporting from a PwC component team from the UK firm auditing the complete financial information of a UK Manufacturing subsidiary, Wm Produce Limited.

Where the work was performed by the component auditor, we determined the level of involvement we needed to have in their audit work to be able to conclude whether sufficient appropriate audit evidence had been obtained as a basis for our opinion on the Group financial statements as a whole. As part of our year-end audit procedures, we held detailed discussions with the UK Manufacturing component audit team, including holding a detailed planning meeting with them and attending the audit clearance meeting with management.

Taken together, the territories and functions where we performed our work accounted for 99% of Group revenues.

**Materiality**

The scope of our audit was influenced by our application of materiality. We set certain quantitative thresholds for materiality. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures on the individual financial statement line items and disclosures and in evaluating the effect of misstatements, both individually and on the financial statements as a whole.

Based on our professional judgement, we determined materiality for the financial statements as a whole as follows:

Overall Group materiality	£16.85m (2016: £12m).
How we determined it	5% of underlying profit before tax.
Rationale for benchmark applied	Consistent with last year, we applied this benchmark because, in our view, this is the most relevant metric against which the performance of the Group is most commonly measured. Underlying profit is defined by management as profit before impairment, onerous contracts and other items that do not relate to the Group's principal activities on an ongoing basis, profit/loss arising on disposal and exit of properties and sale of businesses and investments and IAS 19 pension interest, at a normalised tax rate, as reconciled in note 1.4 of the Group financial statements.

We agreed with the Audit Committee that we would report to them misstatements identified during our audit above £825,000 (2016: £600,000) as well as misstatements below that amount that, in our view, warranted reporting for qualitative reasons.

## Independent auditors' report continued

# Independent auditors' report to the members of Wm Morrison Supermarkets PLC continued

### Going concern

Under the Listing Rules we are required to review the Directors' statement, set out on page 47, in relation to going concern. We have nothing to report having performed our review.

Under ISAs (UK & Ireland) we are required to report to you if we have anything material to add or to draw attention to in relation to the Directors' statement about whether they considered it appropriate to adopt the going concern basis in preparing the financial statements. We have nothing material to add or to draw attention to.

As noted in the Directors' statement, the Directors have concluded that it is appropriate to adopt the going concern basis in preparing the financial statements. The going concern basis presumes that the Group and Company have adequate resources to remain in operation, and that the Directors intend them to do so, for at least one year from the date the financial statements were signed. As part of our audit we have concluded that the Directors' use of the going concern basis is appropriate. However, because not all future events or conditions can be predicted, these statements are not a guarantee as to the Group's and Company's ability to continue as a going concern.

### Other required reporting

#### Consistency of other information and compliance with applicable requirements

##### Companies Act 2006 reporting

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the Strategic report and the Directors' report for the financial period for which the financial statements are prepared is consistent with the financial statements; and
- the Strategic report and the Directors' report have been prepared in accordance with applicable legal requirements.

In addition, in light of the knowledge and understanding of the Group, the Company and their environment obtained in the course of the audit, we are required to report if we have identified any material misstatements in the Strategic report and the Directors' report. We have nothing to report in this respect.

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the Corporate governance statement set out on pages 29 and 30 with respect to internal control and risk management systems and about share capital structures is consistent with the financial statements and has been prepared in accordance with applicable legal requirements; and
- the information given in the Corporate governance statement set out on page 23 with respect to the Group's Corporate Governance Code and practices and about its administrative, management and supervisory bodies complies with rules 7.2.2, 7.2.3 and 7.2.7 of the Disclosure Guidance and Transparency Rules sourcebook of the Financial Conduct Authority.

In addition, in light of the knowledge and understanding of the Group, the Company and their environment obtained in the course of the audit, we are required to report if we have identified any material misstatements in the information referred to above in the Corporate governance statement. We have nothing to report in this respect.

#### ISAs (UK & Ireland) reporting

Under ISAs (UK & Ireland) we are required to report to you if, in our opinion:

- |   |  |
|---|--|
| <ul style="list-style-type: none"> <li>• information in the Annual Report is:               <ul style="list-style-type: none"> <li>– materially inconsistent with the information in the audited financial statements; or</li> <li>– apparently materially incorrect based on, or materially inconsistent with, our knowledge of the Group and Company acquired in the course of performing our audit; or</li> <li>– otherwise misleading.</li> </ul> </li> </ul>   | <ul style="list-style-type: none"> <li>• We have no exceptions to report.</li> </ul> |
| <ul style="list-style-type: none"> <li>• the statement given by the Directors on page 49, in accordance with provision C.1.1 of the UK Corporate Governance Code (the 'Code'), that they consider the Annual Report taken as a whole to be fair, balanced and understandable and provides the information necessary for members to assess the Group's and Company's position and performance, business model and strategy is materially inconsistent with our knowledge of the Group and Company acquired in the course of performing our audit.</li> </ul> | <ul style="list-style-type: none"> <li>• We have no exceptions to report.</li> </ul> |
| <ul style="list-style-type: none"> <li>• the section of the Annual Report on page 28, as required by provision C.3.8 of the Code, describing the work of the Audit Committee does not appropriately address matters communicated by us to the Audit Committee.</li> </ul>   | <ul style="list-style-type: none"> <li>• We have no exceptions to report.</li> </ul> |

### The Directors' assessment of the prospects of the Group and of the principal risks that would threaten the solvency or liquidity of the Group

Under ISAs (UK & Ireland) we are required to report to you if we have anything material to add or to draw attention to in relation to:

<ul style="list-style-type: none"> <li>the Directors' confirmation on page 17 of the Annual Report, in accordance with provision C.2.1 of the Code, that they have carried out a robust assessment of the principal risks facing the Group, including those that would threaten its business model, future performance, solvency or liquidity.</li> </ul>	We have nothing material to add or to draw attention to.
<ul style="list-style-type: none"> <li>the disclosures in the Annual Report that describe those risks and explain how they are being managed or mitigated.</li> </ul>	We have nothing material to add or to draw attention to.
<ul style="list-style-type: none"> <li>the Directors' explanation on page 30 of the Annual Report, in accordance with provision C.2.2 of the Code, as to how they have assessed the prospects of the Group, over what period they have done so and why they consider that period to be appropriate, and their statement as to whether they have a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, including any related disclosures drawing attention to any necessary qualifications or assumptions.</li> </ul>	We have nothing material to add or to draw attention to.

Under the Listing Rules we are required to review the Directors' statement that they have carried out a robust assessment of the principal risks facing the Group and the Directors' statement in relation to the longer-term viability of the Group. Our review was substantially less in scope than an audit and only consisted of making inquiries and considering the Directors' process supporting their statements; checking that the statements are in alignment with the relevant provisions of the Code; and considering whether the statements are consistent with the knowledge acquired by us in the course of performing our audit. We have nothing to report having performed our review.

### Adequacy of accounting records and information and explanations received

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

- we have not received all the information and explanations we require for our audit; or
- adequate accounting records have not been kept by the Group, or returns adequate for our audit have not been received from branches not visited by us; or
- the Group financial statements and the part of the Directors' remuneration report to be audited are not in agreement with the accounting records and returns.

We have no exceptions to report arising from this responsibility.

### Directors' remuneration

#### Directors' remuneration report – Companies Act 2006 opinion

In our opinion, the part of the Directors' remuneration report to be audited has been properly prepared in accordance with the Companies Act 2006.

#### Other Companies Act 2006 reporting

Under the Companies Act 2006 we are required to report to you if, in our opinion, certain disclosures of Directors' remuneration specified by law are not made. We have no exceptions to report arising from this responsibility.

### Corporate governance statement

Under the Companies Act 2006 we are required to report to you if, in our opinion, a Corporate governance statement has not been prepared by the Group. We have no exceptions to report arising from this responsibility.

Under the Listing Rules we are required to review the part of the Corporate governance statement relating to ten further provisions of the Code. We have nothing to report having performed our review.

### Responsibilities for the financial statements and the audit

#### Our responsibilities and those of the Directors

As explained more fully in the Directors' responsibilities statement set out on page 49, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view.

Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and ISAs (UK & Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the Group's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

**Independent auditors'  
report** continued

## Independent auditors' report to the members of Wm Morrison Supermarkets PLC continued

### What an audit of financial statements involves

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of:

- whether the accounting policies are appropriate to the Group's and the Company's circumstances and have been consistently applied and adequately disclosed;
- the reasonableness of significant accounting estimates made by the Directors; and
- the overall presentation of the financial statements.

We primarily focus our work in these areas by assessing the Directors' judgements against available evidence, forming our own judgements, and evaluating the disclosures in the financial statements.

We test and examine information, using sampling and other auditing techniques, to the extent we consider necessary to provide a reasonable basis for us to draw conclusions. We obtain audit evidence through testing the effectiveness of controls, substantive procedures or a combination of both.

In addition, we read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report. With respect to the Strategic report, Directors' report and Corporate governance statement, we consider whether those reports include the disclosures required by applicable legal requirements.

### Andrew Paynter (Senior Statutory Auditor)

for and on behalf of PricewaterhouseCoopers LLP

Chartered Accountants and Statutory Auditors

Leeds

8 March 2017

# Consolidated statement of comprehensive income

## 52 weeks ended 29 January 2017

	Note	2017 £m	2016 £m
<b>Revenue</b>	1.2	16,317	16,122
Cost of sales		(15,713)	(15,505)
<b>Gross profit</b>		604	617
Other operating income		76	72
Profit/loss on disposal and exit of properties and sale of businesses and investments	14, 4.3, 4.5	32	97
Administrative expenses		(244)	(472)
<b>Operating profit</b>	1.6	468	314
Finance costs	6.2	(160)	(112)
Underlying finance costs	6.2	(104)	(112)
Adjustments for:			
Costs associated with the repayment of borrowings	1.4	(56)	–
Finance income	6.2	15	13
Share of profit of joint venture (net of tax)	4.2	2	2
<b>Profit before taxation</b>		325	217
Analysed as:			
Underlying profit before tax		337	242
Adjustments for:			
Impairment and provision for onerous contracts	1.4	6	(87)
Profit/loss on disposal and exit of properties	1.4	19	131
Profit arising on disposal of investment	14, 4.3	13	–
Loss arising on disposal of business	14, 4.5	–	(34)
Costs associated with the repayment of borrowings	1.4	(56)	–
Pension scheme set-up costs	14, 8.6	–	(35)
Net pension income	14, 8.2	8	–
Other exceptional costs	1.4	(2)	–
		325	217
Taxation	2.2	(20)	5
<b>Profit for the period attributable to the owners of the Company</b>		305	222
<b>Other comprehensive income</b>			
<b>Items that will not be reclassified to profit or loss:</b>			
Remeasurement of defined benefit pension schemes	8.2	86	236
Tax on defined benefit pension schemes	2.3	(17)	(47)
		69	189
<b>Items that may be reclassified subsequently to profit or loss:</b>			
Cash flow hedging movement		30	16
Items reclassified from hedging reserve in relation to repayment of borrowings	1.4	6	–
Tax on items that may be reclassified subsequently to profit or loss	2.3	1	(4)
Exchange differences on translation of foreign operations		(1)	1
		36	13
<b>Other comprehensive income for the period, net of tax</b>		105	202
<b>Total comprehensive income for the period attributable to the owners of the Company</b>		410	424
Earnings per share (pence)			
– basic	1.5	13.11	9.51
– diluted	1.5	12.95	9.47

# Consolidated balance sheet

## 29 January 2017

	Note	2017 £m	2016 £m
<b>Assets</b>			
<b>Non-current assets</b>			
Goodwill and intangible assets	3.2	445	483
Property, plant and equipment	3.3	7,227	7,161
Investment property	3.5	33	37
Pension asset	8.2	293	186
Investment in joint venture	4.2	56	63
Investments	4.3	–	31
Derivative financial assets	7.3	16	30
		<b>8,070</b>	<b>7,991</b>
<b>Current assets</b>			
Stock	5.2	614	616
Debtors	5.3	214	192
Derivative financial assets	7.3	22	12
Cash and cash equivalents	6.4	326	496
		<b>1,176</b>	<b>1,316</b>
Assets classified as held-for-sale	3.4	–	–
		<b>1,176</b>	<b>1,316</b>
<b>Liabilities</b>			
<b>Current liabilities</b>			
Creditors	5.4	(2,837)	(2,518)
Short term borrowings	6.3	–	(209)
Derivative financial liabilities	7.3	(3)	(17)
Current tax liabilities		(24)	(11)
		<b>(2,864)</b>	<b>(2,755)</b>
<b>Non-current liabilities</b>			
Borrowings	6.3	(1,550)	(2,003)
Derivative financial liabilities	7.3	(5)	(55)
Pension liability	8.2	(21)	–
Deferred tax liabilities	2.3	(417)	(429)
Provisions	5.5	(326)	(309)
		<b>(2,319)</b>	<b>(2,796)</b>
<b>Net assets</b>		<b>4,063</b>	<b>3,756</b>
<b>Shareholders' equity</b>			
Share capital	6.5	234	234
Share premium	6.5	128	127
Capital redemption reserve	6.6	39	39
Merger reserve	6.6	2,578	2,578
Retained earnings and other reserves	6.6	1,084	778
<b>Total equity attributable to the owners of the Company</b>		<b>4,063</b>	<b>3,756</b>

The notes on pages 65 to 101 form part of these financial statements.

The financial statements on pages 59 to 101 were approved by the Board of Directors on 8 March 2017 and were signed on its behalf by:

**Trevor Strain**  
Chief Financial Officer

## Consolidated cash flow statement

52 weeks ended 29 January 2017

	Note	2017 £m	2016 £m
<b>Cash flows from operating activities</b>			
Cash generated from operations	5.6	1,113	1,026
Interest paid		(100)	(99)
Taxation paid		(35)	(41)
<b>Net cash inflow from operating activities</b>		<b>978</b>	<b>886</b>
<b>Cash flows from investing activities</b>			
Interest received		6	4
Dividends received from joint venture	10.1	8	8
Proceeds from the sale of property, plant and equipment		79	300
Proceeds from the sale of businesses and investments	4.3, 4.5	44	20
Purchase of property, plant and equipment, investment property and assets classified as held-for-sale		(374)	(266)
Purchase of intangible assets		(45)	(99)
<b>Net cash outflow from investing activities</b>		<b>(282)</b>	<b>(33)</b>
<b>Cash flows from financing activities</b>			
Purchase of shares in subsidiary	4.4	–	(3)
Purchase of own shares for trust	6.5	(5)	(13)
Net repayment of revolving credit facility		–	(320)
Repayment of borrowings		(729)	(10)
Proceeds on settlement of derivative financial instruments		37	–
Costs incurred on repayment of borrowings		(42)	–
Dividends paid	1.8	(118)	(260)
<b>Net cash outflow from financing activities</b>		<b>(857)</b>	<b>(606)</b>
<b>Net (decrease)/increase in cash and cash equivalents</b>		<b>(161)</b>	<b>247</b>
Cash and cash equivalents at start of period		487	240
<b>Cash and cash equivalents at end of period</b>	6.4	<b>326</b>	<b>487</b>

### Reconciliation of net cash flow to movement in net debt in the period

	Note	2017 £m	2016 £m
Net (decrease)/increase in cash and cash equivalents		(161)	247
Cash outflow from decrease in debt		692	330
Non-cash movements		21	17
Opening net debt		(1,746)	(2,340)
<b>Closing net debt</b>	6.4	<b>(1,194)</b>	<b>(1,746)</b>

## Consolidated statement of changes in equity

52 weeks ended 29 January 2017

	Note	Attributable to the owners of the Company						Total equity £m
		Share capital £m	Share premium £m	Capital redemption reserve £m	Merger reserve £m	Hedging reserve £m	Retained earnings £m	
<b>Current period</b>								
At 1 February 2016		234	127	39	2,578	(10)	788	3,756
Profit for the period		–	–	–	–	–	305	305
Other comprehensive income/(expense):								
Cash flow hedging movement		–	–	–	–	30	–	30
Items reclassified from hedging reserve in relation to repayment of borrowings	1.4	–	–	–	–	6	–	6
Exchange differences on translation of foreign operations		–	–	–	–	–	(1)	(1)
Remeasurement of defined benefit pension schemes	8.2	–	–	–	–	–	86	86
Tax in relation to components of other comprehensive income	2.3	–	–	–	–	(8)	(8)	(16)
Total comprehensive income for the period		–	–	–	–	28	382	410
Purchase of trust shares	6.5	–	–	–	–	–	(5)	(5)
Proceeds and settlements of employee share award	6.5	–	1	–	–	–	(1)	–
Employee share option schemes:								
Share-based payments	1.7	–	–	–	–	–	20	20
Dividends	1.8	–	–	–	–	–	(118)	(118)
Total transactions with owners		–	1	–	–	–	(104)	(103)
<b>At 29 January 2017</b>		<b>234</b>	<b>128</b>	<b>39</b>	<b>2,578</b>	<b>18</b>	<b>1,066</b>	<b>4,063</b>

	Note	Attributable to the owners of the Company						Total equity £m
		Share capital £m	Share premium £m	Capital redemption reserve £m	Merger reserve £m	Hedging reserve £m	Retained earnings £m	
<b>Prior period</b>								
At 2 February 2015		234	127	39	2,578	(22)	638	3,594
Profit for the period		–	–	–	–	–	222	222
Other comprehensive income/(expense):								
Cash flow hedging movement		–	–	–	–	16	–	16
Exchange differences on translation of foreign operations		–	–	–	–	–	1	1
Remeasurement of defined benefit pension schemes	8.2	–	–	–	–	–	236	236
Tax in relation to components of other comprehensive income	2.3	–	–	–	–	(4)	(47)	(51)
Total comprehensive income for the period		–	–	–	–	12	412	424
Purchase of trust shares	6.5	–	–	–	–	–	(13)	(13)
Employee share option schemes:								
Share-based payments	1.7	–	–	–	–	–	11	11
Dividends	1.8	–	–	–	–	–	(260)	(260)
Total transactions with owners		–	–	–	–	–	(262)	(262)
<b>At 31 January 2016</b>		<b>234</b>	<b>127</b>	<b>39</b>	<b>2,578</b>	<b>(10)</b>	<b>788</b>	<b>3,756</b>



## General information

### Company information

Wm Morrison Supermarkets PLC is a public limited company incorporated in the United Kingdom under the Companies Act 2006 (Registration number 358949). The Company is domiciled in the United Kingdom and its registered address is Hilmore House, Gain Lane, Bradford, BD3 7DL, United Kingdom.

### Basis of preparation

The financial statements have been prepared for the 52 weeks ended 29 January 2017 (2016: 52 weeks ended 31 January 2016) in accordance with International Financial Reporting Standards (IFRS) and International Financial Reporting Standards Interpretation Committee (IFRS IC) interpretations as adopted by the European Union and with those parts of the Companies Act 2006 applicable to companies reporting under IFRS. IFRS and IFRS IC interpretations are issued by the International Accounting Standards Board (the IASB) and must be adopted into European Union law, referred to as endorsement, before they become mandatory under the IAS Regulation.

The financial statements have been prepared on a going concern basis.

The financial statements are presented in pounds sterling, rounded to the nearest million, except in some instances, where it is deemed relevant to disclose the amounts up to two decimal places. They are drawn up on the historical cost basis of accounting, except as disclosed in the accounting policies set out within these financial statements.

The Group's accounting policies have, unless otherwise stated, been applied consistently to all periods presented in these financial statements.

### Accounting reference date

The accounting period of the Group ends on the Sunday falling between 29 January and 4 February each year.

### New IFRS and amendments to IAS and interpretations

There have been no significant changes to accounting under IFRS which have affected the Group's results. The Group has considered the following amendments to published standards that are effective for the first time for the 52 weeks ended 29 January 2017 and concluded that they are either not relevant to the Group or they do not have a significant impact on the Group's financial statements. These amendments are:

- Amendments to IAS 1 'Presentation of Financial Statements';
- 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; and
- Annual improvements 2012-2014.

There are a number of standards and interpretations issued by the IASB that are effective for financial statements after this reporting period. These are:

- IFRS 9 'Financial Instruments' was published in July 2014 and will be effective for the Group from the period beginning 5 February 2018. The standard is applicable to financial assets and financial liabilities, and covers the classification, measurement, impairment and de-recognition of financial assets and financial liabilities together with a new hedge accounting model. Work on the impact of the new recognition, impairment and general hedge accounting requirements is in its early stages and we are assessing whether any changes to the Group's systems and processes are required to aid the implementation of the standard. It is not yet practicable to quantify the effect of IFRS 9 on the Group;
- IFRS 15 'Revenue from Contracts with Customers' will be effective for the Group from the period beginning 5 February 2018, replacing IAS 18 'Revenue', IAS 11 'Construction contracts' and related interpretations. The standard establishes a principles-based approach for revenue recognition and is based on the concept of recognising revenue when a customer obtains control of a goods or service and has the ability to direct the use and obtain the benefits from the goods or services. It applies to all contracts with customers, except those in the scope of other standards. It replaces the separate models for goods, services and construction contracts under the current accounting standards. Based on the Group's preliminary assessment from work performed to date, the Group believes that the adoption of IFRS 15 will not have a material impact on the consolidated financial statements but work is still ongoing to fully quantify its impact, with particular focus on treatment of the Group's customer loyalty arrangements; and
- IFRS 16 'Leases' was published in January 2016 and will be effective for the Group from the period beginning 4 February 2019, replacing IAS 17 'Leases', subject to EU endorsement. The standard requires lessees to recognise assets and liabilities for all leases unless the lease term is 12 months or less or the underlying asset is of low value. IFRS 16 represents a significant change in the accounting and reporting of leases and it will primarily change the balance sheet as well as impacting the income statement and lessee reporting as disclosed in note 6.8. Accounting requirements for lessors as disclosed in note 3.6 will be substantially unchanged from IAS 17. The Group is in the process of quantifying the impact of the new standard. The new standard is likely to have an impact on the Group's results and a material impact on the balance sheet, as the majority of arrangements that are currently accounted for as operating leases will come onto the Group's balance sheet. However, it is not yet practicable to fully quantify the effect of IFRS 16 on these consolidated financial statements.

## General information continued

### Basis of consolidation

Subsidiaries (including partnerships) are all entities over which the Group has control. The Group controls an entity when it has power over that entity, is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are deconsolidated from the date the control ceases. The financial statements of subsidiaries used in the consolidation are prepared for the same reporting period as the Company and are based on consistent accounting policies. Intra-group balances and any unrealised gains and losses or income and expenses arising from intra-group transactions are eliminated on consolidation.

### Foreign currencies

Transactions in foreign currencies are recorded at the rates of exchange at the dates of the transactions. At each balance sheet date, monetary assets and liabilities that are denominated in foreign currency are retranslated at the rates of exchange at the balance sheet date. Gains and losses arising on retranslation are included in the income statement for the period.

### Critical accounting judgements and estimates

The judgements that have the most significant effect on the amounts recognised in these financial statements, and sources of estimation uncertainty that have a significant risk of resulting in material adjustment to carrying amounts in the next financial year, are:

- Impairment of property, plant and equipment and intangible assets and onerous property commitments (note 1.4, 3.1, 3.2, 3.3, 5.5);
- Commercial income (note 1.1, 1.6, 5.2, 5.3, 5.4);
- IT and intangible assets (note 3.2);
- Stock (note 5.1, 5.2); and
- Pensions (note 8).

These are also described within the Corporate governance report on page 29.

### Alternative Performance Measures

The Directors measure the performance of the Group based on a range of financial measures, including measures not recognised by EU-adopted IFRS. These alternative performance measures may not be directly comparable with other companies' alternative performance measures and the Directors do not intend these to be a substitute for, or superior to, IFRS measures. For definitions of the alternative performance measures used, see the Glossary on page 122.

# Notes to the Group financial statements

52 weeks ended 29 January 2017

## 1 Performance in the period

### 1.1 Accounting policies

#### Revenue recognition

##### Sale of goods in-store and online, and fuel

Revenue from the sale of goods in-store and online comprises cash from customers and excludes VAT. It is net of returns, colleague discounts, coupons, vouchers, 'More' points earned in-store and online, and the free element of multi-save transactions. Sale of fuel is recognised net of VAT and 'More' points earned on fuel. Revenue is recognised when transactions are completed in-store, or, in the case of food online, when goods are accepted by the customer on delivery.

##### Other sales

Other sales includes income from concessions and commissions based on the terms of the contract, and sales made direct to third party customers recognised on despatch of goods. Revenue collected on behalf of others is not recognised as revenue, other than the related commission. Sales are recorded net of VAT and intra-group transactions.

##### 'More' points

The fair value of 'More' points is determined to be the value to the customer of the points issued, adjusted for factors such as the expected redemption rate. The Group continues to assess the appropriateness of the expected redemption rates against actual redemptions.

The fair value is treated as a deduction from revenue at the time the points are issued, and is deferred until the rewards are redeemed by the customer in a future sale.

##### Cost of sales

Cost of sales consists of all costs of the goods being sold to the point of sale, net of promotional funding and commercial income, and includes property, manufacturing, warehouse and transportation costs. Store depreciation, store overheads and store-based employee costs are also allocated to cost of sales.

##### Promotional funding

Promotional funding refers to investment in the customer offer by suppliers by way of promotion. The calculation of funding is mechanical and system generated based on a funding level agreed in advance with the supplier. Funding is recognised as units are sold and invoiced in accordance with the specific supplier agreement. Funding is recorded effectively as a direct adjustment to the cost price of the product in the period. Funding is invoiced and collected through the year, shortly after the promotions have ended.

##### Commercial income

Commercial income is recognised as a deduction from cost of sales, based on the expected entitlement that has been earned up to the balance sheet date for each relevant supplier contract. The Group only recognises commercial income where there is documented evidence of an agreement with an individual supplier and when associated performance conditions are met.

The types of commercial income recognised by the Group, and the recognition policies are:

Type of commercial income	Description	Recognition
Marketing and advertising funding	Examples include income in respect of in-store marketing and point of sale, as well as funding for advertising.	Income is recognised over the period as set out in the specific supplier agreement. Income is invoiced once the performance conditions in the supplier agreement have been achieved.
Volume-based rebates	Income earned by achieving volume or spend targets set by the supplier for specific products over specific periods.	Income is recognised through the year based on forecasts for expected sales or purchase volumes, informed by current performance, trends, and the terms of the supplier agreement. Income is invoiced throughout the year in accordance with the specific supplier terms. In order to minimise any risk arising from estimation, supplier confirmations are also obtained to agree the final value to be recognised at year end, prior to it being invoiced.

Uncollected commercial income at the balance sheet date is classified within the financial statements as follows:

- **Creditors:** A large proportion of the Group's trading terms state that income due from suppliers is netted against amounts owing to that supplier. Any outstanding invoiced commercial income relating to these suppliers at the balance sheet date are included within trade payables. Any amounts received in advance of income being recognised are included in accruals and deferred income.
- **Debtors:** Where the trading terms described above do not exist, the Group classifies outstanding commercial income within trade debtors. Where commercial income is earned and not invoiced to the supplier at the balance sheet date, this is classified within accrued commercial income.
- **Stock:** The carrying value of stock is adjusted to reflect unearned elements of commercial income as the stock has not yet been sold. This income is subsequently recognised in cost of sales when the product has been sold.

# Notes to the Group financial statements continued

52 weeks ended 29 January 2017

## 1 Performance in the period continued

### 1.1 Accounting policies continued

In order to provide users of the financial statements with greater understanding in this area, additional income statement and balance sheet disclosure is provided in notes 1.6, 5.2, 5.3 and 5.4 to the financial statements.

#### Other operating income

Other operating income primarily consists of income not directly related to in-store and online grocery retailing and mainly comprises rental income from investment properties and income generated from the recycling of packaging.

#### Profit/loss on disposal and exit of properties

Profit/loss from the disposal and exit of properties includes gains and losses on disposal of property assets and other costs incurred by the Group following a decision to dispose, close or no longer purchase properties. Where the Group disposes of a property, this disposal transaction is accounted for upon unconditional exchange of contracts. Gains and losses are determined by comparing sale proceeds with the asset's carrying amount and are presented net of costs associated with disposal.

### 1.2 Revenue

	Like-for-like sales £m	Other £m	2017 Total £m	2016 Total £m
Sale of goods in stores and online	12,727	20	12,747	12,811
Fuel	3,351	–	3,351	3,124
Total store-based and online sales	16,078	20	16,098	15,935
Other sales	–	219	219	187
<b>Total revenue</b>	<b>16,078</b>	<b>239</b>	<b>16,317</b>	<b>16,122</b>

### 1.3 Segmental reporting

The Group's principal activity is that of retailing, derived from the UK. The Group is not reliant on any major customer for 1% or more of revenues.

The Group is required to determine and present its operating segments based on the way in which financial information is organised and reported to the chief operating decision-maker (CODM). The CODM has been identified as the Executive Committee as this makes the key operating decisions of the Group and is responsible for allocating resources and assessing performance.

Key internal reports received by the CODM, primarily the management accounts, focus on the performance of the Group as a whole. The operations of all elements of the business are driven by the retail sales environment and hence have fundamentally the same economic characteristics. All operational decisions made are focused on the performance and growth of the retail outlets and the ability of the business to meet the supply demands of the stores.

The Group has considered the overriding core principles of IFRS 8 'Operating segments' as well as its internal reporting framework, management and operating structure. In particular, the Group considered its retail outlets, the fuel sale operation, the manufacturing entities and online operations. The Directors' conclusion is that the Group has one operating segment, that of retailing.

#### Reconciliations of reportable segment revenues, profit or loss, assets and liabilities and other material items

Performance is measured by the CODM based on underlying profit before tax as reported in the management accounts. Management believes that this underlying profit measure is the most relevant in evaluating the results of the Group. This information and the reconciliation to the statutory position can be found in note 1.4. In addition, the management accounts present a Group balance sheet containing assets and liabilities.

## 1 Performance in the period continued

### 1.4 Underlying profit

The definition of underlying profit is defined in the Glossary on page 122.

The Directors consider that the underlying profit and underlying adjusted earnings per share measures referred to in the results provide useful information for shareholders on underlying trends and performance. The adjustments are made to reported profit/loss to: (a) remove impairment, provision for onerous contracts, or other items that do not relate to the Group's principal activities on an ongoing basis; (b) remove profit/loss arising on disposal and exit of properties and sale of businesses and investments; (c) remove the impact of pension volatility; and (d) apply a normalised tax rate of 25% (2016: 25%).

	2017 £m	2016 £m
Profit after tax	305	222
Add back: tax charge/(credit) for the period <sup>1</sup>	20	(5)
Profit before tax	325	217
Adjustments for:		
Impairment and provision for onerous contracts <sup>1</sup>	(6)	87
Profit/loss arising on disposal and exit of properties <sup>1</sup>	(19)	(131)
Profit arising on disposal of investment (note 4.3) <sup>1</sup>	(13)	–
Loss arising on disposal of convenience business (note 4.5) <sup>1</sup>	–	34
Costs associated with the repayment of borrowings <sup>1</sup>	56	–
Pension scheme set-up costs (note 8.6) <sup>1</sup>	–	35
Net pension income (note 8.2) <sup>1</sup>	(8)	–
Other exceptional costs <sup>1</sup>	2	–
<b>Underlying profit before tax</b>	<b>337</b>	<b>242</b>
Normalised tax charge at 25% (2016: 25%) <sup>1, 2</sup>	(84)	(61)
<b>Underlying profit after tax</b>	<b>253</b>	<b>181</b>
Underlying earnings per share (pence)		
– basic (note 1.5.2)	10.86	7.77
– diluted (note 1.5.2)	10.73	7.73

<sup>1</sup> Adjustments marked<sup>1</sup> decrease post-tax underlying earnings by £52m (2016: decrease of £41m), as shown in the reconciliation of earnings disclosed in note 1.5.2.

<sup>2</sup> Normalised tax is defined in the Glossary, see page 122 for details.

Following the Group's annual impairment and onerous contract review a net credit of £6m has been recognised, which is made up of £44m net impairment reversal and £38m charge in relation to provision for onerous contracts.

The net impairment reversal of £44m (£191m impairment reversal offset by £147m impairment charge) reflects fluctuations in store level performance (see note 3.3). This has been partially offset by a £38m additional charge relating to the Group's provision for onerous contracts primarily relating to onerous property contracts (see note 5.5). In the prior year the additional charge of £87m reflected changes in estimates related to provisions for stores in the new space pipeline.

Costs associated with the early repayment of borrowing facilities and other refinancing activities total £56m. This includes £33m relating to financing charges on redemption of financial instruments (primarily premiums), other fees incurred on the repayment of bonds and refinancing; write off of facility fees; the payment of £17m relating to the early settlement of the US Private Placement loan notes (USPP); and £6m relating to losses which had previously been recognised in reserves which have been reclassified to the income statement on termination of hedging arrangements.

Profits arising on disposal and exit of properties amounted to £19m (2016: £131m). A £13m profit has been recognised on the disposal of the Group's investment in Fresh Direct Inc (see note 4.3).

Other exceptional costs represent legal costs incurred in relation to cases which the Group pursued in respect of historic events. There are no contingent liabilities associated with these cases.

The 2016 underlying profit before tax included £60m relating to one-off restructuring costs. When adjusted to exclude these items, underlying profit before restructuring and tax for 2016 was £302m.

# Notes to the Group financial statements continued

## 52 weeks ended 29 January 2017

### 1 Performance in the period continued

#### 1.4 Underlying profit continued

The adjustments above are classified within the Consolidated statement of comprehensive income on the following lines:

- impairment and provision for onerous contracts has been included within administrative expenses;
- profit/loss arising on disposal and exit of properties, profit arising on disposal of investments and loss arising on disposal of convenience business are classified within profit/loss arising on disposal and exit of properties and sale of businesses and investments;
- pension scheme set-up costs and other exceptional costs are classified within administrative expenses;
- costs associated with the repayment of borrowings are classified within finance costs; and
- net pension income is included within finance income.

#### 2016/17 Impairment and provision for onerous contracts

Impairment and provision for onerous contracts resulted in a net credit of £6m. This includes a net impairment release of £44m (£191m impairment reversal offset by £147m impairment) and charge of £38m relating to provisions for onerous contracts (see notes 3.3 and 5.5).

#### 2015/16 Impairment and provision for onerous contracts

Impairment and provision for onerous contracts in 2015/16 totalled £87m including £52m relating to onerous leases and £35m in relation to onerous commitments for changes in estimates related to provisions for stores in the new space pipeline. No impairment was recognised during 2015/16.

#### 1.5 Earnings per share

Basic earnings per share (EPS) is calculated by dividing the earnings attributable to ordinary shareholders by the weighted average number of ordinary shares in issue during the period excluding shares held in trust. For diluted EPS, the weighted average number of ordinary shares in issue is adjusted to assume conversion of all potentially dilutive ordinary shares.

The Company has two (2016: two) classes of instrument that are potentially dilutive: those share options granted to employees where the exercise price is less than the average market price of the Company's ordinary shares during the period and contingently issuable shares under the Group's long term incentive plans (LTIP).

##### 1.5.1 Basic and diluted EPS (unadjusted)

Reconciliations of the earnings and weighted average number of shares used in the calculations are set out below:

	2017			2016		
	Earnings £m	Weighted average number of shares millions	EPS pence	Earnings £m	Weighted average number of shares millions	EPS pence
<b>Unadjusted EPS</b>						
<b>Basic EPS</b>						
Profit attributable to ordinary shareholders	305.0	2,327.1	13.11	221.8	2,332.5	9.51
<b>Effect of dilutive instruments</b>						
Share options and LTIPs	–	27.9	(0.16)	–	9.0	(0.04)
<b>Diluted EPS</b>	<b>305.0</b>	<b>2,355.0</b>	<b>12.95</b>	<b>221.8</b>	<b>2,341.5</b>	<b>9.47</b>

## 1 Performance in the period continued

### 1.5 Earnings per share continued

#### 1.5.2 Underlying EPS

Basic EPS is adjusted to more accurately show underlying business performance. The reconciliation of the earnings used in the calculations of underlying earnings per share is set out below:

	2017			2016		
	Earnings £m	Weighted average number of shares millions	EPS pence	Earnings £m	Weighted average number of shares millions	EPS pence
<b>Underlying EPS</b>						
<b>Basic EPS</b>						
Profit attributable to ordinary shareholders	305.0	2,327.1	13.11	221.8	2,332.5	9.51
Adjustments to determine underlying profit (note 1.4)	(52.2)	–	(2.25)	(40.6)	–	(1.74)
	252.8	2,327.1	10.86	181.2	2,332.5	7.77
<b>Effect of dilutive instruments</b>						
Share options and LTIPs	–	27.9	(0.13)	–	9.0	(0.04)
<b>Diluted EPS</b>	252.8	2,355.0	10.73	181.2	2,341.5	7.73

### 1.6 Operating profit

	2017 £m	2016 £m
The following items have been included in arriving at operating profit:		
Employee costs (note 1.7)	1,925	1,944
Depreciation and impairment:		
– Property, plant and equipment (note 3.3)	305	286
– Investment property (note 3.5)	1	2
– Net impairment reversal (note 1.4 and 3.3)	(44)	–
Amortisation		
– Intangible assets (note 3.2)	93	96
Operating lease rentals:		
– Land and buildings	93	99
– Other	16	17
– Sublease receipts	(6)	(6)
Value of stock expensed	12,519	12,321

## Notes to the Group financial statements continued

52 weeks ended 29 January 2017

### 1 Performance in the period continued

#### 1.6 Operating profit continued

##### Value of stock expensed

In order to provide context on commercial income earned in the period, each is shown below as a percentage of the value of stock expensed (VSE) before commercial income is deducted.

	2017		2016	
	£m	% of VSE	£m	% of VSE
<b>Commercial income</b>				
Marketing and advertising funding	52	0.4	260	2.1
Volume-based rebates	257	2.1	143	1.1
<b>Total commercial income</b>	<b>309</b>	<b>2.5</b>	<b>403</b>	<b>3.2</b>

##### Auditor remuneration

During the period PricewaterhouseCoopers LLP, the Group's auditor, provided the following services:

	2017 £m	2016 £m
<b>Audit services</b>		
Fees payable to the Group's auditor for the audit of the Group and the Company financial statements	0.5	0.4
<b>Other services</b>		
Fees payable to the Group's auditor and its associates for other services:		
– the audit of the Group's subsidiaries pursuant to legislation	0.2	0.2
– other services	0.2	0.4
	<b>0.9</b>	<b>1.0</b>

The Board has a policy on the engagement of the external auditor to supply non-audit services, which is available in the Corporate governance compliance statement set out in the investor relations section of the Group's website at [www.morrisons-corporate.com](http://www.morrisons-corporate.com).

#### 1.7 Employees and Directors

	2017 £m	2016 £m
<b>Employee benefit expense for the Group during the period</b>		
Wages and salaries	1,708	1,728
Social security costs	119	116
Share-based payments	20	11
Other pension costs	78	89
	<b>1,925</b>	<b>1,944</b>



## 1 Performance in the period continued

### 1.7 Employees and Directors continued

	2017 No.	2016 No.
<b>Average monthly number of people, including Directors</b>		
Stores	96,612	105,024
Manufacturing	8,207	8,033
Distribution	5,467	5,582
Centre	2,079	2,274
	<b>112,365</b>	<b>120,913</b>

#### Directors' remuneration

A detailed analysis of Directors' remuneration, including salaries, bonuses and long term incentives, and the highest paid Director, is provided in the Single total figure of remuneration table in the audited section of the Directors' remuneration report, which forms part of these financial statements (page 42). There are no Executive Directors (2016: none) who have retirement benefits accruing under any of the Group's defined benefit pension schemes.

#### Senior management remuneration

The table below shows the remuneration of senior managers. It excludes colleagues already included in the Directors' remuneration report. Senior managers are considered to be key management personnel in accordance with the requirements of IAS 24 'Related party disclosures', and in the context of gender disclosures required by the Companies Act 2006.

	2017 £m	2016 £m
<b>Senior managers</b>		
Wages and salaries	25	34
Social security costs	4	4
Share-based payments	8	4
Other pension costs	2	2
	<b>39</b>	<b>44</b>

### 1.8 Dividends

Amounts recognised as distributed to equity holders in the period:

	2017 £m	2016 £m
Interim dividend for the period ended 29 January 2017 of 1.58p (2016: 1.50p)	37	35
Final dividend for the period ended 31 January 2016 of 3.50p (2016: 9.62p)	81	225
	<b>118</b>	<b>260</b>

The Directors propose a final dividend in respect of the financial period ending 29 January 2017 of 3.85p per share which will absorb an estimated £90m of shareholders' funds. Subject to approval at the AGM, it will be paid on 29 June 2017 to shareholders who are on the register on 26 May 2017.

The dividends paid and proposed during the year are from cumulative realised distributable reserves of the Company.

# Notes to the Group financial statements continued

52 weeks ended 29 January 2017

## 2 Taxation

The Group takes a compliance-focused approach to its tax affairs, and has a transparent relationship with the UK and overseas tax authorities and interacts with HMRC on a regular basis. The Group's tax policy provides a governance framework with all related risks and stakeholder interests taken into consideration. The tax policy is approved by the Board, with updates on tax compliance and governance matters being provided to the Audit Committee.

The Group's approach to tax is to ensure compliance with the relevant laws of the territories in which the Group operates. The majority of the Group's stores and sales are in the UK so the majority of the Group's taxes are paid in the UK.

The Group operates a small number of branches and subsidiary companies outside of the UK based in the following overseas jurisdictions:

- The Netherlands: The Group has operations in the Netherlands as part of its produce supply chain. Local corporation taxes of £1.3m were paid during 2017 (2016: £1.0m);
- Hong Kong: Offices in Hong Kong were established in 2011 and source many of the Group's non-food products. Local corporation taxes of £0.3m were paid during 2017 (2016: £0.3m); and
- Isle of Man, Jersey and Guernsey: The Group's insurance company is based in the Isle of Man for regulatory reasons. Companies based in Jersey and Guernsey hold UK property assets with a net book value of £38m as a result of historic acquisitions. All profits arising in these companies are subject to UK tax.

### 2.1 Accounting policies

#### Current tax

The current income tax charge is calculated on the basis of the tax laws in effect during the period and any adjustments to tax payable in respect of previous periods. Taxable profit differs from the reported profit for the period as it is adjusted both for items that will never be taxable or deductible, and temporary differences. Current tax is charged to profit or loss for the period, except when it relates to items charged or credited directly in other comprehensive income or equity, in which case the current tax is reflected in other comprehensive income or equity as appropriate.

#### Deferred tax

Deferred tax is recognised using the balance sheet method. Provision is made for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. No deferred tax is recognised for temporary differences that arise on the initial recognition of goodwill or the initial recognition of assets and liabilities that are not a business combination and that affects neither accounting nor taxable profits.

Deferred tax is calculated based on tax law that is enacted or substantively enacted at the reporting date and provided at rates expected to apply when the temporary differences reverse. Deferred tax is charged or credited to profit for the period except when it relates to items charged or credited directly to other comprehensive income or equity, in which case the deferred tax is reflected in other comprehensive income or equity as appropriate.

Deferred tax assets are recognised to the extent that it is probable that the asset can be utilised. Deferred tax assets are reviewed at each reporting date as judgement is required to estimate the probability of recovery. Deferred tax assets and liabilities are offset where amounts will be settled on a net basis as there is a legally enforceable right to offset.

#### Uncertain tax positions

Uncertain tax positions are assessed with reference to Draft IFRIC Interpretation DI/2015/1 Uncertainty over Income Tax Treatments which provides guidance on the determination of taxable profit and tax bases.

The Group uses in-house tax specialists, professional advisors and relevant previous experience to assess tax risks. The Group recognises a tax provision when it is considered probable that there will be a future outflow of funds to a tax authority. Provisions are measured based on the single most likely outcome for each item unless there is a range of possible outcomes for a particular item where a weighted average measurement is more appropriate. Provisions are included in current liabilities.

## 2 Taxation continued

### 2.2 Taxation

#### 2.2.1 Analysis of charge/(credit) in the period

	2017 £m	2016 £m
<b>Current tax</b>		
– UK corporation tax	57	35
– overseas tax	2	5
– adjustments in respect of prior periods	(11)	(8)
	48	32
<b>Deferred tax</b>		
– origination and reversal of timing differences	(10)	15
– adjustments in respect of prior periods	3	(8)
– impact of change in tax rate	(21)	(44)
	(28)	(37)
<b>Tax charge/(credit) for the period</b>	20	(5)

#### 2.2.2 Tax on items charged in other comprehensive income and equity

	2017 £m	2016 £m
Remeasurements arising in the pension scheme	17	47
Cash flow hedges	8	4
Share-based payments	(9)	–
<b>Total tax on items included in other comprehensive income and equity</b>	16	51
Analysis of items charged to other comprehensive income and equity:		
<b>Deferred tax (note 2.3)</b>	16	51

#### 2.2.3 Tax reconciliation

The reconciliation below shows how the tax charge of £20m (2016: tax credit of £5m) has arisen on profit before taxation of £325m (2016: £217m).

The tax for the period is lower (2016: lower) than the standard rate of corporation tax in the UK of 20% (2016: 20.2%). The differences are explained below:

	2017 £m	2016 £m
Profit before taxation	325	217
Profit before taxation at 20% (2016: 20.2%)	65	44
Effects of:		
Recurring items:		
Expenses not deductible for tax purposes	1	–
Disallowed depreciation on UK properties	20	24
Deferred tax on Safeway acquisition assets	(10)	(5)
Adjustments in respect of prior periods	(8)	(16)
Non-recurring items:		
Profit on property transactions	(6)	(14)
Loss on disposal of business	–	6
Tax impact of impairment and related items	(21)	–
Effect of change in tax rate	(21)	(44)
<b>Tax charge/(credit) for the period</b>	20	(5)

## Notes to the Group financial statements continued

### 52 weeks ended 29 January 2017

#### 2 Taxation continued

##### 2.2 Taxation continued

###### 2.2.3 Tax reconciliation continued

###### Factors affecting current and future tax charges

The effective tax rate for the year was 6.2% (2016: (2.3)%). The normalised tax rate for the year (excluding the impact of property transactions, business disposals and tax rate changes) was 25% (2016: 25%).

The normalised tax rate was 5% above the UK statutory tax rate of 20%. The main factor increasing the normalised tax rate is disallowed depreciation on UK properties which reflects the Group's strategy to maintain a majority freehold estate.

Legislation to reduce the standard rate of corporation tax to 17% from 1 April 2020 was included in the Finance Bill 2016 and was enacted in the period. Accordingly, deferred tax has been provided at 19%, 18% or 17% depending upon when the temporary difference is expected to reverse (2016: 20%, 19% or 18%).

The reduction in tax rate at which deferred tax is provided has reduced the Group's deferred tax liabilities by £21m, resulting in a credit of £21m being recognised in the tax charge for the period.

There have been no indications of any further changes to the rate of corporation tax after 1 April 2020.

##### 2.3 Deferred tax

	2017 £m	2016 £m
<b>Net deferred tax liability</b>	<b>417</b>	<b>429</b>

IAS 12 'Income taxes' permits the offsetting of balances within the same tax jurisdiction. All of the deferred tax assets are available for offset against deferred tax liabilities.

The movements in deferred tax liabilities during the period are shown below:

	Property, plant and equipment £m	Pensions £m	Other short term temporary differences £m	Total £m
<b>Current period</b>				
At 1 February 2016	392	33	4	429
(Credited)/charged to profit for the period	(31)	(4)	7	(28)
Charged/(credited) to other comprehensive income and equity	–	17	(1)	16
<b>At 29 January 2017</b>	<b>361</b>	<b>46</b>	<b>10</b>	<b>417</b>
<b>Prior period</b>				
At 2 February 2015	428	(8)	(5)	415
(Credited)/charged to profit for the period	(36)	(6)	5	(37)
Charged to other comprehensive income and equity	–	47	4	51
At 31 January 2016	392	33	4	429

The analysis of net deferred tax liabilities are as follows:

	2017 £m	2016 £m
Net deferred tax liabilities to be settled after more than 12 months	420	427
Net deferred tax (assets)/liabilities to be settled within 12 months	(3)	2
	<b>417</b>	<b>429</b>

### 3 Operating assets

#### 3.1 Accounting policies

##### Intangible assets

##### Goodwill

Goodwill arising on a business combination is not amortised but is reviewed for impairment on an annual basis or more frequently if there are indicators that it may be impaired. Goodwill is allocated to cash generating units that will benefit from the synergies of the business combination for the purpose of impairment testing.

##### Brands

Brands acquired through a business combination are recognised at their fair value at the acquisition date and amortised to profit or loss on a straight-line basis over their estimated useful economic life.

##### Software development costs

Costs that are directly attributable to the creation of identifiable software, which meet the development asset recognition criteria as laid out in IAS 38 'Intangible assets', are recognised as intangible assets.

Direct costs include consultancy costs, the employment costs of internal software developers, and borrowing costs. All other software development and maintenance costs are recognised as an expense as incurred. Software development assets are held at historic cost less accumulated amortisation and impairment, and are amortised over their estimated useful lives (3 to 10 years) on a straight-line basis. Amortisation is charged in cost of sales.

##### Licences

Separately acquired pharmaceutical licences and software licences are recognised at historic cost less accumulated amortisation and impairment. Those acquired in a business combination are recognised at fair value at the acquisition date. Pharmaceutical licences and software licences are amortised over their useful lives (3 to 10 years) on a straight-line basis or over the life of the licence if shorter. Amortisation is charged in cost of sales.

##### Property, plant and equipment

Property, plant and equipment is stated at cost less accumulated depreciation and accumulated impairment losses. Costs include directly attributable costs such as borrowing costs and employment costs of those people directly working on the construction and installation of property, plant and equipment.

##### Depreciation rates

Depreciation rates used to write off cost less residual value on a straight-line basis are:

Freehold land	0%
Freehold buildings	2.5%
Leasehold land	Over the lease period
Leasehold buildings	Over the shorter of lease period and 2.5%
Plant, equipment, fixtures and vehicles	10% to 33%
Assets under construction	0%

Depreciation expense is primarily charged in cost of sales with an immaterial amount in administration expenses.

##### Investment property

Property held to earn rental income is classified as investment property and is held at cost less accumulated depreciation and impairment. The depreciation policy is consistent with that described for property above.

##### Non-current assets classified as held-for-sale

Non-current assets are classified as held-for-sale if their carrying amount is to be recovered principally through a sale transaction, rather than continuing use within the Group, and the sale is considered highly probable. The sale is expected to complete within one year from the date of classification and the assets are available for sale in their current condition. Non-current assets held-for-sale are stated at the lower of carrying amount and fair value less costs of disposal and are not depreciated.

##### Lessor accounting – operating leases

Assets acquired and made available to third parties under operating leases are recorded as property, plant and equipment or investment property and are depreciated on a straight-line basis to their estimated residual values over their estimated useful lives. Operating lease income is credited on a straight-line basis to the date of the next rent review.

##### Finance leases

Assets funded through finance leases are capitalised as property, plant and equipment and depreciated over their useful economic life or lease term, whichever is shorter. The amount capitalised is the lower of the fair value and the present value, calculated using the interest rate implicit in the lease, of the future minimum lease payments. The obligations to pay future rentals are included within liabilities. Rental payments are apportioned between the finance charge and the outstanding obligation so as to produce a constant rate of finance charge on the remaining balance.

## Notes to the Group financial statements continued

### 52 weeks ended 29 January 2017

#### 3 Operating assets continued

##### 3.1 Accounting policies continued

###### Impairment of non-financial assets

Intangible assets with indefinite lives, such as goodwill, and those in construction that are not yet being amortised, are tested for impairment annually. Other non-financial assets are tested if events or changes in circumstances indicate that the carrying amount may not be recoverable.

Testing is performed at the level of a cash generating unit (CGU) in order to compare the CGU's recoverable amount against its carrying value. An impaired CGU is written down to its recoverable amount, which is the higher of value in use or its fair value less costs to dispose. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

The Group considers that each of its stores is a CGU, which together form a grocery group of CGUs supported by corporate assets such as head office and vertically integrated suppliers.

Impairment losses are reversed if there is evidence of an increase in the recoverable amount of a previously impaired asset, but only to the extent that the recoverable amount does not exceed the carrying amount that would have been determined if no impairment loss had been recognised. Impairment losses relating to goodwill are not reversed. Any reversal of impairment losses is excluded from underlying earnings.

##### 3.2 Goodwill and intangible assets

Current period	Goodwill £m	Software development costs £m	Licences £m	Total £m
<b>Cost</b>				
At 1 February 2016	10	647	31	688
Additions	–	41	14	55
Fully written down assets	–	(41)	(14)	(55)
<b>At 29 January 2017</b>	<b>10</b>	<b>647</b>	<b>31</b>	<b>688</b>
<b>Accumulated amortisation</b>				
At 1 February 2016	–	187	18	205
Charge for the period	–	83	10	93
Fully written down assets	–	(41)	(14)	(55)
<b>At 29 January 2017</b>	<b>–</b>	<b>229</b>	<b>14</b>	<b>243</b>
<b>Net book amount at 29 January 2017</b>	<b>10</b>	<b>418</b>	<b>17</b>	<b>445</b>

Included within software development costs are assets under construction of £3m (2016: £16m).

The Group has performed its annual assessment of its amortisation policies and asset lives and deemed them to be appropriate. No changes have been made to asset lives during the year.

As in previous years, fully amortised assets are retained in the Group's fixed asset register. In order to provide greater understanding of the Group's annual amortisation charge, assets which have become fully amortised in the year have been removed from both cost and accumulated amortisation.

###### Goodwill

The goodwill arose on the acquisition of Flower World Limited (£3m) and Farmers Boy (Deeside) Limited (£7m).

###### Impairment testing of goodwill

Goodwill of £10m is allocated to the grocery group of CGUs. This group of CGUs has been tested for impairment via the value in use calculation described in note 3.3. The pre-tax discount rate used is 9.0% (2016: 9.0%) and the growth rate applied to the period after five years is 2.0% (2016: 2.0%).

###### Software development costs

The cumulative interest capitalised included within software development costs is £41m (2016: £41m). The cost of internal labour capitalised is not material for separate disclosure.

### 3 Operating assets continued

#### 3.2 Goodwill and intangible assets continued

	Goodwill £m	Software development costs £m	Licences £m	Total £m
<b>Prior period</b>				
<b>Cost</b>				
At 2 February 2015	10	633	33	676
Additions	–	58	7	65
Interest capitalised	–	4	–	4
Disposals	–	(14)	(1)	(15)
Fully written down assets	–	(34)	(8)	(42)
<b>At 31 January 2016</b>	<b>10</b>	<b>647</b>	<b>31</b>	<b>688</b>
<b>Accumulated amortisation and impairment</b>				
At 2 February 2015	–	138	18	156
Charge for the period	–	87	9	96
Disposals	–	(4)	(1)	(5)
Fully written down assets	–	(34)	(8)	(42)
<b>At 31 January 2016</b>	<b>–</b>	<b>187</b>	<b>18</b>	<b>205</b>
<b>Net book amount at 31 January 2016</b>	<b>10</b>	<b>460</b>	<b>13</b>	<b>483</b>

#### 3.3 Property, plant and equipment

	Freehold land £m	Freehold buildings £m	Leasehold land and buildings £m	Plant, equipment, fixtures & vehicles £m	Total £m
<b>Current period</b>					
<b>Cost</b>					
At 1 February 2016	3,978	4,290	978	1,306	10,552
Additions	2	10	9	346	367
Interest capitalised	–	1	–	–	1
Reclassifications	3	11	(14)	–	–
Transfers to investment properties	–	(4)	–	–	(4)
Transfers to assets held-for-sale	(35)	(30)	–	(4)	(69)
Disposals	–	(9)	(24)	(76)	(109)
Fully written down assets	–	(18)	(5)	(163)	(186)
<b>At 29 January 2017</b>	<b>3,948</b>	<b>4,251</b>	<b>944</b>	<b>1,409</b>	<b>10,552</b>
<b>Accumulated depreciation and impairment</b>					
At 1 February 2016	657	1,645	510	579	3,391
Depreciation charge for the period	–	99	16	190	305
Impairment	55	38	18	36	147
Impairment reversal	(92)	(53)	(39)	(7)	(191)
Reclassifications	–	9	(9)	–	–
Transfers to assets held-for-sale	(19)	(26)	–	(4)	(49)
Disposals	–	(4)	(22)	(66)	(92)
Fully written down assets	–	(18)	(5)	(163)	(186)
<b>At 29 January 2017</b>	<b>601</b>	<b>1,690</b>	<b>469</b>	<b>565</b>	<b>3,325</b>
<b>Net book amount at 29 January 2017</b>	<b>3,347</b>	<b>2,561</b>	<b>475</b>	<b>844</b>	<b>7,227</b>
<b>Assets under construction included above</b>	<b>4</b>	<b>–</b>	<b>–</b>	<b>2</b>	<b>6</b>

## Notes to the Group financial statements continued

### 52 weeks ended 29 January 2017

#### 3 Operating assets continued

##### 3.3 Property, plant and equipment continued

The Group has performed its annual assessment of its depreciation policies and asset lives and deemed them to be appropriate. No changes have been made to asset lives during the year.

As in previous years, fully depreciated assets are retained in the Group's fixed asset register. In order to provide greater understanding of the Group's annual depreciation charge, assets which have been fully depreciated in the year have been removed from both cost and accumulated depreciation.

Included within the table on page 77 are leasehold land and buildings held under finance lease with a cost of £294m (2016: £308m) and accumulated depreciation of £80m (2016: £94m).

The cost of financing property developments prior to their opening date has been included in the cost of the asset. The cumulative amount of interest capitalised in the total cost above amounts to £198m (2016: £197m).

##### Impairment

The Group considers that each store is a separate cash generating unit (CGU) and therefore considers every store for an indication of impairment annually. The Group calculates each store's recoverable amount and compares this amount to its book value. The recoverable amount is determined as the higher of 'value in use' and 'fair value less costs of disposal'. If the recoverable amount is less than the book value, an impairment charge is recognised based on the following methodology:

'Value in use' is calculated by projecting individual store pre-tax cash flows over the remaining useful life of the store, based on forecasting assumptions. The methodology used for calculating future cash flows is to:

- use the actual cash flows for each store in the current year;
- allocate a proportion of the Group's central costs to each store on an appropriate basis;
- project each store's cash flows over the next five years by applying forecast sales and cost growth assumptions;
- project cash flows beyond year five for the remaining useful life of each store by applying a long term growth rate; and
- discount the cash flows using a pre-tax rate of 9.0% (2016: 9.0%). The discount rate takes into account the Group's weighted average cost of capital.

'Fair value less costs of disposal' is estimated by the Directors based on their knowledge of individual stores and the markets they serve and likely demand from grocers or other retailers. The Directors also obtain valuations by store prepared by independent valuers and consider these in carrying out their estimate of fair value less cost of disposal for the purposes of testing for impairment. In determining their valuation, the independent valuers assume an expected rent and yield for each store based on the quality of the asset, local catchment and the store being occupied by a supermarket tenant with a similar covenant to Morrisons.

In order to reflect specific local market conditions, in particular the continued low demand from major grocery retailers for supermarket space, the Directors consider it appropriate for the purpose of testing for impairment to revise downwards the rent and yield assumptions in the independent valuation to reflect the following factors on a store by store basis:

- Whether a major grocery operator might buy the store, taking into consideration whether they are already located near the store, and whether the store size is appropriate for their business model, and then if not;
- Assessing whether a smaller store operator might buy the store, in which case the value has been updated to reflect the Directors' assessment of the yield which would be achievable if such an operator acquired the store, and then if not;
- Assessing whether a non-food operator might buy the store, in which case the value has been updated to reflect the Directors' assessment of the yield which would be achievable if such an operator acquired the store.

Having applied the above methodology and assumptions, the Group has recognised a net impairment reversal of £44m during the year (2016: £nil) (£191m impairment reversal offset by £147m impairment charge). This movement reflects fluctuations expected from store level trading performance and local market conditions. At 29 January 2017, the key assumption to which the value in use calculation is most sensitive to is the discount rate. Specific sensitivity analysis with regard to this assumption shows that an increase of 1% in the discount rate would result in an additional impairment charge of £56m.



### 3 Operating assets continued

#### 3.3 Property, plant and equipment continued

	Freehold land £m	Freehold buildings £m	Leasehold land and buildings £m	Plant, equipment, fixtures & vehicles £m	Total £m
<b>Prior period</b>					
<b>Cost</b>					
At 2 February 2015	3,989	4,330	1,055	1,301	10,675
Additions	5	13	14	256	288
Reclassifications	–	(8)	8	–	–
Transfers from investment properties	–	5	–	–	5
Transfers to assets held-for-sale	(3)	(5)	–	(3)	(11)
Disposals	(13)	(44)	(91)	(90)	(238)
Fully written down assets	–	(1)	(8)	(158)	(167)
At 31 January 2016	3,978	4,290	978	1,306	10,552
<b>Accumulated depreciation</b>					
At 2 February 2015	660	1,576	548	639	3,423
Charge for the period	–	102	18	166	286
Transfers from investment properties	–	5	–	–	5
Transfers to assets held-for-sale	–	(4)	–	(3)	(7)
Disposals	(3)	(33)	(48)	(65)	(149)
Fully written down assets	–	(1)	(8)	(158)	(167)
At 31 January 2016	657	1,645	510	579	3,391
Net book amount at 31 January 2016	3,321	2,645	468	727	7,161
Assets under construction included above	–	7	3	2	12

#### 3.4 Assets classified as held-for-sale

	2017 £m	2016 £m
At start of period	–	84
Additions	19	–
Transfers from property, plant and equipment at net book value	20	4
Transfers from investment property at net book value	7	30
Disposals	(46)	(118)
<b>At end of period</b>	<b>–</b>	<b>–</b>

Assets transferred from property, plant and equipment had a cost of £69m (2016: £11m) and accumulated depreciation of £49m (2016: £7m). Assets transferred from investment property had a cost of £10m (2016: £45m) and accumulated depreciation of £3m (2016: £15m).

## Notes to the Group financial statements continued

52 weeks ended 29 January 2017

### 3 Operating assets continued

#### 3.5 Investment property

	2017 £m	2016 £m
<b>Cost</b>		
At start of period	59	108
Additions	–	3
Transfers from/(to) property, plant and equipment	4	(5)
Transfers to assets classified as held-for-sale	(10)	(45)
Disposals	–	(2)
<b>At end of period</b>	<b>53</b>	<b>59</b>
<b>Accumulated depreciation and impairment</b>		
At start of period	22	40
Charge for the period	1	2
Transfers from/(to) property, plant and equipment	–	(5)
Transfers to assets classified as held-for-sale	(3)	(15)
Disposals	–	–
<b>At end of period</b>	<b>20</b>	<b>22</b>
<b>Net book amount at end of period</b>	<b>33</b>	<b>37</b>

Included in other operating income is £7m (2016: £12m) of rental income generated from investment properties. At the end of the period the fair value of investment properties, was £51m (2016: £68m). Investment properties are valued by independent surveyors on a vacant possession basis using observable inputs (fair value hierarchy level 2).

#### 3.6 Operating leases – lessor

The Group has non-cancellable agreements with tenants with varying terms, escalation clauses and renewal rights. The future minimum lease income is as follows:

	2017 £m	2016 £m
Within one year	16	18
More than one year and less than five years	55	61
After five years	27	73
	<b>98</b>	<b>152</b>

#### 3.7 Capital commitments

	2017 £m	2016 £m
Contracts placed for future capital expenditure not provided in the financial statements (property, plant and equipment and intangible assets)	28	26

## 4 Interests in other entities

### 4.1 Accounting policies

#### Joint ventures

The Group applies IFRS 11 'Joint Arrangements' to all joint arrangements. Under IFRS 11 investments in joint arrangements are classified as either joint operations or joint ventures depending on the contractual rights and obligations of each investor. The Group has assessed the nature of its joint arrangements and determined them to be joint ventures. Joint ventures are accounted for under the equity method and are initially recognised at cost.

The consolidated financial statements include the Group's share of the profit or loss and other comprehensive income of the equity accounted investees, from the date that joint control commences until the date that joint control ceases.

#### Investments

Investments comprise investments in equity instruments held for long term investment. They are measured at fair value through other comprehensive income, where the fair value can be measured reliably. Where the fair value of the instruments cannot be measured reliably, for example, when there is variability in the range of estimates, the investments are recognised at cost less accumulated impairment losses. When the Group disposes of an investment, the fair value of the consideration received less the carrying value of the investment at the date of disposal is recognised in profit or loss, along with any amounts previously recognised in other comprehensive income in respect of the investment.

#### Business combinations

The acquisition method is used to account for business combinations. Consideration is the fair value of the assets transferred, the liabilities incurred and the equity interests issued by the Group, including the fair value of any contingent consideration arrangement. Acquisition related costs are expensed as incurred. Identifiable assets acquired, and liabilities and contingent liabilities assumed, are measured initially at their fair values at the acquisition date. On an acquisition by acquisition basis, the Group recognises any non-controlling interest in the acquiree either at fair value or at the non-controlling interest's proportionate share of the acquiree's net assets.

Goodwill is the excess of consideration transferred, plus any non-controlling interest and the fair value of any previous equity interest in the acquiree, over the fair value of the identifiable net assets acquired. In the event that this excess is negative the difference is recognised directly in profit for the period.

#### Disposal of subsidiaries

When the Group ceases to have control over a subsidiary, any retained interest in the entity is remeasured to its fair value at the date when control is lost, with the change in carrying amount recognised in profit or loss. The fair value is the initial carrying amount for the purposes of subsequently accounting for the retained interest as an associate, joint venture or financial asset. In addition, any amounts previously recognised in other comprehensive income in respect of that entity are accounted for as if the Group had directly disposed of the related assets or liabilities. This may mean that amounts previously recognised in other comprehensive income are reclassified to profit or loss.

### 4.2 Joint ventures

The Group and Ocado Group plc are sole investors in a company (MHE JV Co), which owns the plant and equipment at the Dordon Customer Fulfilment Centre. Each party owns 50% of the equity of MHE JV Co and decisions regarding MHE JV Co require the unanimous consent of both parties. The Directors have considered the impact of IFRS 11 and determined that the Group continues to jointly control MHE JV Co.

MHE JV Co	2017 £m	2016 £m
Non-current assets	96	125
Current assets	22	7
Current liabilities	(6)	(7)
Net assets	112	125
Group's share of net assets	56	63
Profit	4	4
Group's share of profit	2	2

## Notes to the Group financial statements continued

### 52 weeks ended 29 January 2017

#### 4 Interests in other entities continued

##### 4.3 Investments

	2017 £m	2016 £m
At start of period	31	31
Fair value adjustments	14	—
Disposals	(45)	—
At end of period	—	31

On 16 August 2016, the Group disposed of its 10% stake in Fresh Direct Inc, a US internet grocer for cash consideration of £45m, net of £1m of transaction costs. In line with IAS 39 'Financial Instruments: Recognition and Measurement', the asset was remeasured to fair value before the sale completed, resulting in a £14m increase in the book value of the investment. On disposal the £14m revaluation gain was recognised in profit or loss net of £1m of transaction costs. This profit is one-off in nature and therefore has been excluded from reported underlying earnings (see note 1.4).

Following the transaction the undrawn loan facility provided to Fresh Direct Inc ceased.

##### 4.4 Business combinations

###### 52 weeks ended 29 January 2017

In the 52 weeks ended 29 January 2017 there were no business combinations.

###### 52 weeks ended 31 January 2016

On 7 December 2015, Wm Morrison Produce Limited exercised an option to acquire the remaining 49% of the issued share capital of Wm Morrison Bananas Limited from Global Pacific Group, for a cash consideration of £3m. Due to the existence of the put and call option, the Group had previously treated Wm Morrison Bananas Limited as a 100% subsidiary.

For part of the year the Group was part of a joint venture in respect of The Morrisons Farm at Dumfries House Limited (the Farm). The Group terminated this agreement on 13 November 2015 when Wm Morrison Supermarkets PLC acquired the remaining 50% of the issued share capital of the Farm. On 6 January 2016, the Farm was renamed Neerock Farming Limited. The Farm's results are immaterial to the Group.

##### 4.5 Disposals of businesses

###### 52 weeks ended 29 January 2017

In the 52 weeks ended 29 January 2017 there were no disposals of businesses.

###### 52 weeks ended 31 January 2016

On 26 October 2015, the Group disposed of its subsidiary Wm Morrison Convenience Stores Limited and associated assets to MLCG Limited for cash consideration of £20m. This resulted in a loss on disposal of £34m. This loss was one-off in nature and was excluded from reported underlying earnings in the 52 weeks ended 31 January 2016 (see note 1.4).

Following the sale, the Group continues to guarantee certain leases relating to its former convenience stores. At 31 January 2016, the Group made an assessment of the likelihood and amount of future rental commitments should these leases revert, and recognised a liability on the balance sheet reflecting the estimated cash outflow. In the event of lessee default the Group will look to minimise its liability by finding alternative occupiers as soon as possible.

On 29 June 2016, MLCG Limited announced it was entering administration. The Group has subsequently reassessed the liability it recognised in the 52 weeks ended 31 January 2016 and considers this still to be appropriate.

## 5 Working capital and provisions

### 5.1 Accounting policies

#### Stock

Stock represents goods for resale and is measured at the lower of cost and net realisable value. Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs necessary to make the sale. Cost is calculated on a weighted average basis and comprises purchase price, import duties and other non-recoverable taxes, reduced by promotional funding and commercial income and a provision for estimated losses relating to shrinkage and markdowns. Losses relating to shrinkage in stores are based on historical losses verified by physical stock counts conducted by an independent third party. Provision is made for obsolete and slow moving items.

#### Trade and other debtors

Trade and other debtors are initially recognised at fair value, which is generally equal to face value, and subsequently held at amortised cost. Provision is made when there is objective evidence that the Group will not be able to recover balances in full, with the charge being included in administrative expenses.

#### Cash and cash equivalents

Cash and cash equivalents for cash flow purposes includes cash-in-hand, cash-at-bank and bank overdrafts. In the balance sheet, bank overdrafts that do not have right of offset are presented within current liabilities.

Cash held by the Group's captive insurer, Farock Insurance Company Limited, is not available for use by the rest of the Group as it is restricted for use against the specific liability of the captive. As the funds are available on demand, they meet the definition of cash in IAS 7 'Cash flow statements'.

#### Trade and other creditors

Trade and other creditors are initially recognised at fair value, which is generally equal to face value of the invoices received, and subsequently held at amortised cost. Trade creditors are presented net of commercial income due when the Group's trading terms state that income from suppliers will be netted against amounts owing to that supplier.

#### Provisions

Provisions are created where the Group has a present obligation as a result of a past event, where it is probable that it will result in an outflow of economic benefits to settle the obligation, and where it can be reliably measured. For petrol filling station decommissioning costs this is when the filling station is first constructed and for dilapidations on leased buildings, when the lease is entered into. Provisions for onerous leases and other onerous contracts are recognised when the Group believes that the unavoidable costs of meeting the obligations exceed the economic benefits expected to be received under the contract. The amounts provided are based on the Group's best estimate of the least net cost of exit. Where material, these estimated outflows are discounted to net present value using a pre-tax rate that reflects current market assumptions. The unwinding of this discount is recognised as a financing cost in the income statement.

### 5.2 Stock

	2017 £m	2016 £m
Finished goods	614	616

Unearned elements of commercial income are deducted from finished goods as the stock has not been sold.

## Notes to the Group financial statements continued

### 52 weeks ended 29 January 2017

#### 5 Working capital and provisions continued

##### 5.3 Debtors

	2017 £m	2016 £m
<b>Trade debtors:</b>		
– Commercial income trade debtors	4	13
– Accrued commercial income	38	26
– Other trade debtors	101	99
Less: provision for impairment of trade debtors	(6)	(6)
	137	132
Prepayments and accrued income	68	56
Other debtors	9	4
	214	192

The ageing analysis of trade debtors is as follows:

	2017 £m	2016 £m
Neither past due nor impaired	137	132
Past due but not impaired:		
Not more than three months	–	–
Greater than three months	–	–
Impaired debt	6	6
	143	138

As at 29 January 2017 and 31 January 2016, trade debtors that were neither past due nor impaired related to a number of debtors for whom there is no recent history of default. The other classes of debtors do not contain impaired assets.

As of 5 March 2017, £4m of the £4m commercial income trade debtor balance had been settled and £28m of the £38m accrued commercial income balance had been invoiced and settled.

##### 5.4 Creditors – current

	2017 £m	2016 £m
Trade creditors	2,160	1,775
Less: commercial income due, offset against amounts owed	(34)	(85)
	2,126	1,690
Other taxes and social security payable	68	86
Other creditors	198	267
Accruals and deferred income	445	475
	2,837	2,518

Included within accruals and deferred income is £3m (2016: £5m) in respect of deferred commercial income.

As of 5 March 2017, £25m of the £34m commercial income due above had been offset against payments made.

## 5 Working capital and provisions continued

### 5.5 Provisions

	Onerous leases and onerous contracts £m	Other property provisions £m	Total £m
At 1 February 2016	289	20	309
Charged to profit for the period	38	–	38
Utilised/released during the period	(34)	–	(34)
Unwinding of discount	13	–	13
<b>At 29 January 2017</b>	<b>306</b>	<b>20</b>	<b>326</b>

Part of the onerous leases relate to sublet and vacant properties, with commitments ranging from one to 56 years. The provision is revised regularly in response to market conditions. During the year, £38m has been charged to onerous lease and onerous contracts provisions as detailed in note 1.4. The utilisation of provisions relates to the ongoing utilisation of onerous contracts and the assignment of onerous leases.

Other property provisions include a petrol filling station decommissioning reserve for the cost of decommissioning petrol tanks, and provisions for dilapidations on leased buildings, for the cost of restoring assets to their original condition.

### 5.6 Cash generated from operations

	2017 £m	2016 £m
Profit for the period	305	222
Net finance costs	145	99
Taxation charge/(credit)	20	(5)
Share of profit of joint venture	(2)	(2)
Operating profit	468	314
Adjustments for:		
Depreciation and amortisation	399	384
Impairment	147	–
Impairment reversal	(191)	–
Profit arising on disposal and exit of properties and sale of businesses and investments	(32)	(97)
Adjustment for non-cash element of pension charges	7	11
Share-based payments	20	11
Other non-cash charges	2	1
Decrease in stock <sup>1</sup>	2	40
(Increase)/decrease in debtors <sup>1</sup>	(19)	30
Increase in creditors <sup>1</sup>	306	313
Increase in provisions <sup>1</sup>	4	19
<b>Cash generated from operations</b>	<b>1,113</b>	<b>1,026</b>

Total working capital inflow (the sum of items marked<sup>1</sup> in the table) is £293m in the year. This includes £38m as a result of the current year onerous contract charge, net of £94m of onerous payments and other non-operating payments of £11m. When adjusted to exclude these items, the working capital inflow is £360m.

## Notes to the Group financial statements continued

52 weeks ended 29 January 2017

### 6 Capital and borrowings

#### 6.1 Accounting policies

##### Borrowings

Interest-bearing loans and overdrafts are initially recorded at fair value, net of attributable transaction costs. Subsequent to initial recognition, any difference between the redemption value and the initial carrying amount is recognised in profit for the period over the period of the borrowings on an effective interest rate basis.

##### Borrowing costs

All borrowing costs are recognised in the Group's profit for the period on an effective interest rate basis except for interest costs that are directly attributable to the construction of buildings and other qualifying assets, which are capitalised and included within the initial cost of the asset. Capitalisation commences when both expenditure on the asset and borrowing costs are being incurred, and necessary activities to prepare the asset for use are in progress. In the case of new stores, this is generally once planning permission has been obtained. Capitalisation ceases when the asset is ready for use. Interest is capitalised at the effective rate incurred on borrowings before taxation of 5% (2016: 5%). Capitalised interest is included within interest paid in cash flow from operating activities.

##### Leases

Leases in which substantially all the risks and rewards of ownership are retained by the lessor are classified as operating leases; all other leases are classified as finance leases. Property leases are analysed into separate components for land and buildings and tested to establish whether the components are operating leases or finance leases. Rental payments on operating leases in which the Group is lessee are taken to profit for the period on a straight-line basis over the life of the lease.

##### Sale and leaseback of properties

The accounting treatment of the sale and leaseback depends upon the substance of the transaction (by applying the lease classification principles described above). For sale and operating leasebacks, the assets are sold at fair value, and accordingly the profit or loss from the sale is recognised immediately in the Statement of comprehensive income. When forming the conclusion of operating lease classification, consideration was given to the key lease classification indicators of IAS 17. The leases are typically for a 25 year period. The Directors have reviewed the remaining useful lives for these particular properties and concluded they are significantly longer than the period of the lease. As disclosed on page 78 a review of the useful economic lives of each of the property, plant and equipment categories has been performed in the year with no changes made. Other key indicators considered in reaching an operating lease classification were the present value of the minimum lease payments and the ownership clauses in the contracts upon expiry of the lease.

##### Share capital

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds. Where any Group company purchases the Company's equity share capital, the consideration paid, including directly attributable incremental costs, is deducted from retained earnings until the shares are cancelled. On cancellation, the nominal value of the shares is deducted from share capital and the amount is transferred to the capital redemption reserve.

##### Own shares held

The Group has employee trusts for the granting of Group shares to executives and members of the employee share plans. Shares in the Group held by the employee share trusts are presented in the balance sheet as a deduction from retained earnings. The shares are deducted for the purpose of calculating the Group's earnings per share.

##### Net debt

Net debt is cash and cash equivalents, long term cash on deposit, bank and other current loans, bonds, private placement loan notes and derivative financial instruments (stated at current fair value).



## 6 Capital and borrowings continued

### 6.2 Finance costs and income

	2017 £m	2016 £m
Interest payable on short term loans and bank overdrafts	(3)	(4)
Interest payable on bonds	(86)	(98)
Interest capitalised	1	4
Total interest payable	(88)	(98)
Provisions: unwinding of discount	(13)	(11)
Other finance costs	(3)	(3)
<b>Underlying finance costs<sup>1</sup></b>	<b>(104)</b>	<b>(112)</b>
Costs associated with the repayment of borrowings (note 1.4)	(56)	–
<b>Finance costs</b>	<b>(160)</b>	<b>(112)</b>
Bank interest received	6	5
Amortisation of bonds	1	1
Other finance income	–	7
<b>Underlying finance income<sup>1</sup></b>	<b>7</b>	<b>13</b>
Net pension income (note 1.4 and 8.2)	8	–
<b>Finance income</b>	<b>15</b>	<b>13</b>
<b>Net finance cost</b>	<b>(145)</b>	<b>(99)</b>

<sup>1</sup> Underlying net finance costs marked <sup>1</sup> amount to £97m (2016: £99m).

### 6.3 Borrowings

The Group had the following current borrowings and other financial liabilities:

	2017 £m	2016 £m
<b>Current</b>		
Bank overdraft	–	9
£200m Sterling bonds 6.00% January 2017	–	200
	–	209

The Group had the following non-current borrowings and other financial liabilities:

	2017 £m	2016 £m
<b>Non-current</b>		
£135m Sterling bonds 6.12% December 2018 (2016: £200m)	136	202
£365m Sterling bonds 4.625% December 2023 (2016: £400m)	363	398
£384m Sterling bonds 3.50% July 2026 (2016: £400m)	411	416
£300m Sterling bonds 4.75% July 2029 (2016: £300m)	292	291
US Private Placement loan notes (USPP) 4.4% November 2026 (2016: \$250m)	–	174
€411m Euro bond 2.25% June 2020 (2016: €700m)	348	527
<b>Total non-current bonds and loan notes</b>	<b>1,550</b>	<b>2,008</b>
Revolving credit facility	–	(5)
	<b>1,550</b>	<b>2,003</b>

The £200m 2017 Sterling bond was repaid in January 2017 on maturity. The movements on the nominal value of the other bonds and the US Private Placement loan notes (USPP) are due to early repayment during the 52 weeks ended 29 January 2017.

## Notes to the Group financial statements continued

### 52 weeks ended 29 January 2017

#### 6 Capital and borrowings continued

##### 6.3 Borrowings continued

###### Borrowing facilities

Borrowings are denominated in sterling and euro, and bear fixed interest rates. All borrowings are unsecured.

In September 2016 the Group extended its syndicated committed revolving credit facility of £1.35bn by a further year, resetting its five year term and resulting in a maturity date of September 2021. The revolving credit facility incurs commitment fees and drawdowns bear interest at floating interest rates at a spread above LIBOR. There were no borrowings under the revolving credit facility at the balance sheet date. In the year, the Group did not renew a further credit facility of £150m that was in place during 2016. Therefore the Group had £1.35bn of undrawn committed borrowing facilities available (2016: £1.5bn).

In the event of default of covenants the principal amounts of borrowings and any interest accrued become repayable on demand.

###### Maturity of borrowings

The table below summarises the maturity profile of the Group's borrowings based on contractual, undiscounted payments, which include interest payments. As a result, amounts shown below do not agree to the amounts disclosed on the balance sheet for borrowings. Creditors (note 5.4) are excluded from this analysis.

	2017 £m	2016 £m
Less than one year	61	291
One to two years	195	79
Two to three years	52	278
Three to four years	400	67
Four to five years	45	593
More than five years	1,248	1,574

###### Fair values

The fair value of the sterling and euro denominated bonds is measured using closing market prices (level 1). The fair value of the USPP at 2016 was estimated by comparing the interest rate to market rates available to the Group at the balance sheet date (level 2). The fair values of borrowings included in level 2 are based on the net present value of the anticipated future cash flows associated with these instruments using rates currently available for debts on similar terms, credit risk and equivalent maturity dates.

These compare to carrying values as follows:

	2017		2016	
	Amortised cost £m	Fair value £m	Amortised cost £m	Fair value £m
Total bonds: non-current and current	1,550	1,676	2,034	2,019
Total loan notes: non-current	—	—	174	167
	1,550	1,676	2,208	2,186

The fair value of other items within current and non-current borrowing equals their carrying amount, as the impact of discounting is not material.

## 6 Capital and borrowings continued

### 6.4 Analysis of net debt

	Note	2017 £m	2016 £m
Cash and cash equivalents per balance sheet		326	496
Bank overdrafts	6.3	–	(9)
<b>Cash and cash equivalents per cash flow statement</b>		<b>326</b>	<b>487</b>
Cross-currency contracts and interest rate swaps		6	30
Fuel and energy price contracts		10	–
<b>Non-current financial assets</b>	7.3	<b>16</b>	<b>30</b>
Foreign exchange forward contracts		11	12
Fuel and energy price contracts		11	–
<b>Current financial assets</b>	7.3	<b>22</b>	<b>12</b>
Foreign exchange forward contracts	7.3	(2)	–
Fuel and energy price contracts	7.3	(1)	(17)
Bonds	6.3	–	(200)
<b>Current financial liabilities</b>		<b>(3)</b>	<b>(217)</b>
Bonds	6.3	(1,550)	(1,834)
Private placement loan notes	6.3	–	(174)
Revolving credit facility	6.3	–	5
Cross-currency contracts and interest rate swaps	7.3	–	(46)
Fuel and energy price contracts	7.3	(5)	(9)
<b>Non-current financial liabilities</b>		<b>(1,555)</b>	<b>(2,058)</b>
<b>Net debt</b>		<b>(1,194)</b>	<b>(1,746)</b>

Cash and cash equivalents include restricted balances of £9m (2016: £16m) which is held by Farock Insurance Company Limited, a subsidiary of Wm Morrison Supermarkets PLC.

In March 2016, the IFRS Interpretations Committee issued an agenda decision regarding the treatment of offsetting and cash-pooling arrangements in accordance with IAS 32 'Financial instruments: Presentation'. This provided additional guidance on when bank overdrafts in cash-pooling arrangements would meet the requirements for offsetting in accordance with IAS 32. Following this additional guidance, the Group has reviewed its cash-pooling arrangements and recognised £nil of cash-pooling facilities within bank overdrafts and short term borrowings in the current period that would previously have been offset against cash and cash equivalent balances. Comparatives at 31 January 2016 have been restated by £8m. There is no impact of this change in presentation on cash flows or net debt.

## Notes to the Group financial statements continued

### 52 weeks ended 29 January 2017

#### 6 Capital and borrowings continued

##### 6.5 Called-up share capital

	Number of shares millions	Share capital £m	Share premium £m	Total £m
At 1 February 2016	2,335.2	234	127	361
Share options exercised	0.4	–	1	1
<b>At 29 January 2017</b>	<b>2,335.6</b>	<b>234</b>	<b>128</b>	<b>362</b>

The total authorised number of ordinary shares is 4,000 million shares (2016: 4,000 million shares) with a par value of 10p per share (2016: 10p per share). All issued shares are fully paid. The Group did not acquire any of its own shares for cancellation in the 52 weeks ended 29 January 2017 or 31 January 2016.

The holders of ordinary shares are entitled to receive dividends as declared and are entitled to one vote per share at the meetings of the Company.

##### Trust shares

Included in retained earnings is a deduction of £14m (2016: £13m) in respect of own shares held at the balance sheet date. This represents the cost of 8,458,487 (2016: 8,401,491) of the Group's ordinary shares (nominal value of £0.8m (2016: £0.8m)). These shares are held in a trust and were acquired by the business to meet obligations under the Group's employee share plans using funds provided by the Group. The market value of the shares at 29 January 2017 was £20m (2016: £15m). The trust has waived its right to dividends. These shares are not treasury shares as defined by the London Stock Exchange.

During the period the Group acquired 2,790,045 (2016: 8,612,819) of its own shares to hold in trust for consideration of £5m (2016: £13m), and utilised 2,733,049 (2016: 3,118,702) trust shares to satisfy awards under the Group's employee share plans.

##### Issue of new shares

The Group issued 381,043 (2016: 70,480) new shares to satisfy options exercised by employees during the period. Proceeds received on exercise of these shares amounted to £0.6m (2016: £0.1m).

##### 6.6 Reserves

	2017 £m	2016 £m
Capital redemption reserve	39	39
Merger reserve	2,578	2,578
Hedging reserve	18	(10)
Retained earnings	1,066	788
<b>Total</b>	<b>3,701</b>	<b>3,395</b>

##### Capital redemption reserve

The capital redemption reserve at the start of the period related to 389,631,561 of the Company's own shares which it purchased on the open market for cancellation between 31 March 2008 and 8 March 2013 at a total cost of £1,081m.

##### Merger reserve

The merger reserve represents the reserve in the Company's balance sheet arising on the acquisition in 2004 of Safeway Limited. In the opinion of the Directors, this reserve is not distributable and accordingly it will be carried forward as a capital reserve.

##### Hedging reserve

This represents the gains and losses arising on derivatives used for cash flow hedging.

##### 6.7 Capital management

The Group defines the capital that it manages as the Group's total equity and net debt balances, as well as its lease commitments.

The Group's capital management objectives are to safeguard its viability taking into consideration the risks that it faces whilst maintaining an investment grade credit rating and having adequate liquidity headroom. The Group manages its capital structure by managing the balance of debt and shares outstanding. It does this by seeking an effective balance between debt and equity. During the current financial year, net debt has reduced by £552m, reflecting strong operating cash flow driven by working capital management and property and business disposals. Throughout the year, the Group has comfortably complied with the gearing and fixed charge cover covenants attaching to its revolving credit facility.

## 6 Capital and borrowings continued

### 6.8 Operating leases – lessee

The Group has outstanding commitments for future minimum lease payments under non-cancellable operating leases. The leases have varying terms, escalation clauses and renewal rights, and fall due as follows:

	2017		2016	
	Property £m	Vehicles, plant and equipment £m	Property £m	Vehicles, plant and equipment £m
Within one year	121	14	119	15
More than one year and less than five years	466	34	451	25
After five years	1,851	–	1,854	–
	2,438	48	2,424	40

The movement in the property lease commitments within one year is summarised below:

	£m
At 1 February 2016	119
Net impact of disposal programme	(4)
New lease commitments	4
Other	2
At 29 January 2017	121

## 7 Financial risk and hedging

### 7.1 Accounting policies

#### Derivative financial instruments and hedge accounting

Derivatives are transacted to mitigate financial risks that arise as a result of the Group's operating activities and funding arrangements. At the inception of a hedge, the Group documents the relationship between the hedging instrument and the hedged item, the risk management objective and strategy for undertaking the hedge.

The Group assesses whether the hedging instrument is highly effective in offsetting changes in fair values or cash flows of the hedged item at inception and it also assesses whether the hedge has been and will continue to be effective on an ongoing basis.

All derivatives are initially recognised at fair value and are also measured at fair value at each reporting date. Derivatives with positive fair values are recognised as assets and those with negative fair values as liabilities. They are also categorised as current or non-current according to the maturity of each derivative. All gains or losses arising due to changes in the fair value of derivatives are recognised in profit or loss except when the derivative qualifies for cash flow hedge accounting.

#### Cash flow hedges

The Group designates derivatives into a cash flow hedge where they have been transacted to hedge a highly probable forecast transaction or a particular risk associated with an asset or liability. The effective portion of the change in the fair value of the derivatives, that are designated into cash flow hedge relationships, are recognised in other comprehensive income. Cumulative gains or losses on derivatives are reclassified from other comprehensive income into profit or loss in the period when the transaction occurs. Any ineffective portion of the gain or loss on the derivative is immediately recognised in profit or loss.

Hedge accounting is discontinued when the hedging instrument expires or is sold, terminated or exercised or no longer qualifies for hedge accounting. At that time, any cumulative gain or loss on the hedging instrument recognised in equity is retained in equity until the forecasted transaction occurs at which point the net cumulative gain or loss recognised in equity is transferred to profit or loss in the period.

#### Fair value hedge

The Group designates derivatives into a fair value hedge relationship when they hedge the Group's exposure to changes in the fair value of a recognised asset or liability, or a firm commitment. The change in fair value of the hedged asset or liability that is attributable to the hedged risk is recognised in profit or loss for the period as well as the gain or loss from changes in the fair value of the derivative.

# Notes to the Group financial statements continued

## 52 weeks ended 29 January 2017

### 7 Financial risk and hedging continued

#### 7.2 Financial risk management

The Group has a centralised treasury function which manages funding, liquidity and other financial risk in accordance with the Board approved Treasury Policy. The objective of the policy and controls that are established is to mitigate the risk of an adverse impact on the performance of the Group as a result of its exposure to financial risks arising from the Group's operations and its sources of finance. It is the Group's policy not to engage in speculative trading of financial instruments.

The Board retains ultimate responsibility for treasury activity and is involved in key decision making. A Treasury Committee is established to provide governance and oversight to treasury activity within delegated authority limits and formally reports to the Audit Committee.

##### Foreign currency risk

The majority of purchases made by the Group are denominated in sterling, however some trade purchases are made in other currencies, primarily the euro and US dollar. The Group's objective is to reduce short term profit volatility from exchange rate fluctuations. It is Group policy that a minimum of 80% of committed and highly probable exposures within the next six months are hedged and at least 40% of exposures in the following six months.

Cross-currency interest rate swaps are used to mitigate the Group's currency exposure arising from payments of interest and principal in relation to foreign currency funding.

At the reporting date, the sensitivity to a reasonable possible change (+/-10%) in the US dollar and euro exchange rates would equate to a £10m post-tax profit or loss exposure in relation to the euro and £7m in relation to the US dollar, for the unhedged forecast foreign currency exposures over the next 12 months. A weakening of the pound sterling by 10% against the euro and US dollar exchange rates would impact other comprehensive income by £19m.

##### Liquidity risk

The Group policy is to maintain an appropriate maturity profile across its borrowings and a sufficient level of committed headroom to meet obligations. The Group finances its operations using a diversified range of funding providers including banks and bondholders.

A central cash forecast is maintained by the treasury function who monitor the availability of liquidity to meet business requirements and any unexpected variances. The treasury function seek to centralise surplus cash balances to minimise the level of gross debt. Short term cash balances, together with undrawn committed facilities, enable the Group to manage its day-to-day liquidity risk. Any short term surplus is invested in accordance with Treasury Policy.

The Treasury Committee compares the committed liquidity available to the Group against the forecast requirements including policy headroom. This policy includes a planning assumption that supply chain finance facilities are not available.

##### Interest rate risk

The Group seeks to protect itself against adverse movements in interest rates by maintaining at least 60% of its total borrowings at fixed interest rates. As at the balance sheet date, 100% (2016: 91%) of the Group's borrowings are at fixed rate.

Whilst still applying the policy described above, from time-to-time the Group enters into fixed-to-floating interest rate swaps to achieve the appropriate proportion of fixed versus floating rate borrowings.

##### Credit risk

As a retailer, the majority of the Group's revenue is received in cash at the point of sale and therefore credit risk is not considered significant to the Group. Some credit risk does arise from cash and cash equivalents, deposits with banking groups and exposures from other sources of income such as commercial income and tenants of investment properties.

The Group has established appropriate credit verification procedures in respect of financial institutions. Limits on the total exposure to any counterparty or Group of connected counterparties are established within Treasury Policy, taking into account credit ratings. Compliance with limits is regularly monitored.

There are no significant concentrations of credit risk within the Group.

##### Commodity price risk

The Group manages the risks associated with the purchase of electricity, gas and diesel consumed by its activities (excluding fuel purchased for resale to customers) by entering into hedging contracts to fix prices for expected consumption.

The Group has adopted a capital at risk model for hedging its fuel and power consumption. The Treasury Committee reviews the Group's exposure to commodity prices and ensures it remains within policy limits. A change of +/-10% in the market value of the commodity price at the balance sheet date would affect other comprehensive income by £18m (2016: £8m).

## 7 Financial risk and hedging continued

### 7.3 Derivative financial assets and liabilities

	2017 £m	2016 £m
<b>Derivative financial assets</b>		
<b>Current</b>		
Foreign exchange forward contracts	11	12
Fuel and energy price contracts	11	–
	22	12
<b>Non-current</b>		
Cross-currency contracts and interest rate swaps	6	30
Fuel and energy price contracts	10	–
	16	30

All derivatives are categorised as level 2 instruments. Level 2 fair values for simple, over-the-counter derivatives are calculated by using benchmarked, observable market interest rates to discount future cash flows.

	2017 £m	2016 £m
<b>Derivative financial liabilities</b>		
<b>Current</b>		
Foreign exchange forward contracts	2	–
Fuel and energy price contracts	1	17
	3	17
<b>Non-current</b>		
Cross-currency contracts and interest rate swaps	–	46
Fuel and energy price contracts	5	9
	5	55

The amounts disclosed in the table below are the contractual undiscounted derivative cash flows and therefore differ to those in the balance sheet.

	2017 £m		2016 £m		
	< 1 year £m	1-5 years £m	< 1 year £m	1-5 years £m	5+ years £m
<b>Maturity analysis of derivatives</b>					
<b>Derivatives settled on a gross basis</b>					
Cross-currency swaps – cash flow hedges					
– Outflow	(10)	(381)	(25)	(694)	(203)
– Inflow	8	376	20	613	223
Interest rate swaps – fair value hedges					
– Outflow	–	–	(3)	(11)	(16)
– Inflow	–	–	7	28	39
Forward contracts – cash flow hedges					
– Outflow	(246)	–	(184)	–	–
– Inflow	251	–	194	–	–
<b>Derivatives settled on a net basis</b>					
Energy price contracts – cash flow hedges					
– Inflow/(outflow)	8	7	(18)	(8)	–

## Notes to the Group financial statements continued

52 weeks ended 29 January 2017

### 7 Financial risk and hedging continued

#### 7.4 Hedging activities

##### Cash flow hedges

At 29 January 2017 and 31 January 2016, the Group held cross-currency swaps designated as cash flow hedges. The notional principal amount of the outstanding cross-currency swaps at 29 January 2017 was \$nil (2016: \$250m) and €413m (2016: €700m).

The fuel and energy price contracts and foreign currency derivatives shown in note 7.3 are designated as cash flow hedges.

##### Fair value hedges

The valuation of fixed-to-floating interest rate swaps designated in fair value hedges are £nil (2016: £21m). These financial instruments were terminated during the period. Early termination costs have been included in costs associated with repayment of borrowings as an adjustment to underlying earnings (see note 1.4).

### 8 Pensions

#### 8.1 Accounting policies

A defined contribution scheme is a pension scheme under which the Group pays fixed contributions into a separate entity and provides no guarantee as to the quantum of retirement benefits that those contributions will ultimately purchase. A defined benefit scheme is one that is not a defined contribution scheme.

##### 8.1.1 Defined benefit schemes

Pension scheme assets are valued at fair market value as required by IAS 19. Pension scheme obligations are an estimate of the amount required to pay the benefits that employees have earned in exchange for current and past service, assessed and discounted to present value using the assumptions shown in note 8.4.1. The net pension liability or asset recognised in the Consolidated balance sheet is the net of the schemes' assets and obligations, which are calculated separately for each scheme.

Current service cost is treated as an operating cost in the Consolidated statement of comprehensive income and Consolidated cash flow statement and is part of underlying earnings. Net interest income/expense is calculated by applying the discount rate on liabilities to the net pension liability or asset (adjusted for cash flows over the accounting period) and is recognised in finance costs or income and excluded from underlying earnings.

Expenses incurred in respect of the management of scheme assets are included in other comprehensive income as a reduction in the return on scheme assets. Other scheme expenses are recognised in profit or loss as an operating expense.

Remeasurements comprise of actuarial gains and losses on the obligations and the return on scheme assets (excluding interest). They are recognised immediately in other comprehensive income. Amounts shown within note 8 are before any adjustments for deferred taxation.

#### 8.2 Defined benefit schemes: Summary and description

The Group operates a number of defined benefit retirement schemes (together 'the Schemes') providing benefits based on a benefit formula that depends on factors including the employee's age and number of years of service. The Morrison and Safeway Schemes provide pension benefits based on either the employee's compensation package and/or career average revalued earnings (CARE) (the 'CARE Schemes'). The CARE Schemes are not open to new members and were closed to future accrual in July 2015. The RSP is a cash balance scheme, which provides a lump sum benefit based upon a defined proportion of an employee's annual earnings in each year, which is revalued each year in line with inflation subject to a cap.

The position of each scheme at 29 January 2017 is as follows:

	2017 £m	2016 £m
CARE Schemes	293	178
RSP	(21)	8
<b>Net pension asset</b>	<b>272</b>	<b>186</b>



## 8 Pensions continued

### 8.2 Defined benefit schemes: summary and description continued

The disclosures below show the details of the schemes combined:

	2017 CARE £m	2017 RSP £m	2016 CARE £m	2016 RSP £m
<b>Balance sheet:</b>				
Fair value of scheme assets	4,455	219	3,812	138
Present value of obligations	(4,162)	(240)	(3,634)	(130)
<b>Net pension asset/(liability)</b>	<b>293</b>	<b>(21)</b>	<b>178</b>	<b>8</b>
<b>Consolidated statement of comprehensive income</b>				
Current service cost – recognised in cost of sales	–	42	21	42
Current service cost – recognised in administrative expenses	–	29	3	20
Administrative costs paid by the Schemes – recognised in administrative expenses	3	1	3	1
Curtailement gain	(1)	–	(3)	–
Net interest on net pension asset – finance income	(6)	(2)	–	–
Total expense (credited)/charged to statement of comprehensive income	(4)	70	24	63
Statement of other comprehensive income:				
Remeasurements in other comprehensive income (credit)/charge	(101)	15	(236)	–

The Schemes are registered schemes under the provisions of Schedule 36 of the Finance Act 2004 and the assets are held in legally separate, trustee-administered funds. The Board of each scheme is required by law to act in the best interests of the scheme participants within the context of administering the scheme in accordance with the purpose for which the trust was created, and is responsible for setting the investment, funding and governance policies of the fund. A representative of the Group attends Trustee Investment Committee meetings in order to provide the Group's view on investment strategy, but the ultimate power lies with the Trustees. The Deed and Rules of the Morrison Scheme gives the Trustees the power to set contributions, while in the Safeway Scheme and the RSP this power is given to the Group, subject to regulatory override.

### 8.3 Scheme assets

Assets of the Schemes generate returns and ultimately cash that is used to satisfy the Schemes' obligations. They are not necessarily intended to be realised in the short term. The Trustees of each Scheme invest in different categories of asset and with different allocations amongst those categories, according to the investment principles of that Scheme.

Currently, the investment strategy of the CARE Schemes is to maintain a balance of growth assets (equities and diversified growth funds), income assets (comprising credit investments, corporate bonds and absolute return bonds) and protection assets (comprising an LDI portfolio), with a weighting towards protection assets. There are no direct investments in the parent Company's own shares or property occupied by any member of the Group.

#### Fair value of Scheme assets:

	2017 CARE £m	2017 RSP £m	2016 CARE £m	2016 RSP £m
Equities (quoted)	770	107	681	98
Corporate bonds (quoted)	382	–	833	–
Absolute return bonds (quoted)	382	–	–	–
Diversified growth funds (quoted)	489	50	734	–
Credit funds (unquoted)	417	–	271	–
Liability driven investments (unquoted)	1,998	61	1,286	34
Cash (quoted)	17	1	7	6
<b>Total</b>	<b>4,455</b>	<b>219</b>	<b>3,812</b>	<b>138</b>

## Notes to the Group financial statements continued

### 52 weeks ended 29 January 2017

#### 8 Pensions continued

##### 8.3 Scheme assets continued

###### Liability driven investments (LDI)

Part of the investment objective of the Schemes is to minimise fluctuations in the Schemes' funding levels due to changes in the value of the liabilities. This is primarily achieved through the use of 'liability driven investments' (LDI), whose main goal is to align movements in the value of assets with movements in the Schemes' liabilities arising from changes in market conditions. The Schemes have hedging that broadly covers interest rate movements and inflation movements, as measured on the Trustees' funding assumptions which use a discount rate derived from gilt yields.

LDI primarily involves the use of government fixed and inflation linked bonds (including re-purchase agreements). Derivatives such as interest rate and inflation swaps are also used. There are no annuities or longevity swaps.

###### Diversified growth funds

The Schemes employ diversified growth funds in order to reduce their exposure to equity markets. These funds typically invest in a range of public and private market assets, including equities, bonds, commodities, property and other assets.

###### Credit funds

The Schemes invest in credit funds in order to improve returns available from their bond assets. These funds typically lend directly to corporations on a senior secured basis, rather than purchasing debt issued in the public markets.

###### Absolute return bonds

The Schemes employ absolute return bond managers to target a moderate investment return whilst aiming to preserve capital in most market environments. These funds typically invest in a range of fixed income instruments and derivatives, across different countries and currencies, actively managing their exposure according to their market views and opportunities available.

The movement in the fair value of the Schemes' assets over the period was as follows:

	2017 CARE £m	2017 RSP £m	2016 CARE £m	2016 RSP £m
<b>Fair value of scheme assets at start of period</b>	3,812	138	4,050	87
Interest income	138	7	123	3
Return on scheme assets excluding interest	612	20	(299)	(5)
Employer contributions	10	56	27	49
Employee contributions	–	3	1	6
Benefits paid	(114)	(4)	(87)	(1)
Administrative expenses	(3)	(1)	(3)	(1)
<b>Fair value of scheme assets at end of period</b>	<b>4,455</b>	<b>219</b>	<b>3,812</b>	<b>138</b>

###### Scottish Limited Partnership

The Group has previously entered into a pension funding partnership structure. In January 2013, Wm Morrison Supermarkets PLC made a contribution to the CARE Schemes of £90m. On the same day, the CARE Schemes invested £90m in the Wm Morrison Property Partnership (SLP) as a limited partner. The SLP holds properties which have been leased back to the Group in return for rental income payments. The Group retains control over these properties, including the flexibility to substitute alternative properties.

As partners in the SLP, the CARE Schemes are entitled to receive a fixed distribution of £6.6m p.a. from the profits of the SLP for 20 years from 2013, subject to certain conditions. The distributions shared with the Schemes are reflected in the Group financial statements as Employer pension contributions.

In July 2015, the SLP was amended to enhance the security provided to the Schemes by including additional properties. The terms of these additional properties are such that the CARE Schemes have no entitlement to receive a distribution.

The CARE Schemes' interests in the SLP reduce the respective deficits on a funding basis, although the agreements do not affect the position directly on an IAS 19 accounting basis because the investments held by the CARE Schemes do not qualify as assets for IAS 19 purposes.

## 8 Pensions continued

### 8.4 Present value of obligations

The movement in the defined benefit obligation over the period was as follows:

	2017 CARE £m	2017 RSP £m	2016 CARE £m	2016 RSP £m
<b>Defined benefit obligation at start of period</b>	(3,634)	(130)	(4,093)	(83)
Current service cost	–	(71)	(24)	(62)
Interest expense	(132)	(5)	(123)	(3)
Actuarial gain – demographic assumptions	94	–	–	–
Actuarial (loss)/gain – financial assumptions	(852)	(40)	517	18
Actuarial gain – experience	247	5	–	5
Curtailement gain	1	–	3	–
Employee contributions	–	(3)	(1)	(6)
Benefits paid	114	4	87	1
<b>Defined benefit obligation at end of period</b>	<b>(4,162)</b>	<b>(240)</b>	<b>(3,634)</b>	<b>(130)</b>

The durations of the defined benefit obligations at the end of the 2017 reporting period are: RSP 20 years; Morrison CARE 26 years; Safeway CARE 24 years. The weighted average duration of all three Schemes is 24 years.

#### 8.4.1 Significant actuarial assumptions

The following are the principal actuarial assumptions at the reporting date (expressed as weighted averages):

	2017 CARE	2017 RSP	2016 CARE	2016 RSP
<b>Financial assumptions</b>				
Discount rate applied to scheme liabilities (% p.a.)	2.9%	2.8%	3.7%	3.7%
Inflation assumption (RPI) (% p.a.)	3.5%	3.5%	3.2%	3.2%
<b>Life expectancies</b>				
<b>Longevity in years from age 65 for current pensioners</b>				
Male	22.3	n/a	22.6	n/a
Female	23.8	n/a	24.1	n/a
<b>Longevity in years from age 65 for current members aged 45</b>				
Male	24.5	n/a	24.9	n/a
Female	26.2	n/a	26.5	n/a

Assumptions regarding future mortality experience are set based on actuarial advice and in accordance with published statistics. Following analysis completed as part of the 2016 actuarial valuations, the 2017 year-end mortality tables used have been updated to the S2PMA/S2PFA-Heavy tables (males/females) based on year of birth with a scaling factor of 110%/100% applied to the mortality rates in the Morrison/Safeway Schemes respectively, with CMI 2015 projections and a long term rate of improvement of 1.5% p.a.

#### Related actuarial assumptions (expressed as weighted averages)

	2017 CARE	2017 RSP	2016 CARE	2016 RSP
Rate of increases in salaries (% p.a.)	–	2.4%	–	2.2%
Rate of increase of pensions in payment: RPI inflation capped at either 2.5% p.a. or 5% p.a. (% p.a.)	2.2%/3.3%	–	2.1%/3.2%	–
Pre-retirement revaluation for active members (% p.a.)	–	1.9%	–	1.8%
Rate of increase of pensions in deferment: CPI inflation capped at either 2.5% p.a. or 5% p.a. (% p.a.)	–/2.4%	2.4%/–	–/2.2%	2.2%/–
CPI inflation (% p.a.)	2.4%	2.4%	2.2%	2.2%

## Notes to the Group financial statements continued

### 52 weeks ended 29 January 2017

#### 8 Pensions continued

##### 8.4 Present value of obligations continued

###### 8.4.2 Sensitivity analysis on significant actuarial assumptions

The following table summarises the impact on the defined benefit obligation at the end of the reporting period if each of the significant actuarial assumptions listed above were changed, in isolation, assuming no other changes in market conditions at the accounting date. In practice any movement in assumptions could be accompanied by a partially offsetting change in asset values, and the corresponding overall impact on the net asset/(liability) is therefore likely to be lower than the amounts below in a number of scenarios. Extrapolation of the sensitivities shown may not be appropriate.

		2017 CARE £m	2017 RSP £m	2016 CARE £m	2016 RSP £m
Discount rate applied to Scheme obligations	+/- 0.1% p.a.	-/+105	-/+5	-/+83	-/+3
Inflation assumption (RPI and associated assumptions)	+/- 0.1% p.a.	+/-95	+/-3	+/-76	+/-2
Longevity	+/- one year	+180	-	+141	-

##### 8.5 Funding

The Morrison Scheme is entirely funded by the parent company and the Safeway Scheme is funded by Safeway Limited and its subsidiaries.

The Group's subsidiaries participate in the RSP. There is no contractual agreement or stated policy for charging the net defined benefit cost between the parent Company and its subsidiaries. The contribution of each participating subsidiary to the RSP is currently calculated in proportion to the number of employees that are members of the RSP.

The latest full actuarial valuations were carried out as at 1 April 2016 for the Safeway Scheme and 5 April 2016 for the Morrison Scheme and the RSP. The valuations indicated that, on the agreed funding basis, the Safeway, Morrison and RSP Schemes had surpluses of £100m, £1m and £10m respectively. As a result of these funding positions there are currently no deficit contributions payable. As such there is no 'minimum funding requirement' in force.

The results of the 2016 actuarial valuations for the CARE Schemes have been used and updated for IAS 19 'Employee benefits' purposes for the period to 29 January 2017 by a qualified independent actuary. For the RSP an actuarial valuation for the purposes of IAS 19, based on member data as at 31 December 2016, has been completed and updated to 29 January 2017 by a qualified independent actuary. The Schemes expose the Group to inflation risk, interest rate risk and market investment risk. In addition, the CARE Schemes expose the Group to longevity risk.

At the year end, schemes in surplus have been disclosed within the assets on the balance sheet. The Group has taken legal advice with regard to the recognition of a pension surplus and also recognition of a minimum funding requirement under IFRIC 14 'IAS 19 – The limit on a defined benefit asset, minimum funding requirement and their interaction'. This advice concluded that recognition of a surplus is appropriate on the basis that the Group has an unconditional right to a refund of a surplus. In respect of the RSP this is on the basis that paragraph 11(a) of IFRIC 14 applies enabling a refund of surplus during the life of the RSP. In respect of the Morrison Scheme, this is on the basis that paragraph 11(b) or 11(c) of IFRIC 14 applies enabling a refund of surplus assuming the gradual settlement of the scheme liabilities over time until all members have left the scheme or the full settlement of the Scheme's liabilities in a single event (i.e. as a scheme wind up). In respect of the Safeway Scheme, a refund is available on the basis that paragraph 11(b) of IFRIC 14 applies. Amendments to the current version of IFRIC 14 are currently being considered. The legal advice received by the Group has considered the proposed new wording to paragraph 12(A) of IFRIC 14 concerning whether other parties have a unilateral power to use a scheme's surplus to settle in full the scheme's liabilities and has concluded that the above accounting treatment should not be affected by the current exposure draft of the revised wording to IFRIC 14.

The current best estimate of Group contributions to be paid to the defined benefit schemes for the accounting period commencing 29 January 2017 is £79m (2016: £67m). This estimate includes amounts payable from the SLP and salary sacrificed contributions from employees.

##### 8.6 Defined contribution scheme set-up costs

As previously announced the Group intends to open a new defined contribution pension scheme for colleagues during the accounting period commencing 30 January 2017. This scheme will become the Auto Enrolment scheme and as such the Group will be liable for backdated contributions for eligible colleagues to 1 October 2012. The estimated set up costs relating to backdated contributions of £35m were initially recognised in the 52 weeks to 31 January 2016. The accrual has been updated to 29 January 2017 to reflect a further year's contribution for eligible colleagues and changes to accounting assumptions.

## 9 Share-based payments

### 9.1 Accounting policy

#### Share-based payments

The Group issues equity-settled share-based payments to certain employees in exchange for services rendered by them. The fair value of the share-based award is calculated at the date of grant and is expensed on a straight-line basis over the vesting period with a corresponding increase in equity. This is based on the Group's estimate of share options that will eventually vest. This takes into account movement of non-market conditions, being service conditions and financial performance, if relevant.

The fair value of share options is measured by use of the Black-Scholes model. The expected life used in the model has been adjusted, based on management's best estimate, for effects of non-transferability, exercise restrictions and behavioural considerations. The charge in the period for share-based payments was £20m (2016: £11m).

### 9.2 Share save schemes

The Share save scheme began in May 2000 and all employees (including Executive Directors) are eligible once the necessary service requirements have been met. The scheme allows participants to save up to a maximum of £350 each month for a fixed period of three years. Options are offered at a discount to the mid-market closing price on the day prior to the offer and are exercisable for a period of six months commencing after the end of the fixed period of the contract. The exercise of options under this scheme is subject only to service conditions. The schemes that launched in May 2011 and subsequently are under the new scheme rules approved by the shareholders in June 2010.

The fair value of options granted, and the inputs used to determine it are as follows:

Grant date	16 May 2016	19 May 2015	20 May 2014	13 May 2013
Share price at grant date	£1.91	£1.81	£2.10	£2.83
Fair value of options granted	£5.1m	£4.8m	£11.6m	£8.1m
Exercise price	£1.70	£1.64	£1.64	£2.25
Dividend yield	2.62%	5.15%	6.21%	4.17%
Annual risk free interest rate	0.87%	1.06%	1.00%	0.45%
Expected volatility <sup>1</sup>	26.8%	22.7%	18.3%	16.8%

<sup>1</sup> The volatility measured at the standard deviation of expected share price returns is based on statistical analysis on weekly share prices over the past 3.37 years prior to the date of grant.

The requirement that the employee has to save in order to purchase shares under the Share save plan is a non-vesting condition. This feature has been incorporated into the fair value at grant date by applying a discount to the valuation obtained from the Black-Scholes option pricing model. The discount is determined by estimating the probability that the employee will stop saving based on expected future trends in the share price and employee behaviour.

	2017		2016	
	Weighted average exercise price in £ per share	Options thousands	Weighted average exercise price in £ per share	Options thousands
<b>Movement in outstanding options</b>				
Outstanding at start of period	1.72	48,827	1.85	50,785
Granted	1.70	13,478	1.64	21,729
Exercised	1.69	(381)	1.66	(70)
Forfeited	1.89	(15,159)	1.93	(23,617)
Outstanding at end of period	1.66	46,765	1.72	48,827
Exercisable at end of period	2.25	52	2.36	17

	2017			2016		
	Weighted average share price at date of exercise £	Weighted average option price at date of exercise £	Number of shares thousands	Weighted average share price at date of exercise £	Weighted average option price at date of exercise £	Number of shares thousands
<b>Share options exercised in the financial period</b>	2.14	1.69	381	1.74	1.66	70

	2017		2016	
	Range of exercise prices	Weighted average remaining contractual life	Range of exercise prices	Weighted average remaining contractual life
<b>Share options outstanding at the end of the period</b>				
Range of exercise prices	£1.64 to £2.25		£1.64 to £2.36	
Weighted average remaining contractual life	1.1 years		2.2 years	

## Notes to the Group financial statements continued

52 weeks ended 29 January 2017

### 9 Share-based payments continued

#### 9.3 Long term incentive plans

In May 2007, a discretionary LTIP for the benefit of certain employees was introduced. The awards have no exercise price and accrue the value of dividends over the vesting period with the exception of senior employees within the schemes granted this year.

LTIP grants issued between 2013 and 2016 had associated performance conditions for Executive Committee members, whilst other senior employees eligible for LTIPs had to satisfy a service condition only. The LTIP schemes granted in April, May and October 2016 have service and performance conditions for all employees. The performance conditions associated with all awards are measured through free cash flow, sales and earnings per share performance.

Awards normally vest three years after the original grant date, provided the relevant service and performance criteria have been met.

The fair value of awards granted and the inputs used to determined it are as follows:

Grant date	25 Oct 2016	13 May 2016	06 Apr 2016	01 Oct 2015	23 Apr 2015	16 Oct 2014	20 Jun 2014	22 Apr 2014	17 Oct 2013	22 Apr 2013
Option fair value at grant date	£2.28	£1.90	£2.00	£1.74	£1.97	£1.57	£1.91	£2.02	£2.79	£2.80
Fair value of share awards	£9.2m	£1.9m	£73.6m	£1.8m	£5.3m	£0.9m	£3.0m	£16.7m	£1.5m	£18.8m

	2017	2016
	Share awards thousands	Share awards thousands
<b>Movement in outstanding share awards</b>		
Outstanding at start of period	20,279	18,793
Granted	42,258	3,711
Exercised	(2,459)	—
Forfeited	(13,596)	(2,225)
Outstanding at end of period	46,482	20,279
Exercisable at end of period	—	—

The weighted average remaining contractual life of the share awards is 1.96 years (2016: 1.1 years).

#### 9.4 One-off share awards

As part of the package for certain senior management, restricted share awards may be granted. These are primarily designed to replace the value of share scheme awards forfeited from the previous employer. Vesting of these awards is subject only to service conditions.

The fair value of awards granted and the inputs used to determined it are as follows:

Grant date	10 July 2015
Share price at grant date	£1.72
Assumed leavers	—
Fair value of share awards granted	£0.1m

There are 62,332 share awards outstanding at the end of the period (2016: 175,029). The movement during the period is entirely the result of options vesting in the period. The weighted average remaining contractual life of the share awards is 1.09 years (2016: 0.8 years).

## 9 Share-based payments continued

### 9.5 Restricted share award

	2017	2016
	Share awards thousands	Share awards thousands
<b>Movement in outstanding share awards</b>		
Outstanding at start of period	1	2,340
Exercised	–	(1,808)
Lapsed	(1)	(531)
Outstanding at end of period	–	1

### 9.6 Deferred share bonus plan

Certain members of senior management participate in the deferred share bonus plan under which 50% of any bonus payable is deferred in shares for three years from the date the deferred share award is made. Dividend equivalents accrue over the vesting period, to be paid when the shares vest. Vesting of these share awards is subject only to service conditions.

The fair value of awards granted and the inputs used to determine it:

Grant date	2016/17 scheme	2015/16 scheme
Share price at grant date	£2.02	£2.05
Assumed leavers	–	–
Exercise price	£nil	£nil
Fair value of share awards granted	£2.0m	£1.1m

	2017	2016
	Share awards thousands	Share awards thousands
<b>Movement in outstanding share awards</b>		
Outstanding at start of period	413	815
Granted	947	559
Exercised	–	(432)
Lapsed	–	(529)
Outstanding at end of period	1,360	413

The weighted average remaining contractual life of the share awards is 1.8 years (2016: 1.9 years).

## 10 Other

### 10.1 Related party transactions

The Group's related party transactions in the period include the remuneration of the senior managers (see note 1.7), and the Directors' emoluments and pension entitlements, share awards and share options in the audited section of the Directors' remuneration report, which forms part of these financial statements.

During the year, the Group received a dividend of £8m (2016: £8m) from MHE JVCo. The Group owns 50% of the equity of MHE JVCo (see note 4.2).

# Wm Morrison Supermarkets PLC – Company balance sheet

## 29 January 2017

	Note	2017 £m	2016 £m
<b>Fixed assets</b>			
Intangible assets	11.6	428	465
Property, plant and equipment	11.7	2,134	2,149
Investment property	11.8	10	17
Investments	11.9	3,439	3,470
Investment in joint venture		64	65
		6,075	6,166
<b>Current assets</b>			
Stock		388	390
Debtors	11.10	3,077	2,674
Pension asset due after more than one year	11.16	120	69
Derivative financial assets due within one year	11.13	22	12
Derivative financial assets due after more than one year	11.13	16	30
Cash and cash equivalents		235	405
		3,858	3,580
Creditors – amounts falling due within one year	11.11	(3,501)	(2,943)
Derivative financial liabilities due within one year	11.13	(3)	(17)
<b>Net current assets</b>		354	620
<b>Total assets less current liabilities</b>		6,429	6,786
Creditors – amounts falling due after more than one year	11.12	(1,593)	(1,974)
Derivative financial liabilities due after more than one year	11.13	(5)	(55)
Pension liabilities due after more than one year	11.16	(21)	–
Deferred tax liabilities	11.14	(130)	(132)
Provisions for liabilities	11.15	(271)	(254)
<b>Net assets</b>		4,409	4,371
<b>Shareholders' equity</b>			
Share capital	11.17	234	234
Share premium	11.17	128	127
Capital redemption reserve	11.18	39	39
Merger reserve	11.18	2,578	2,578
Retained earnings and other reserves <sup>1</sup>	11.18	1,430	1,393
<b>Total shareholders' funds</b>		4,409	4,371

<sup>1</sup> Included within Retained earnings and other reserves is profit after tax of £78m (52 weeks ended 31 January 2016: £91m).

The accounting policies on pages 104 to 106 and the notes on pages 107 to 118 form part of these financial statements.

The financial statements on pages 102 to 118 were approved by the Board of Directors and authorised for issue on 8 March 2017. They were signed on its behalf by:

**Trevor Strain**  
Chief Financial Officer



# Wm Morrison Supermarkets PLC – Company statement of changes in equity

## 52 weeks ended 29 January 2017

	Note	Attributable to the owners of the Company						Total shareholders' funds £m
		Share capital £m	Share premium £m	Capital redemption reserve £m	Merger reserve £m	Hedging reserve £m	Retained earnings £m	
<b>Current period</b>								
At 1 February 2016		234	127	39	2,578	(10)	1,403	4,371
Profit for the period	11.4	–	–	–	–	–	78	78
Other comprehensive income/(expense):								
Cash flow hedging movement		–	–	–	–	22	–	22
Items reclassified from hedging reserve in relation to repayment of borrowings		–	–	–	–	6	–	6
Remeasurement of defined benefit pension schemes	11.16	–	–	–	–	–	42	42
Tax in relation to components of other comprehensive income	11.14	–	–	–	–	(7)	–	(7)
Total comprehensive income for the period		–	–	–	–	21	120	141
Purchase of trust shares	6.5	–	–	–	–	–	(5)	(5)
Proceeds and settlements of employee share awards	6.5	–	1	–	–	–	(1)	–
Employee share option schemes:								
Share-based payments	11.5	–	–	–	–	–	20	20
Dividends	1.8	–	–	–	–	–	(118)	(118)
Total transactions with owners		–	1	–	–	–	(104)	(103)
<b>At 29 January 2017</b>		<b>234</b>	<b>128</b>	<b>39</b>	<b>2,578</b>	<b>11</b>	<b>1,419</b>	<b>4,409</b>

	Note	Attributable to the owners of the Company						Total shareholders' funds £m
		Share capital £m	Share premium £m	Capital redemption reserve £m	Merger reserve £m	Hedging reserve £m	Retained earnings £m	
<b>Prior period</b>								
At 2 February 2015		234	127	39	2,578	(22)	1,519	4,475
Profit for the period	11.4	–	–	–	–	–	91	91
Other comprehensive income/(expense):								
Cash flow hedging movement		–	–	–	–	16	–	16
Remeasurement of defined benefit pension schemes	11.16	–	–	–	–	–	69	69
Tax in relation to components of other comprehensive income	11.14	–	–	–	–	(4)	(14)	(18)
Total comprehensive income for the period		–	–	–	–	12	146	158
Purchase of trust shares	6.5	–	–	–	–	–	(13)	(13)
Employee share option schemes:								
Share-based payments	11.5	–	–	–	–	–	11	11
Dividends	1.8	–	–	–	–	–	(260)	(260)
Total transactions with owners		–	–	–	–	–	(262)	(262)
<b>At 31 January 2016</b>		<b>234</b>	<b>127</b>	<b>39</b>	<b>2,578</b>	<b>(10)</b>	<b>1,403</b>	<b>4,371</b>

The accounting policies on pages 104 to 106 and the notes on pages 107 to 118 form part of these financial statements.

# Wm Morrison Supermarkets PLC – Company accounting policies

## 52 weeks ended 29 January 2017

### 11 Company financial statements

#### 11.1 General information

The principal activity of Wm Morrison Supermarkets PLC ('the Company') is the operation of retail supermarket stores under the Morrisons brand and associated activities. The Company is incorporated and domiciled in the United Kingdom. The address of its registered office is Hilmore House, Gain Lane, Bradford, BD3 7DL, United Kingdom.

#### 11.2 Basis of preparation

The financial statements have been prepared for the 52 weeks ended 29 January 2017 (2016: 52 weeks ended 31 January 2016). These separate financial statements of the Company have been prepared in accordance with Financial Reporting Standard 101 'Reduced Disclosure Framework' (FRS 101) and the Companies Act 2006 ('the Act'). FRS 101 sets out a reduced disclosure framework for a 'qualifying entity' as defined in the standard which addresses the financial reporting requirements and disclosure exemptions in the individual financial statements of qualifying entities that otherwise apply the recognition, measurement and disclosure requirements of EU-adopted IFRS.

The Company is a qualifying entity for the purposes of FRS 101 as it is a member of a group which prepares publicly available consolidated financial statements and it is included in the consolidation for that group.

The disclosure exemptions adopted by the Company in preparation of these financial statements in accordance with FRS 101 are as follows:

- a) IFRS 2 'Share-based payment' (paragraphs 45(b) and 46 to 52) – details of the number and weighted-average exercise prices of share options, and how the fair value of goods or services received was determined;
- b) IFRS 7 'Financial Instruments: Disclosures';
- c) IFRS 13 'Fair value measurement' (paragraphs 91 to 99) – disclosure of valuation techniques and inputs used for fair value measurement of assets and liabilities;
- d) IAS 1 'Presentation of financial statements' (paragraph 38) – comparative information requirements in respect of:
  - (i) paragraph 79(a)(iv) of IAS 1;
  - (ii) paragraph 73(e) of IAS 16 'Property, plant and equipment';
  - (iii) paragraph 118(e) of IAS 38 'Intangible assets' – reconciliations between the carrying amount at the beginning and end of the period; and
  - (iv) paragraph 76 and 79(d) of IAS 40 'Investment property';
- e) The following paragraphs of IAS 1 'Presentation of financial statements':
  - (i) 10(d), (statement of cash flows);
  - (ii) 111 (cash flow statement information); and
  - (iii) 134-136 (capital management disclosures);
- f) IAS 7 'Statement of cash flows';
- g) IAS 8 'Accounting policies, changes in accounting estimates and errors' (paragraph 30 and 31) – requirement for the disclosure of information when an entity has not applied a new IFRS that has been issued but is not yet effective;
- h) The following requirements of IAS 24 'Related party disclosures':
  - (i) paragraph 17 – key management compensation; and
  - (ii) the requirements to disclose related party transactions entered into with two or more wholly owned members of a group.

## 11 Company financial statements continued

### 11.2 Basis of preparation continued

In addition to the FRS 101 exemptions above, the Company has taken advantage of the exemption available under section 408 of the Act and not presented a profit and loss account for the Company.

The financial statements have been prepared on a going concern basis under the historical cost convention except as disclosed in the Summary of accounting policies in note 11.3. The Company's accounting policies have, unless otherwise stated, been applied consistently to all periods presented in these financial statements.

The preparation of financial statements in conformity with FRS 101 requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Company's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements are the same for the Company as they are for the Group. For further details, see page 64 in the Group financial statements.

#### Accounting reference date

The accounting period of the Company ends on the Sunday falling between 29 January and 4 February each year.

### 11.3 Summary of accounting policies

The accounting policies listed below are the same for the Company as for the Group. As such, for further detail see the following notes:

- a) Revenue recognition (1.1);
- b) Cost of sales (1.1);
- c) Promotional funding and commercial income (1.1);
- d) Other operating income (1.1);
- e) Taxation (2.1);
- f) Intangible assets (3.1);
- g) Property, plant and equipment (3.1);
- h) Investment property (3.1);
- i) Impairment of non-financial assets (3.1);
- j) Lessor accounting – operating leases (3.1);
- k) Finance leases (3.1);
- l) Stock (5.1);
- m) Trade and other debtors (5.1);
- n) Cash and cash equivalents (5.1);
- o) Trade and other creditors (5.1);
- p) Provisions (5.1);
- q) Borrowings and borrowing costs (6.1);
- r) Lessee accounting – operating leases (6.1);
- s) Sale and leaseback (6.1);
- t) Share capital (6.1);
- u) Derivative financial instruments and hedge accounting (7.1);
- v) Pensions (8.1); and
- w) Share-based payments (9.1).

# Wm Morrison Supermarkets PLC – Company accounting policies continued

## 52 weeks ended 29 January 2017

### 11 Company financial statements continued

#### 11.3 Summary of accounting policies continued

The following accounting policies are those policies which are specific, and which deal with items considered material, in relation to the Company's financial statements.

##### Investments

Investments in subsidiary undertakings and joint ventures are stated at cost less provision for impairment.

All other equity instruments are held for long term investment and are measured at fair value, where the fair value can be measured reliably. Gains or losses arising from changes in the fair value are presented in the profit and loss account within finance income or expenses in the period they arise.

Where the fair value of the instruments cannot be measured reliably, for example, when there is variability in the range of estimates, the investments are recognised at cost less accumulated impairment losses.

Impairment losses or reversals of previous impairment losses are presented in the profit and loss account in the period they arise.

##### Contingent liabilities

Contingent liabilities are possible obligations whose existence will be confirmed only on the occurrence or non-occurrence of uncertain future events outside the Company's control, or present obligations that are not recognised because it is not probable that an outflow of economic benefits will be required to settle the obligation or the amount cannot be measured reliably. The Company does not recognise contingent liabilities but does disclose any such balances (see note 11.21). The disclosure includes an estimate of their potential financial effect and any uncertainties relating to the amount or timing of any outflow, unless the possibility of settlement is remote.

##### Financial guarantees

Where the Company enters into financial contracts to guarantee the indebtedness of other companies within its Group, the Company considers these to be insurance arrangements, and accounts for them as such. In this respect, the Company treats the guarantee contract as a contingent liability until such time as it becomes probable that the Company will be required to make a payment under the guarantee.

#### 11.4 Operating profit

The employee benefit expense for the Company is £977m (2016: £1,047m). The average monthly number of people, including Directors, employed by the Company is 55,556 (2016: 60,250).

The Company's auditor, PricewaterhouseCoopers LLP charged £0.5m (2016: £0.4m) for audit services in the year, £nil (2016: £nil) for services related to taxation and £0.2m (2016: £0.4m) for other services.

During the period the Company disposed of its 10% stake in Fresh Direct Inc. For further disclosure see notes 4.3 and 11.9.

#### 11.5 Share-based payments

The Company issues equity-settled share-based payments to certain employees in exchange for services rendered by them. The fair value of the share-based award is calculated at the date of grant and is expensed on a straight-line basis over the vesting period with a corresponding increase in equity. This is based on the Company's estimate of share options that will eventually vest. This takes into account movement of non-market conditions, being service conditions and financial performance, if relevant.

The fair value of share options is measured by use of the Black-Scholes model. The expected life used in the model has been adjusted, based on management's best estimate, for effects of non-transferability, exercise restrictions and behavioural considerations.

The charge in the period for share-based payments was £20m (2016: £11m).

Further details of the Company's share schemes are disclosed in note 9, including:

- a) a description of the type of share-based payment arrangements that existed during the reporting period, including general terms and conditions, maximum terms of options granted, and the method of entitlement;
- b) weighted average share price information in respect of options exercised during the reporting period; and
- c) the range of exercise prices and weighted average remaining contractual life of share options outstanding at the end of the reporting period.

# Notes to the Company financial statements

## 52 weeks ended 29 January 2017

### 11 Company financial statements continued

#### 11.6 Intangible assets

	Licences £m	Software development costs £m	Total £m
<b>Cost</b>			
At 1 February 2016	30	635	665
Additions	13	41	54
Fully written down assets	(14)	(37)	(51)
<b>At 29 January 2017</b>	<b>29</b>	<b>639</b>	<b>668</b>
<b>Accumulated amortisation and impairment</b>			
At 1 February 2016	19	181	200
Charged in the period	8	83	91
Fully written down assets	(14)	(37)	(51)
<b>At 29 January 2017</b>	<b>13</b>	<b>227</b>	<b>240</b>
<b>Net book amount at 29 January 2017</b>	<b>16</b>	<b>412</b>	<b>428</b>

The Company has performed its annual assessment of its amortisation policies and asset lives and deemed them to be appropriate. No changes have been made to asset lives during the year.

In previous years, fully amortised assets have been retained in the Company's fixed asset register. In order to provide greater understanding of the Company's annual amortisation charge, assets which have become fully amortised in the year have been removed from both cost and accumulated amortisation.

Included within software development costs are assets under construction of £3m (2016: £16m).

The cost of financing asset developments prior to them being ready for use has been included in the cost of the project.

The cumulative amount of interest capitalised in the total cost above amounts to £41m (2016: £41m). Interest is capitalised at the effective interest rate of 5% (2016: 5%) incurred on borrowings.

## Notes to the Company financial statements continued

### 52 weeks ended 29 January 2017

#### 11 Company financial statements continued

##### 11.7 Property, plant and equipment

	Freehold land £m	Freehold buildings £m	Leasehold land & buildings £m	Plant, equipment, fixtures & vehicles £m	Total £m
<b>Cost</b>					
At 1 February 2016	843	1,498	675	739	3,755
Additions	1	–	3	172	176
Disposals	(5)	(19)	(31)	(39)	(94)
Fully written down assets	–	(11)	(7)	(70)	(88)
<b>At 29 January 2017</b>	<b>839</b>	<b>1,468</b>	<b>640</b>	<b>802</b>	<b>3,749</b>
<b>Accumulated depreciation and impairment</b>					
At 1 February 2016	180	653	377	396	1,606
Depreciation charged in the period	–	35	8	101	144
Impairment	10	10	36	32	88
Impairment reversal	(16)	(10)	(25)	(8)	(59)
Disposals	(2)	(7)	(28)	(39)	(76)
Fully written down assets	–	(11)	(7)	(70)	(88)
<b>At 29 January 2017</b>	<b>172</b>	<b>670</b>	<b>361</b>	<b>412</b>	<b>1,615</b>
<b>Net book amount at 29 January 2017</b>	<b>667</b>	<b>798</b>	<b>279</b>	<b>390</b>	<b>2,134</b>

The Company has performed its annual assessment of its depreciation policies and asset lives and deemed them to be appropriate. No changes have been made to asset lives during the year.

In previous years, fully depreciated assets have been retained in the Company's fixed asset register. In order to provide greater understanding of the Company's annual depreciation charge, assets which have become fully depreciated in the year have been removed from both cost and accumulated depreciation.

Included in the note above is an amount of £839m (2016: £843m) relating to non-depreciable land and £2m (2016: £6m) of assets under construction.

The cost of assets held under finance leases at 29 January 2017 is £354m (2016: £353m), with related accumulated depreciation of £158m (2016: £143m).

The cost of financing asset developments prior to them being ready for use has been included in the cost of the project. The cumulative amount of interest capitalised in the total cost above amounts to £73m (2016: £73m). Interest is capitalised at the effective interest rate of 5% (2016: 5%) incurred on borrowings.

The Company considers that each store is a separate cash generating unit (CGU) and therefore considers every store for an indication of impairment annually. The Company calculates each store's recoverable amount and compares this amount to its book value. The recoverable amount is determined as the higher of 'value in use' and 'fair value less costs of disposal'. If the recoverable amount is less than the book value, an impairment charge is recognised. The methodology applied by the Company is the same methodology as applied by the Group, see note 3.3 for further details.

Having applied the methodology and assumptions, the Company has recognised a net impairment charge of £29m during the year (2016: £nil) (£88m impairment charge offset by £59m impairment reversal). This movement reflects fluctuations expected from store level trading performance and local market conditions.

## 11 Company financial statements continued

### 11.8 Investment property

	Total £m
<b>Cost</b>	
At 1 February 2016	30
Disposals	(10)
<b>At 29 January 2017</b>	<b>20</b>
<b>Accumulated depreciation and impairment</b>	
At 1 February 2016	13
Disposals	(3)
<b>At 29 January 2017</b>	<b>10</b>
<b>Net book amount at 29 January 2017</b>	<b>10</b>

Included in other operating income is £9m (2016: £8m) of rental income generated from investment properties. At the end of the period the fair value of investment properties was £18m (2016: £39m). Investment properties are valued by independent surveyors on a vacant possession basis using observable inputs (fair value hierarchy Level 2).

### 11.9 Investments

	Investment in equity instruments £m	Investment in subsidiary undertakings £m	Total £m
<b>Cost</b>			
At 1 February 2016	31	3,440	3,471
Fair value adjustments	14	–	14
Disposals	(45)	–	(45)
<b>At 29 January 2017</b>	<b>–</b>	<b>3,440</b>	<b>3,440</b>
<b>Provision for impairment</b>			
At 29 January 2017 and 31 January 2016	–	1	1
<b>Net book amount at 29 January 2017</b>	<b>–</b>	<b>3,439</b>	<b>3,439</b>
<b>Net book amount at 31 January 2016</b>	<b>31</b>	<b>3,439</b>	<b>3,470</b>

The disposal above relates to Fresh Direct Inc, for further details see note 4.3.

A list of all of the Company's related undertakings is shown on pages 117 to 118. The Directors believe that the carrying value of investments is supported by their underlying net assets.

### 11.10 Debtors – amounts falling due within one year

	2017 £m	2016 £m
Trade debtors	119	122
Amounts owed by Group undertakings	2,640	2,249
Current tax asset	82	92
Prepayments and accrued income	236	211
	<b>3,077</b>	<b>2,674</b>

Prepayments includes £165m (2016: £182m) relating to amounts falling due after more than one year. Amounts owed by Group undertakings are unsecured and repayable on demand.

## Notes to the Company financial statements continued

### 52 weeks ended 29 January 2017

#### 11 Company financial statements continued

##### 11.11 Creditors – amounts falling due within one year

	2017 £m	2016 £m
Trade creditors	1,991	1,609
Amounts owed to Group undertakings	992	740
Other taxation and social security	56	124
Other creditors	79	89
Accruals and deferred income	383	377
Bank overdraft	–	4
	<b>3,501</b>	<b>2,943</b>

Amounts owed to Group undertakings within one year are unsecured and repayable on demand.

In March 2016, the IFRS Interpretations Committee issued an agenda decision regarding the treatment of offsetting and cash-pooling arrangements in accordance with IAS 32 'Financial instruments: Presentation'. This provided additional guidance on when bank overdrafts in cash-pooling arrangements would meet the requirements for offsetting in accordance with IAS 32. Following this additional guidance, the Company has reviewed its cash-pooling arrangements and recognised £nil of cash-pooling facilities within bank overdrafts and short term borrowings in the current period that would previously have been offset against cash and cash equivalent balances. Comparatives at 31 January 2016 have been restated by £4m. There is no impact of this change in presentation on cash flows or net debt.

##### 11.12 Creditors – amounts falling due after more than one year

	2017 £m	2016 £m
£365m Sterling bonds 4.625% December 2023 (2016: £400m)	363	398
£384m Sterling bonds 3.50% July 2026 (2016: £400m)	411	416
£300m Sterling bonds 4.75% July 2029 (2016: £300m)	292	291
US Private Placement loan notes 4.4% November 2026 (2016: \$250m)	–	174
€411m Euro bond 2.25% June 2020 (2016: €700m)	348	527
Revolving credit facility	–	(5)
Amounts owed to Group undertakings	179	173
	<b>1,593</b>	<b>1,974</b>

The movements on the nominal value of the bonds and the US Private Placement loan notes are due to early repayment made during the year.

Borrowings are denominated in sterling, US dollars and euros, and bear fixed interest rates, with the exception of the revolving credit facility which bears floating interest rates. All borrowings are unsecured. The revolving credit facility incurs commitment fees at market rates and drawdowns bear interest at a spread above LIBOR.

In the event of default of covenants on the bank facility, the principal amounts and any interest accrued are repayable on demand.

Amounts owed to Group undertakings are unsecured and are non-interest-bearing.

##### Finance leases

Net obligations under finance leases of £179m (2016: £173m) are payable in two to five years, and are included in amounts owed to Group undertakings in the table above.



## 11 Company financial statements continued

### 11.13 Derivative financial assets and liabilities

	2017 £m	2016 £m
<b>Assets due within one year</b>		
Foreign exchange forward contracts	11	12
Fuel and energy price contracts	11	–
	22	12
<b>Assets due after more than one year</b>		
Cross-currency contracts and interest rate swaps	6	30
Fuel and energy price contracts	10	–
	16	30
<b>Liabilities due within one year</b>		
Foreign exchange forward contracts	2	–
Fuel and energy price contracts	1	17
	3	17
<b>Liabilities due after more than one year</b>		
Cross-currency contracts and interest rate swaps	–	46
Fuel and energy price contracts	5	9
	5	55

Further details of the derivative financial instruments are provided in note 7, including:

- significant assumptions underlying the valuation;
- fair value and the amounts recognised in profit and loss; and
- significant assumptions underlying the valuation.

### 11.14 Deferred tax liabilities

	2017 £m	2016 £m
Deferred tax liability	148	149
Deferred tax asset	(18)	(17)
<b>Net deferred tax liability</b>	130	132

IAS 12 'Income taxes' permits the offsetting of balances within the same tax jurisdiction. All of the deferred tax assets are available for offset against deferred tax liabilities. The movements in deferred tax liabilities/(assets) during the period are shown below:

	Property, plant and equipment £m	Pensions £m	Other short term temporary differences £m	Total £m
<b>Current period</b>				
At 1 February 2016	137	12	(17)	132
(Credited)/charged to profit for the period	(6)	(4)	1	(9)
Charged/(credited) to other comprehensive income and equity	–	9	(2)	7
<b>At 29 January 2017</b>	131	17	(18)	130
<b>Prior period</b>				
At 2 February 2015	136	3	(26)	113
Charged/(credited) to profit for the period	1	(5)	5	1
Charged to other comprehensive income and equity	–	14	4	18
<b>At 31 January 2016</b>	137	12	(17)	132

# Notes to the Company financial statements continued

## 52 weeks ended 29 January 2017

### 11 Company financial statements continued

#### 11.15 Provision for liabilities

	Onerous leases and onerous contracts £m	Other property provisions £m	Total £m
At 1 February 2016	247	7	254
Charge recognised in profit and loss	36	–	36
Utilised/released during the period	(29)	–	(29)
Unwinding of discount	10	–	10
<b>At 29 January 2017</b>	<b>264</b>	<b>7</b>	<b>271</b>

Further details of the provisions are provided in note 5.5.

#### 11.16 Pensions

##### 11.16.1 Defined benefit schemes: summary and description

The Company operates two defined benefit retirement schemes (together 'the Schemes') providing benefits based on a benefit formula that depends on factors including the employee's age and number of years of service. The Morrison Scheme provides pension benefits based on either the employee's compensation package or career average revalued earnings (CARE) (the 'CARE Scheme'). The CARE Scheme is no longer open to new members and was closed to future accrual in July 2015. The RSP is a cash balance scheme, which provides a lump sum benefit based upon a defined proportion of an employee's annual earnings, which is revalued each year in line with inflation subject to a cap. For details on the scheme rules, funding and the defined contribution scheme set-up costs see note 8.

The position of each scheme at the balance sheet date is as follows:

	2017 £m	2016 £m
CARE Scheme	120	61
RSP	(21)	8
<b>Net pension asset</b>	<b>99</b>	<b>69</b>

<b>Balance sheet:</b>	2017 CARE £m	2017 RSP £m	2016 CARE £m	2016 RSP £m
Fair value of scheme assets	1,222	219	1,047	138
Present value of obligations	(1,102)	(240)	(986)	(130)
<b>Net pension asset/(liability)</b>	<b>120</b>	<b>(21)</b>	<b>61</b>	<b>8</b>

<b>Statement of comprehensive income</b>	2017 CARE £m	2017 RSP £m	2016 CARE £m	2016 RSP £m
Current service cost – recognised in cost of sales	–	42	12	42
Current service cost – recognised in administrative expenses	–	29	–	20
Administrative costs paid by Schemes – recognised in Administrative expenses	2	1	2	1
Curtailement gain	–	–	(1)	–
Net interest on net pension asset – finance income	(2)	(2)	–	–
Total expense charged to statement of comprehensive income	–	70	13	63
Statement of other comprehensive income:				
Remeasurements in other comprehensive income (credit)/charge	(57)	15	(53)	(16)

The Schemes are registered schemes under the provisions of Schedule 36 of the Finance Act 2004 and the assets are held in legally separate, trustee-administered funds. The Board of each Scheme is required by law to act in the best interests of the Scheme participants within the context of administering the Scheme in accordance with the purpose for which the trust was created, and is responsible for setting the investment, funding and governance policies of the fund. A representative of the Group attends Trustee Investment Committee meetings in order to provide the Group's view on investment strategy, but the ultimate power lies with the Trustees. The Deed and Rules of the Morrison Scheme gives the Trustees the power to set contributions, while in the RSP this power is given to the Group, subject to regulatory override.

## 11 Company financial statements continued

### 11.16 Pensions continued

#### 11.16.2 Scheme assets

Assets of the Schemes generate returns and ultimately cash that is used to satisfy the Schemes' obligations. They are not necessarily intended to be realised in the short term. The Trustees of each Scheme invest in different categories of asset and with different allocations amongst those categories, according to the investment principles of that Scheme.

Currently, the investment strategy of the CARE Scheme is to maintain a balance of growth assets (equities and diversified growth funds), income assets (comprising credit investments, corporate bonds and absolute return bonds) and protection assets (comprising an LDI portfolio), with a weighting towards protection assets. There are no direct investments in the Group's own shares or property occupied by any member of the Group.

Fair value of Scheme assets:

	2017 CARE £m	2017 RSP £m	2016 CARE £m	2016 RSP £m
Equities (quoted)	208	107	182	98
Corporate bonds (quoted)	106	–	225	–
Absolute return bonds (quoted)	101	–	–	–
Diversified growth funds (quoted)	129	50	195	–
Credit funds (unquoted)	133	–	72	–
Liability driven investments (unquoted)	508	61	342	34
Scottish Limited Partnership (unquoted)	28	–	29	–
Cash (quoted)	9	1	2	6
<b>Total</b>	<b>1,222</b>	<b>219</b>	<b>1,047</b>	<b>138</b>

For definitions of the liability driven instruments, diversified growth funds, credit funds and absolute return bonds, see note 8.3.

The movement in the fair value of the Schemes' assets over the period was as follows:

	2017 CARE £m	2017 RSP £m	2016 CARE £m	2016 RSP £m
<b>Fair value of scheme assets at start of period</b>	<b>1,047</b>	<b>138</b>	<b>1,106</b>	<b>87</b>
Interest income	38	7	34	3
Return on scheme assets excluding interest	171	20	(82)	(5)
Employer contributions	2	56	12	49
Employee contributions	–	3	–	6
Benefits paid	(34)	(4)	(21)	(1)
Administrative expenses	(2)	(1)	(2)	(1)
<b>Fair value of scheme assets at end of period</b>	<b>1,222</b>	<b>219</b>	<b>1,047</b>	<b>138</b>

#### Scottish Limited Partnership

The Company has previously entered into a pension funding partnership structure. In January 2013, the Company made a contribution to the CARE Scheme of £30m. On the same day, the CARE Scheme invested £30m in the Wm Morrison Property Partnership (SLP) as a limited partner. The SLP holds properties which have been leased back to the Company in return for rental income payments. The Group retains control over these properties, including the flexibility to substitute alternative properties.

As a partner in the SLP, the CARE Scheme is entitled to receive a fixed distribution of £2.2m p.a. from the profits of the SLP for 20 years from 2013, subject to certain conditions.

In July 2015, the SLP was amended to enhance the security provided to the Schemes by including additional properties. The terms of these additional properties are such that the CARE Scheme has no entitlement to receive a distribution.

The CARE Scheme's interests in the SLP increases the net pension asset on an IAS 19 accounting basis because the investments held by the CARE Scheme qualify as an asset for Company IAS 19 purposes.

## Notes to the Company financial statements continued

### 52 weeks ended 29 January 2017

#### 11 Company financial statements continued

##### 11.16 Pensions continued

##### 11.16.3 Present value of obligations

The movement in the defined benefit obligation over the period was as follows:

	2017 CARE £m	2017 RSP £m	2016 CARE £m	2016 RSP £m
Defined benefit obligation at start of period	(986)	(130)	(1,095)	(83)
Current service cost	–	(71)	(12)	(62)
Interest expense	(36)	(5)	(34)	(3)
Actuarial gain – demographic assumptions	36	–	–	–
Actuarial (loss)/gain – financial assumptions	(232)	(40)	133	18
Actuarial gain – experience	82	5	–	5
Curtailement gain	–	–	1	–
Employee contributions	–	(3)	–	(6)
Benefits paid	34	4	21	1
<b>Defined benefit obligation at end of period</b>	<b>(1,102)</b>	<b>(240)</b>	<b>(986)</b>	<b>(130)</b>

The durations of the defined benefit obligations at the end of the 2017 reporting period are: RSP 20 years; CARE 26 years. The weighted average duration of the Schemes is 25 years.

##### 11.16.4 Significant actuarial assumptions

The following are the principal actuarial assumptions at the reporting date (expressed as weighted averages):

Financial assumptions	2017 CARE	2017 RSP	2016 CARE	2016 RSP
Discount rate applied to scheme liabilities (% p.a.)	2.9%	2.8%	3.70%	3.70%
Inflation assumption (RPI) (% p.a.)	3.5%	3.5%	3.20%	3.20%

##### Life expectancies

	2017 CARE	2017 RSP	2016 CARE	2016 RSP
<b>Longevity in years from age 65 for current pensioners</b>				
Male	21.7	n/a	22.0	n/a
Female	23.2	n/a	23.5	n/a
<b>Longevity in years from age 65 for current members aged 45</b>				
Male	23.9	n/a	24.3	n/a
Female	25.6	n/a	25.9	n/a

Assumptions regarding future mortality experience are set based on actuarial advice and in accordance with published statistics. Following analysis completed as part of the 2016 actuarial valuation, the 2017 year-end mortality tables used have been updated to the S2PMA/S2PFA-Heavy tables (males/females) based on year of birth with a scaling factor of 110% applied to the mortality rates in the CARE Scheme, with CMI 2015 projections and a long term rate of improvement of 1.5% p.a.

##### Related actuarial assumptions (expressed as weighted averages)

	2017 CARE	2017 RSP	2016 CARE	2016 RSP
Rate of increases in salaries (% p.a.)	n/a	2.4%	–	2.20%
Rate of increase of pensions in payment: RPI inflation capped at either 2.5% p.a. or 5% p.a. (% p.a.)	2.2%/3.3%	–	2.10%/3.20%	–
Pre-retirement revaluation for active members (% p.a.)	–	1.9%	–	1.80%
Rate of increase of pensions in deferment: CPI inflation capped at either 2.5% p.a. or 5% p.a. (% p.a.)	–/2.4%	2.4%/–	–/2.20%	2.20%/–
CPI inflation (% p.a.)	2.4%	2.4%	2.20%	2.20%

## 11 Company financial statements continued

### 11.16 Pensions continued

#### 11.16.4 Significant actuarial assumptions continued

##### Sensitivity analysis on significant actuarial assumptions

The following table summarises the impact on the defined benefit obligation at the end of the reporting period if each of the significant actuarial assumptions listed above were changed, in isolation, assuming no other changes in market conditions at the accounting date. In practice any movement in assumptions could be accompanied by a partially offsetting change in asset values, and the corresponding overall impact on the net asset/(liability) is therefore likely to be lower than the amounts below in a number of scenarios. Extrapolation of the sensitivities shown may not be appropriate.

		2017 CARE	2017 RSP	2016 CARE	2016 RSP
Discount rate applied to Scheme obligations	+/-0.1% p.a.	-/+30	-/+5	-/+24	-/+3
Inflation assumption (RPI and associated assumptions)	+/-0.1% p.a.	+/-25	+/-3	+/-21	+/-2
Longevity	+one year	+50	n/a	+39	—

#### 11.16.5 Funding

The CARE Scheme is entirely funded by the Company. The Company along with other subsidiaries of the Group participate in the RSP. There is no contractual agreement or stated policy for charging the net defined benefit cost between the Company and its subsidiaries. The contribution of each participating subsidiary to the RSP is currently calculated in proportion to the number of employees that are members of the RSP.

The latest full actuarial valuations were carried out as at 5 April 2016 for the Morrison Scheme and the RSP. The valuations indicated that, on the agreed funding basis, the Morrison and RSP Schemes had surpluses of £1m and £10m respectively. As a result of these funding positions there are currently no deficit contributions payable. As such there is no 'minimum funding requirement' in force.

The results of the 2016 actuarial valuations for the CARE Scheme has been used and updated for IAS 19 'Employee benefits' purposes for the period to 29 January 2017 by a qualified independent actuary. For the RSP an actuarial valuation for the purposes of IAS 19, based on member data as at 31 December 2016, has been completed and updated to 29 January 2017 by a qualified independent actuary. The Schemes expose the Company to inflation risk, interest rate risk and market investment risk. In addition, the CARE Scheme exposes the Company to longevity risk.

At the year end, schemes in surplus have been disclosed within the assets on the balance sheet. The Company has taken legal advice with regard to the recognition of a pension surplus and also recognition of a minimum funding requirement under IFRIC 14 'IAS 19 – The limit on a defined benefit asset, minimum funding requirement and their interaction'. This advice concluded that recognition of a surplus is appropriate on the basis that the Company has an unconditional right to a refund of a surplus. In respect of the RSP this is on the basis that paragraph 11(a) of IFRIC 14 applies enabling a refund of surplus during the life of the RSP. In respect of the Morrison Scheme, this is on the basis that paragraph 11(b) or 11(c) of IFRIC 14 applies enabling a refund of surplus assuming the gradual settlement of the scheme liabilities over time until all members have left the scheme or the full settlement of the Scheme's liabilities in a single event (i.e. as a scheme wind up).

Amendments to the current version of IFRIC 14 are currently being considered. The legal advice received by the Company has considered the proposed new wording to paragraph 12(A) of IFRIC 14 concerning whether other parties have a unilateral power to use a scheme's surplus to settle in full the scheme's liabilities and has concluded that the above accounting treatment should not be affected by the current exposure draft, including the planned revised wording, to IFRIC 14.

The current best estimate of Company contributions to be paid to the defined benefit schemes for the accounting period commencing 29 January 2017 is £73m (2016: £59m). This estimate includes amounts payable from the SLP and salary sacrificed contributions from employees.

## Notes to the Company financial statements continued

### 52 weeks ended 29 January 2017

#### 11 Company financial statements continued

##### 11.17 Share capital and other reserves

	2017 £m	2016 £m
<b>Authorised</b>		
4,000 million ordinary shares of 10p each (2016: 4,000 million)	400	400
<b>Issued and fully paid</b>		
2,336 million ordinary shares of 10p each (2016: 2,335 million)	234	234

For details of the share premium and shares issued in the period, see note 6.5.

##### 11.18 Reserves

	2017 £m	2016 £m
Capital redemption reserve	39	39
Merger reserve	2,578	2,578
Hedging reserve	11	(10)
Retained earnings	1,419	1,403
<b>Total</b>	<b>4,047</b>	<b>4,010</b>

##### Capital redemption reserve

The capital redemption reserve at the start of the period related to 389,631,561 of the Company's own shares which it purchased on the open market for cancellation between 31 March 2008 and 8 March 2013 at a total cost of £1,081m.

##### Merger reserve

The merger reserve represents the reserve arising on the acquisition in 2004 of Safeway Limited. In the opinion of the Directors, this reserve is not distributable and accordingly it will be carried forward as a capital reserve.

##### Hedging reserve

This represents the gains and losses arising on derivatives used for cash flow hedging.

##### 11.19 Capital commitments

	2017 £m	2016 £m
Contracts placed for future capital expenditure not provided in the financial statements (property, plant and equipment and intangible assets)	20	24

##### 11.20 Operating lease commitments

Total outstanding commitments for future minimum lease payments under non-cancellable operating leases are:

	2017		2016	
	Land and buildings £m	Plant, equipment, fixtures and vehicles £m	Land and buildings £m	Plant, equipment, fixtures and vehicles £m
Within one year	79	14	80	15
More than one year and less than five years	308	34	316	25
After five years	1,263	—	1,341	—
	<b>1,650</b>	<b>48</b>	<b>1,737</b>	<b>40</b>

##### 11.21 Contingent liabilities

The Company has given an unlimited guarantee in respect of the overdraft of all the subsidiary undertakings within the Group's banking offset agreement. The overdraft position at 29 January 2017 was £nil (2016: £4m). The Company has also provided a guarantee in respect of sterling bonds amounting to £147m at fair value (2016: £426m) in respect of a subsidiary undertaking. Where the Company enters into financial contracts to guarantee the indebtedness of other companies within its Group, the Company considers these to be insurance arrangements, and accounts for them as such. In this respect, the Company treats the guarantee contract as a contingent liability until such time as it becomes probable that the Company will be required to make a payment under the guarantee.

## Related undertakings

In accordance with section 409 of the Companies Act 2006, a full list of related undertakings including the country of incorporation, the principal activity and the effective percentage of equity owned as at 29 January 2017 is disclosed below. The registered address of all undertakings is Hilmore House, Gain Lane, Bradford, BD3 7DL unless otherwise stated.

### Related undertakings of Wm Morrison Supermarkets PLC

Name	Country of incorporation	Principal activity	Interest
Bos Brothers Fruit and Vegetables B.V. <sup>1</sup>	Holland	Acquirer of food products	100%
De Mandeville Gate Management Limited	United Kingdom	Property maintenance	51%
Erith Pier Company Limited	United Kingdom	Property maintenance	100%
Farmers Boy Limited	United Kingdom	Manufacturer and distributor of fresh food products	100%
Farock Insurance Company Limited <sup>2</sup>	Isle of Man	Insurance captive	100%
Firsdell Ltd	United Kingdom	Property investment	100%
G Park Management Company Limited <sup>3</sup>	United Kingdom	Property management	100%
Holsa Limited	United Kingdom	Dormant	100%
I Morrisons.com Limited	United Kingdom	Dormant	100%
International Seafoods Limited	United Kingdom	Preparation and supply of seafood	100%
Kiddicare Properties Limited	United Kingdom	Lease company	100%
MHE JVCo Limited <sup>4</sup>	United Kingdom	Joint venture with Ocado	50%
Morrisons Food Online Limited	United Kingdom	Dormant	100%
Morrisons-online.com Limited	United Kingdom	Dormant	100%
My Morrisons.com Limited	United Kingdom	Dormant	100%
Neerock Farming Limited <sup>5</sup>	United Kingdom	Dormant	100%
Neerock Limited	United Kingdom	Fresh meat processor	100%
Optimisation Developments Limited	United Kingdom	Property development	100%
Optimisation Investments Limited	United Kingdom	Property investment	100%
Rathbone Kear Limited	United Kingdom	Manufacturer and distributor of morning goods and bread	100%
Safeway Limited	United Kingdom	Holding company	100%
Wm Morrison GP 1 Limited	United Kingdom	General partner in a partnership	100%
Wm Morrison GP 2 Limited	United Kingdom	General partner in a partnership	100%
Wm Morrison GP 3 Limited	United Kingdom	General partner in a partnership	100%
Wm Morrison (HK) Limited <sup>6</sup>	Hong Kong	Acquirer of non-food products	100%
Wm Morrison LP 1 Limited	United Kingdom	Limited partner in a partnership	100%
Wm Morrison LP 2 Limited	United Kingdom	Limited partner in a partnership	100%
Wm Morrison LP 3 Limited	United Kingdom	Limited partner in a partnership	100%
Wm Morrison Nominee 1 Limited	United Kingdom	Dormant	100%
Wm Morrison Nominee 2 Limited	United Kingdom	Dormant	100%
Wm Morrison Nominee 3 Limited	United Kingdom	Dormant	100%
Wm Morrison Online Ltd	United Kingdom	Dormant	100%
Wm Morrison Pension Trustee Limited	United Kingdom	Dormant	100%
Wm Morrison Produce Limited	United Kingdom	Produce packer and purchaser	100%
Wm Morrison Property Investments Limited <sup>7</sup>	United Kingdom	General partner in a partnership	100%
Wm Morrison Supermarket Stores Ltd	United Kingdom	Dormant	100%

### Related undertakings of other Group companies

Name	Country of incorporation	Principal activity	Interest
Alliance Property Holdings Limited	United Kingdom	Dormant	100%
Amos Hinton & Sons Ltd	United Kingdom	Dormant	100%
Argyle Securities Limited <sup>7</sup>	United Kingdom	Dormant	100%
Argyll Foods Limited	United Kingdom	Dormant	100%
Argyll Stores (Holdings) Limited	United Kingdom	Dormant	100%
Ascot Road Watford Limited	United Kingdom	Holding company	100%
Cancede Limited	United Kingdom	Property investment	100%

<sup>1</sup> Registered address 3151 ZJ Hoek van Holland, the Netherlands, Amersgat 17.

<sup>2</sup> Registered address 1st Floor, Rose House, 51-59 Circular Road, Douglas, Isle of Man, IM1 1AZ.

<sup>3</sup> Registered address 100 Barbirolli Square, Manchester, M2 3AB.

<sup>4</sup> Registered address Titan Court 3 Bishops Square, Hatfield Business Park, Hatfield, Hertfordshire, AL10 9NE.

<sup>5</sup> Registered address Market Hill, Market Hill Road, Turriff, Aberdeenshire, Scotland, AB53 4PA.

<sup>6</sup> Registered address 4304 China Resources Building, 26 Harbour Road, Wanchai, Hong Kong.

<sup>7</sup> Registered address Capella Building (Tenth Floor), 60 York Street, Glasgow, G2 8JX.

## Related undertakings continued

### Related undertakings of other Group companies continued

Name	Country of incorporation	Principal activity	Interest
Cordon Bleu Freezer Food Centres Limited	United Kingdom	Dormant	100%
Divertigo Limited	United Kingdom	Dormant	100%
English Real Estates Limited	United Kingdom	Property holding company	100%
Evermere Limited	United Kingdom	Dormant	100%
Farmers Boy (Deeside) Limited	United Kingdom	Dormant	100%
Federated Properties Limited	United Kingdom	Dormant	100%
Flower World Limited	United Kingdom	Dormant	100%
Freehold Investments Limited <sup>8</sup>	Jersey	Property investment	100%
J3 Property Limited <sup>7</sup>	United Kingdom	Dormant	100%
Lease Securities Limited <sup>8</sup>	Jersey	Property management	100%
Maypole Limited <sup>9</sup>	Guernsey	Investment company	100%
MDW (Eastbourne) Limited	United Kingdom	Dormant	100%
Monument Hill Properties Limited	United Kingdom	Property development	100%
Newincco 1072 Limited	United Kingdom	Property development	100%
Oldwest Limited <sup>7</sup>	United Kingdom	Dormant	100%
Presto Stores (LC) Limited	United Kingdom	Dormant	100%
Presto Stores Limited	United Kingdom	Dormant	100%
Rathbones Bakeries Limited	United Kingdom	Dormant	100%
RP (No.37) Limited <sup>8</sup>	Jersey	Property investment	100%
Safeway (Overseas) Limited	United Kingdom	Grocery retailer	100%
Safeway Development Limited	United Kingdom	Dormant	100%
Safeway Food Stores Limited	United Kingdom	Dormant	100%
Safeway Pensions Trustees Company Limited	United Kingdom	Dormant	100%
Safeway Pension Trustees Limited	United Kingdom	Dormant	100%
Safeway Properties Limited	United Kingdom	Dormant	100%
Safeway QUEST Trustees Limited	United Kingdom	Dormant	100%
Safeway Stores (Gibraltar) Pension Trustees Limited <sup>10</sup>	United Kingdom	Dormant	100%
Safeway Stores (Ireland) Limited	United Kingdom	Dormant	100%
Safeway Stores Limited	United Kingdom	Grocery retailer	100%
Safeway Trustee (FURB) Limited	United Kingdom	Dormant	100%
Simply Fresh Foods Holdings Limited	United Kingdom	Dormant	100%
Safeway Wholesale Limited	United Kingdom	Dormant	100%
Stalwart Investments Limited <sup>8</sup>	Jersey	Property investment	100%
Stores Group Limited	United Kingdom	Investment company	100%
The Home & Colonial Stores Limited	United Kingdom	Dormant	100%
The Medical Hall Limited <sup>11</sup>	Gibraltar	Pharmaceutical licence holder (Gibraltar)	100%
The Morrisons Foundation	United Kingdom	Charity	100%
Tower Centre Hoddesdon Limited	United Kingdom	Property development	100%
Trilogy (Leamington Spa) Limited	United Kingdom	Property development	100%
Velligrist Limited	United Kingdom	Dormant	100%
Wm Morrison Bananas Limited	United Kingdom	Property investment	100%
Wm Morrison Growers Limited <sup>12</sup>	United Kingdom	Acquirer of food products	100%
Wm Morrison Property Partnership LP <sup>7</sup>	United Kingdom	Scottish Limited Property Partnership	100%
Wm Morrison Property Partnership 1 Limited Partnership	United Kingdom	Property partnership	100%
Wm Morrison Property Partnership 2 Limited Partnership	United Kingdom	Property partnership	100%
Wm Morrison Property Partnership 3 Limited Partnership	United Kingdom	Property partnership	100%

<sup>7</sup> Registered address Capella Building (Tenth Floor), 60 York Street, Glasgow, G2 8JX.

<sup>8</sup> Registered address Lime Grove House, Green Street, St Helier, Jersey, JE1 2ST.

<sup>9</sup> Registered address 1st & 2nd floors, Elizabeth House, Les Ruettes Brayes, St Peter Port, Guernsey, GY1 4LX.

<sup>10</sup> Registered address Suites 41/42 Victoria House, 26 Main Street, Gibraltar.

<sup>11</sup> Registered address 5 Secretary's Lane, Gibraltar GX11 1AA.

<sup>12</sup> Registered address Stubbings Farm, Otley, West Yorkshire, United Kingdom, LS21 1DN.



## Five year summary

52 weeks ended 29 January 2017

### Consolidated statement of comprehensive income

	2017 £m	2016 £m	2015 £m	2014 £m	2013 £m
<b>Turnover</b>	16,317	16,122	16,816	17,680	18,116
Cost of sales	(15,713)	(15,505)	(16,055)	(16,606)	(16,910)
<b>Gross profit</b>	604	617	761	1,074	1,206
Other operating income	76	72	78	81	80
Profit/loss on disposal and exit of properties and sale of businesses and investments	32	97	135	9	(1)
Administrative expenses	(244)	(472)	(1,670)	(1,259)	(336)
<b>Operating profit/(loss)</b>	468	314	(696)	(95)	949
Finance costs	(160)	(112)	(105)	(87)	(75)
Finance income	15	13	7	5	5
Share of profit of joint venture (net of tax)	2	2	2	1	–
<b>Profit/(loss) before taxation</b>	325	217	(792)	(176)	879
Analysed as:					
Underlying profit before tax <sup>1</sup>	337	242	345	719	880
Impairment and provision for onerous contracts	6	(87)	(1,273)	(903)	–
Profit/loss on disposal and exit of properties	19	131	131	9	(1)
Profit arising on disposal of investment	13	–	–	–	–
Costs associated with the repayment of borrowings	(56)	–	–	–	–
Pension scheme set-up costs	–	(35)	–	–	–
(Loss)/profit arising on disposal of businesses	–	(34)	4	–	–
Net pension income	8	–	1	(1)	–
Other exceptional costs	(2)	–	–	–	–
	325	217	(792)	(176)	879
Taxation	(20)	5	31	(62)	(232)
<b>Profit/(loss) for the period attributable to the owners of the Company</b>	305	222	(761)	(238)	647
Earnings per share (pence)					
– basic	13.11	9.51	(32.63)	(10.23)	26.65
– diluted	12.95	9.47	(32.63)	(10.23)	26.57
– underlying basic <sup>1</sup>	10.86	7.77	10.93	23.08	26.75
Dividend per ordinary share (pence)	5.43	5.00	13.65	13.00	11.80

<sup>1</sup> 2013 and 2014 underlying profit restated to include new business development costs.

## Five year summary continued

52 weeks ended 29 January 2017

### Consolidated balance sheet

	2017 £m	2016 £m	2015 £m	2014 £m	2013 £m
<b>Assets</b>					
Goodwill and intangible assets	445	483	520	458	415
Property, plant and equipment	7,227	7,161	7,252	8,625	8,616
Investment property	33	37	68	119	123
Pension asset	293	186	4	–	–
Investment in joint venture	56	63	68	66	–
Investments	–	31	31	31	31
Other financial assets	16	30	–	–	–
<b>Non-current assets</b>	<b>8,070</b>	<b>7,991</b>	<b>7,943</b>	<b>9,299</b>	<b>9,185</b>
<b>Current assets</b>	<b>1,176</b>	<b>1,316</b>	<b>1,144</b>	<b>1,430</b>	<b>1,342</b>
Assets classified as held-for-sale	–	–	84	–	–
<b>Liabilities</b>					
<b>Current liabilities</b>	<b>(2,864)</b>	<b>(2,755)</b>	<b>(2,273)</b>	<b>(2,873)</b>	<b>(2,334)</b>
Other financial liabilities	(1,555)	(2,058)	(2,558)	(2,516)	(2,396)
Deferred tax liabilities	(417)	(429)	(415)	(430)	(471)
Pension liabilities	(21)	–	(43)	(11)	(20)
Provisions	(326)	(309)	(288)	(207)	(76)
<b>Non-current liabilities</b>	<b>(2,319)</b>	<b>(2,796)</b>	<b>(3,304)</b>	<b>(3,164)</b>	<b>(2,963)</b>
<b>Net assets</b>	<b>(4,063)</b>	<b>3,756</b>	<b>3,594</b>	<b>4,692</b>	<b>5,230</b>
<b>Shareholders' equity</b>					
Called-up share capital	234	234	234	234	235
Share premium	128	127	127	127	107
Capital redemption reserve	39	39	39	39	37
Merger reserve	2,578	2,578	2,578	2,578	2,578
Retained earnings and other reserves	1,084	778	616	1,714	2,273
<b>Total equity attributable to the owners of the Company</b>	<b>4,063</b>	<b>3,756</b>	<b>3,594</b>	<b>4,692</b>	<b>5,230</b>

## Supplementary information

### 52 weeks ended 29 January 2017

	2017 %	2016 %	2015 %	2014 %	2013 %
<b>Increase/(decrease) on previous year %</b>					
Turnover	1.21	(4.13)	(4.89)	(2.41)	2.56
Underlying operating profit/(loss)	27.43	(23.30)	(44.60)	(14.86)	(2.47)
(Loss)/profit before taxation	49.77	(127.40)	349.35	(120.02)	(7.18)
(Loss)/profit after taxation	37.39	(129.17)	219.38	(136.79)	(6.23)
Underlying profit before taxation	39.26	(29.86)	(52.02)	(18.67)	(5.45)
Diluted earnings per share	36.74	(129.17)	(218.96)	(138.50)	1.92
Dividend per ordinary share	8.60	(18.32)	5.00	10.17	10.28
<b>% of turnover</b>					
Underlying operating profit	2.65	2.10	2.63	4.57	5.24
Profit/(loss) before taxation	1.99	1.35	(4.71)	(1.00)	4.85
Profit/(loss) after taxation	1.87	1.38	(4.52)	(1.35)	3.57
<b>Retail portfolio</b>					
Size 000s square feet (net sales area)					
0–5	4	4	153	102	12
5–15	54	57	75	76	64
15–25	118	124	126	123	135
25–40	259	260	260	252	239
40+	56	53	53	52	48
<b>Total number of stores</b>	<b>491</b>	<b>498</b>	<b>667</b>	<b>605</b>	<b>498</b>
Petrol filling stations	334	336	335	328	312
Total sales area (000s square feet)	14,094	14,142	14,732	14,233	13,421
Total sales area excluding convenience (000s square feet)	14,094	14,142	14,332	13,976	13,383
Average sales area (000s square feet) <sup>1</sup>	14,313	14,532	14,442	13,640	13,396
Average store size (000s square feet) <sup>2</sup>	28.7	28.4	27.9	27.8	26.9
Total supermarket takings ex petrol (gross) £m <sup>2</sup>	13,591	13,700	14,033	14,593	14,875
Average takings per square feet per week (£) <sup>2</sup>	18.40	18.48	19.11	20.58	21.62
Average takings per store per week ex petrol (£000) <sup>2</sup>	531	521	531	558	591
Average number of customers per store per week <sup>2</sup>	23,532	22,573	22,034	22,874	23,905
Average take per customer (£) <sup>2</sup>	22.62	23.44	23.83	24.41	24.73
<b>Employees</b>					
Full time	42,054	47,925	48,519	52,315	56,177
Part time	70,311	72,988	71,259	75,088	72,528
<b>Total</b>	<b>112,365</b>	<b>120,913</b>	<b>119,778</b>	<b>127,403</b>	<b>128,705</b>
Full time equivalent (average)	77,300	82,992	85,545	90,264	91,760
Average per FTE employee:					
Turnover (£000s)	211	194	197	196	197
Underlying operating profit (£)	5,589	4,085	5,167	8,952	10,342
Employee costs (£)	24,900	23,424	23,029	21,847	21,327

<sup>1</sup> Includes sales area of divested stores.

<sup>2</sup> Excludes convenience and online.

The impact of week 53 in the period ended 3 February 2013 was to increase turnover by £328m and increase profit before taxation by £11m.

## Glossary

### Alternative Performance Measures

In response to the Guidelines on Alternative Performance Measures (APMs) issued by the European Securities and Markets Authority (ESMA), we have provided additional information on the APMs used by the Group. The Directors use the APMs listed below as they are critical to understanding the financial performance and financial health of the Group. As they are not defined by IFRS, they may not be directly comparable with other companies who use similar measures.

APM	Definition	Reconciliation for 2016/17 Group measures
<b>Like-for-like (LFL) sales growth</b>	Percentage change in year-on-year sales (excluding VAT and fuel), removing the impact of new store openings and closures in the current or previous financial year.	Total turnover growth of 1.2% comprises LFL sales of 1.7%, the impact of store openings and closures of (2.2)% and fuel and other sales 1.7%.
<b>Underlying profit before tax (UPBT)</b>	Reported profit before tax including restructuring costs, but excluding impairment and provisions for onerous contracts, profit/loss on disposal and exit of properties and sale of businesses and investments, the impact of pension volatility and other items that do not relate to the Group's principal activities on an ongoing basis.	A reconciliation of this measure is provided in note 1.4 of the financial statements.
<b>Underlying profit before tax and restructuring costs</b>	UPBT excluding restructuring costs.	A reconciliation of this measure is provided in note 1.4 of the financial statements.
<b>Underlying profit after tax</b>	UPBT adjusted for a normalised tax charge.	UPBT of £337m less a normalised tax charge of £84m (note 1.4 of the financial statements).
<b>Underlying operating profit</b>	Reported operating profit including restructuring costs, but excluding impairment and provisions for onerous contracts, profit/loss on disposal and exit of properties and sale of businesses and investments and other items impacting operating profit that do not relate to the Group's principal activities on an ongoing basis.	Reported operating profit (£468m) less impairment and provisions for onerous contracts (£6m), profit/loss on disposal and exit of properties (£19m), profit on sale of investments (£13m), plus other exceptional costs (£2m).
<b>Underlying net finance costs</b>	Reported net finance costs excluding net pension income and other items impacting net finance costs that do not relate to the Group's principal activities on an ongoing basis.	A reconciliation of this measure is provided in note 6.2 of the financial statements.
<b>Underlying earnings per share</b>	Earnings per share based on underlying profit after tax rather than reported profit after tax as described above.	A reconciliation of this measure is included in note 1.5 of the financial statements.
<b>Free cash flow</b>	Movement in net debt before payment of dividend.	Movement in net debt (£552m) before payment of dividend (£118m).
<b>Net debt</b>	Net debt is cash and cash equivalents, non-current financial assets and current financial assets, less borrowings, current financial liabilities and non-current financial liabilities.	A reconciliation of this measure is provided in note 6.4 of the financial statements.
<b>Working capital movement</b>	Movement in stock, movement in debtors, movement in creditors and movement in provisions.	A reconciliation of this measure is provided in note 5.6 of the financial statements.
<b>Operating working capital movement</b>	Working capital movement adjusted for charges for onerous contracts, onerous payments and other non-operating payments.	A reconciliation of this measure is provided in note 5.6 of the financial statements.
<b>Return on capital employed</b>	Return on capital employed is calculated as return divided by average capital employed. Return is defined as underlying profit after tax adjusted for underlying net finance costs and operating lease rentals (on land and buildings). Capital employed is defined as average net assets excluding net pension assets and liabilities, less average net debt, plus the lease multiplier (14 times rent payable).	ROCE (6.9%) equals return divided by average capital employed: <b>Return (£443m)</b> Underlying profit after tax (£253m) adjusted for underlying net finance costs (£97m) and operating lease rentals (on land and buildings) (£93m). <b>Average capital employed (£6,453m)</b> Average net assets excluding the net pension asset (£3,681m), average net debt (£1,470m) and the lease multiplier (£1,302m).
<b>Normalised tax</b>	Normalised tax is the tax rate applied to the Group's principal activities on an ongoing basis. This is calculated by adjusting the effective tax rate for the period to exclude the impact of profit/loss relating to property disposals and sale of businesses and investments, pension interest, impairment and provisions for onerous contracts, and other items that do not relate to the Group's principal activities on an ongoing basis.	A reconciliation of the tax charge is found in note 2.2.3 of the financial statements.

## Investor relations and financial calendar

### Financial calendar 2017/18

#### Financial events and dividends

Quarterly management statement	4 May 2017
Final dividend record date	26 May 2017
Annual General Meeting	15 Jun 2017
Final dividend payment date	29 Jun 2017
Half year end	30 Jul 2017
Interim results announcement	14 Sep 2017
Interim dividend record date	29 Sep 2017
Quarterly management statement	2 Nov 2017
Interim dividend payment date	6 Nov 2017
Financial year end	4 Feb 2018

### Company Secretary

Jonathan Burke

### Registered office

Wm Morrison Supermarkets PLC  
Hilmore House  
Gain Lane  
Bradford  
BD3 7DL  
Telephone: 0845 611 5000  
[www.morrisons.com](http://www.morrisons.com)

### Investor relations

Telephone: 0845 611 5710  
Email: [accinvr@morrisonsplc.co.uk](mailto:accinvr@morrisonsplc.co.uk)

### Corporate responsibility enquiries

Telephone: 0845 611 5000.

### Annual General Meeting

The AGM will be held on 15 June 2017 at Wm Morrison Supermarkets PLC Head Office, Gain Lane, Bradford BD3 7DL.

A separate notice convening the meeting is sent to shareholders, which includes an explanation of the items of special business to be considered at the meeting.

### Dividend reinvestment plan

The Company has a dividend reinvestment plan which allows shareholders to reinvest their cash dividends in the Company's shares bought in the market through a specifically arranged share dealing service. Full details of the plan and its charges, together with mandate forms, are available from the Registrars.

### Morrisons website

Shareholders are encouraged to visit our website, [www.morrisons.com](http://www.morrisons.com), to obtain information on Company history, stores and services, latest offers, press information and a local store finder.

### Share price information

The investor information section of our website provides our current and historical share price data and other share price tools. Share price information can also be found in the financial press and the Cityline service operated by the Financial Times. Telephone: 0906 843 3545.

### Online reports and accounts

Our annual and interim Group financial statements are available to download from the website along with Corporate responsibility reports and other financial announcements. The 2016/17 Annual Report is also available to view in HTML format at [www.morrisons-corporate.com/annual-report-2017](http://www.morrisons-corporate.com/annual-report-2017)

The information in the Annual Report and Financial Statements, Strategic report, and the Interim reports is exactly the same as in the printed version.

### Environmental matters

Our environmental footprint is taken very seriously. In the production of the 2016/17 Annual Report, we have contributed to the reduction in environmental damage in the following ways:

#### a) Website

Shareholders receive notification of the availability of the results to view or download on the Group's website, [www.morrisons-corporate.com](http://www.morrisons-corporate.com), unless they have elected to receive a printed version of the results.

Shareholders are encouraged to view the report on the website which is exactly the same as the printed version, but using the internet has clear advantages such as lowering costs and reducing the environmental impact.

#### b) Recycled paper

This document has been printed on recycled paper that is manufactured in mills with ISO 14001 accreditation from 100% recycled fibre. It is totally chlorine free and is an NAPM certified recycled product.

## Investor relations and financial calendar continued

### Registrars and shareholding enquiries

Administrative enquiries about the holding of Morrisons shares, such as change of address, change of ownership, dividend payments and the dividend reinvestment plan should be directed to:

Capita Asset Services  
The Registry  
34 Beckenham Road  
Beckenham  
Kent BR3 4TU

Telephone: 0871 664 0300  
Overseas: +44 371 664 0300  
Calls cost 12p per minute plus your phone company's access charge. If you are outside the United Kingdom, please call +44 371 664 0300. Calls outside the United Kingdom will be charged at the applicable international rate. We are open between 9.00 am – 5.30 pm, Monday to Friday excluding public holidays in England and Wales.

Web: [www.capitashareportal.com](http://www.capitashareportal.com)

Email: [shareholder.services@capita.co.uk](mailto:shareholder.services@capita.co.uk)

### Solicitors

Ashurst LLP  
Broadwalk House  
5 Appold Street  
London EC2A 2HA

Eversheds Sutherland (international) LLP  
1 Wood Street  
London EC2V 7WS

DWF LLP  
1 Scott Place  
2 Hardman Street  
Manchester M3 3AA

Allen & Overy LLP  
One Bishops Square  
London E1 6AD

### Independent auditors

PricewaterhouseCoopers LLP  
Chartered Accountants and Statutory Auditors  
Central Square  
29 Wellington Street  
Leeds LS1 4DL

### Stockbrokers

Jefferies Hoare Govett  
Vintners Place  
68 Upper Thames Street  
London EC4V 3BJ

Credit Suisse  
One Cabot Square  
London E14 4QJ

Shore Capital  
Bond Street House  
14 Clifford Street  
London W1S 4JU

### Investment bankers

NM Rothschild & Sons Limited  
St Swithin's Lane  
London EC4N 8AL

### Shareholder information

The number of shareholders at 29 January 2017 was 42,308 (2016: 45,571) and the number of shares in issue was 2,335,535,537 (2016: 2,335,154,494).

Analysis by shareholder	Number of holders	% holders	Balances at 29 Jan 17	% capital
Private shareholder	38,626	91.3	90,330,970	3.88
Nominee companies	2,978	7.04	2,082,108,865	89.15
Deceased accounts	395	0.93	739,409	0.03
Limited companies	137	0.32	2,416,457	0.10
Other institutions	60	0.14	4,435,761	0.19
Bank and bank nominees	70	0.17	90,927,663	3.89
Investment trusts	15	0.04	74,540	0.00
Pension funds	13	0.03	77,334	0.00
Family interests	14	0.03	64,424,538	2.76

Analysis by shareholder	Number of holders	% holders	Balances at 29 Jan 17	% capital
1–1,000	23,849	56.37	9,981,166	0.43
1,001–10,000	16,155	38.18	48,016,173	2.06
10,001–1,000,000	2,126	5.03	182,249,562	7.80
Over 1,000,000	178	0.42	2,095,288,636	89.71

# Information at your fingertips

## Customer

Our website, [www.morrisons.com](http://www.morrisons.com), allows you to shop online, search hundreds of inspirational recipes for the food we make, move and sell, and even find ideas for popular event-themed activities.

Morrisons.com deliveries currently service 58% of Great Britain; a postcode checker enables you to see if you are eligible for our home delivery service.

### At Morrisons.com you can:

- Buy over 19,000 Morrisons grocery products
- Benefit from competitive 'one-off' delivery charges
- Purchase a monthly, weekly or annual delivery pass for flat-fee unlimited delivery
- Check out latest promotions and seasonal events
- Review selected offline-only products
- Sign up for our latest offers by email
- Find recipes based on our ingredients and inspired by our campaigns/events
- Learn about our produce and its journey from 'field to fork'
- Read content on healthy eating, reducing food waste and our support for various causes

You can also sign up to and manage your More Card account on our website. In our dedicated area, you can find out what our loyalty card scheme has to offer, check your points balance and make changes to preferences.

Not all products are available online. However, the website is an excellent vehicle for finding out more about things we offer.

You are also able to preview selected items from ranges such as Nutmeg and Market Street, and our new café offers, in-store services, award wins, pharmacies, glass hire, flower shops and new store openings online.

We also provide an online Store Finder where you can find details of your nearest store, opening times and services.

## Corporate

Our corporate website, [www.morrisons-corporate.com](http://www.morrisons-corporate.com), is a one-stop portal that exists for the benefit of our investors, the public and the media. This site has the following sections:

### About Morrisons

You will find information about the Group, its operations, strategy and structure, and past financial information.

### Jobs

Career opportunities and information about working for Morrisons. For our dedicated recruitment website, go to [www.morrisons.co.uk/jobs](http://www.morrisons.co.uk/jobs)

### Media centre

Latest releases about the growing estate of Morrisons, along with promotions and product news.

### Corporate responsibility

Here you can find out about our corporate responsibility ethos, including how we take good care of our environment, society and how we go about business. [www.morrisons.co.uk/cr](http://www.morrisons.co.uk/cr)

### Investors

Presentations, announcements and financial reports can be quickly and easily downloaded or viewed on-screen as PDFs. You can easily navigate around the Annual Report and Financial Statements 2016/17 on-screen, viewing only the parts you want to, at [www.morrisons-corporate.com/annual-report-2017](http://www.morrisons-corporate.com/annual-report-2017)

### Webcasts

Webcasts of the Directors delivering the preliminary results for 2016/17 on 9 March 2017 are available.

## Shareholder information

Other relevant shareholder information is available, for example share price history, dividends, financial calendar and AGM minutes.

### Electronic communications

Electronic communications (eComms) is the fastest and most environmentally friendly way to communicate with our shareholders.

Instead of receiving paper copies of the annual and interim financial results, notices of shareholder meetings and other shareholder documents, you will receive an email to let you know this information is available on our website.

Visiting our website to obtain our results reduces our environmental impact by saving on paper and also reduces our print and distribution costs.

Sign up to eComms on our website at [www.morrisons-corporate.com](http://www.morrisons-corporate.com) and follow the investor eComms link.

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