Sainsbury's Supermarkets Ltd
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Full Year Unaudited Results & Combination of J Sainsbury plc and Asda Group Limited Transcript

David Tyler
Chairman
Good morning everybody. Welcome to this important Presentation this morning. I am delighted in particular to welcome Judith McKenna who is the President and CEO of Walmart International, who is sitting in front of me, and Roger Burnley the CEO of Asda. Both of them will speak a bit later in this Presentation.

So today we are making a historic, pivotal announcement about the future of our business and indeed of the industry. We have agreed a plan with Walmart to bring the businesses of Asda and Sainsbury's together into a combined, enlarged company.

At Sainsbury's we believe that we will generate considerably more value for our shareholders in the future by pursuing this opportunity than any other. Not only that, we believe that this combination will deliver benefits for every stakeholder. For British consumers, for the 330,000 colleagues of our two businesses, for our suppliers and indeed for the British economy as a whole. Mike will explain the details behind our strategy when he gets up shortly. Roger will give an up-to-date picture of the Asda business and Judith will set out Walmart's perspectives. Following that we will have a Q&A led by Mike and Judith to give you as complete a picture as we can of our plans.

But first before all that, we are also announcing today, two days early, Sainsbury's financial results for our year to the 10th March 2018. This has been another year that has demonstrated the strength and resilience of our existing business. In particular you will note that with underlying earnings per share up by 8 per cent in the second half year, compared to the comparative period of the previous year, we are growing earnings again for the first time for several years. And we now see, even before the impact of the transaction we are announcing today, an opportunity for good earnings growth in the existing Sainsbury's business in the years ahead, underpinned by the strength of our core grocery operation. Underpinned by the growth potential of our general merchandise and clothing business and indeed underpinned by a balance sheet now with lower leverage and a much lower pension deficit.

So Kevin O'Byrne our CFO will take you through a short presentation on our results before handing over to Mike to talk about today's transaction. Kevin.

Kevin O'Byrne
Group Chief Financial Officer
Thank you David, good morning everyone. I have the unenviable task of standing between the Presentation by Mike, Judith and Roger and you, but we want to take you through our Results for the year to the 10th March. These are unaudited numbers, the full audited numbers will be released as planned on Wednesday morning. And this morning's Presentation will also cover an outline of guidance for the coming financial year.

We are pleased with the financial performance in the year to March. We delivered underlying profit before tax of £589 million, up 1 per cent for the year and up strongly as David said in the second half. Cost savings in Argos synergies were both ahead of plan and Sainsbury's bank profits were up 11 per cent as we integrated Argos Financial Services. Strong free cash flow generation of £432 million, up £113 million year-on-year and this enabled us to reduce net debt ahead of previous guidance. The final dividend is up 8 per cent reflecting earnings growth in the second half.

And finally we confirm, we will confirm the consensus for the year 2018/19. In the year sales were up 9 per cent largely reflecting the full year's consolidation of Argos which versus only part year in the previous year. Retail operation profit was broadly flat supported by synergy delivery, cost savings, a better underlying margin trend in the food business, offset by some pressure on the general merchandise margins in a tough environment.

Underlying UPBT was up £8 million for the full year with a much stronger performance as I said in the second half. And the business was fully like-for-like in the second half after the Argos consolidation. And you will recall in the first half UPBT was down. EPS is down, reflecting a full year's dilution of shares issued in relation to the HRG acquisition, dividend per share is flat with a final dividend up 8 per cent. Non underlying costs relating to three main areas, the new bank programme, the Argos integration and the recently announced re-organisation of our management teams in-store.

In the year we saw sales growth across all channels. We grew like-for-likes by 3 per cent and taking out the impact of consolidating the Argos and Habitat businesses, sales grew 1.6 per cent with strong performance from the grocery business with growth of 2.3 per cent. In general merchandise we outperformed a very tough market, gaining share despite some drag from the closure of Argos stores inside Homebase stores. And clothing grew just under 4 per cent across the year. And we were pleased with the consistent strength of our grocery online and convenience businesses.

Our grocery business had a good year. We saw an improving margin trend particularly in the second half and transactions grew ahead of the market. We continue to innovate, launching 128 range reviews to offer customers the quality they expect. We further enhanced our offer by reducing prices in over 900 products. And our store teams did a great job offering customers market beating service and availability.

We are currently our store operating model to ensure that we can continue to deliver this level of service while remaining efficient and paying our colleagues competitively.

In a challenging general merchandise and clothing market we are pleased with our performance. As I said, we grew clothing sales by 4 per cent, online clothing sales grew 45 per cent and we are delighted with the early customer reaction to the launch of Tu in Argos in the last few weeks. We grew share in general merchandise with particularly strong performances in areas like audio, mobiles and video games. In the year we continued to invest in making it easier for our customers to shop with us. Demand for our popular fast track service grew strongly. Over 40 per cent of customers now start their shopping trip with us on their mobile. And we are very pleased with the performance of the Argos stores in stores inside Sainsbury's where we have seen strong sales growth.

We have a proven track record in delivering synergies from the HRG acquisition. This year synergies totalled £87 million which is ahead of schedule reflecting progress made on buying common goods and services more cheaply and the successful rollout of Argos stores inside Sainsbury's stores. So we are very confident in that we will deliver the £160 million total by the end of this year.

Moving on to the Bank. The Bank delivered a good performance this year in a challenging market. Sainsbury's shoppers made up well over half of the Bank's 1.9 million customers. Net interest margin has increased to 4.9 per cent with the inclusion of Argos financial services. However excluding Argos financial services the net interest margin has been impacted by the continued pressure in the unsecured market. As expected we saw a modest tick-up in bad debt year-on-year again partly down to full year of AFS. Our bad debt ratios remain low compared to peers. And our capital ratio has increased to 14.1 per cent in the year and the total capital ratio has been boosted by the £175 million external capital raised in November.

In the year just started we expect Bank profits to decline. There are four factors at play here. Firstly, tighter profit margins on new lending and reduced lending. And second year predicted modest increase in bad debt provision in the current climate. That will take us from £69 million to £48 million effectively like-for-like. The third factor is the cost of Tier 2 capital that I mentioned that we raised. And finally there is the cost of the new IFRS 9 accounting standard which basically has a more conservative view of how you provision for bad debts and this is something that clearly will be applied right across the banking sector.

In the year we delivered strong free cash flow of £432 million, up year-on-year strongly, which allowed us as I said to reduce out net debt to under £1.4 billion. And at the year end our adjusted net debt to EDITDAR ratio reduced from 3.7 to 3.2. We refinanced our evolving credit facility extending maturity and in April in addition we repaid our Eddystone bond of £568 million from cash resources. Our combined pensions deficit reduced from £850 million to £261 million at the year end.

As you know, our aim is to reduce debt over time and we are targeting adjusted net debt to EDITDA ratio of less than three times, and fixed charge cover of greater than three times.

So looking forward in the current financial year we expect inflation of around 3 per cent. Against this background we have plans to deliver further £200 million of cost savings and £60 million of EBIT from synergies. As noted earlier, we expect the profits of the Bank to reduce and we are comfortable with the 2018 consensus of £629 million. In the year we are targeting a further reduction in net debt of £100 million and as a result of re-paying the Eddystone bond we expect net finance costs this year of around £100 million.

I would now like to hand you back to Mike. Thank you.

Mike Coupe
Group Chief Executive Officer
Thank you Kevin. Good morning everyone. I am going to take you through the details of the historic transaction that we have announced today. First I would like to start by thanking a number of people in this room who have worked incredibly hard to get the transaction to where it is today, not least over the last 48 hours where a lot of midnight oil has been burnt in order to get all the transaction documents up to shape for this morning.

Secondly I would like to extend my personal thanks firstly to Dave Cheesright, who is not with us today. He has been instrumental in getting this transaction together from the Walmart side. He has clearly stepped down as the Walmart Head of International. And I would like to thank Judith and Roger for their help and support also over the last period of time in their pragmatic approach to getting this deal to where it is today.

And my last thanks are to both of the respective Boards. The Walmart Board, Doug McMillan and the Sainsbury's Board, chaired by David, have enabled this transaction to occur through a very pragmatic approach of breaking through the various hurdles that we have to in a situation like this. So I thank those Boards for their help and support. And from a personal point of view, I am incredibly proud that both Boards are putting their faith in me to see this transaction through to completion and ultimately to lead the business into the future. So that is a great position for me to be in.

The other point I would emphasise is that a lot of the people that I have talked about know each other extremely well. So Roger and I go back a long way, indeed we started our careers together, or at least we first knew each other in our Asda days as well as subsequently working together within Sainsbury's. And again Judith and I go back a long way. We worked very closely together within the Asda business as well. So there is a lot of shared history amongst us and that gives us confidence in the way that will bring these businesses together in the future.

I'll start by talking about the combination. We have talked about a dual brand strategy. This is about the best of both and this is about making sure that we maintain the strength of the two businesses. But we can use the synergies that will be generated by this deal to sharpen both the customer propositions.

Asda is consolidated on a debt free, a cash free and a pension free basis. Walmart will continue to be a major shareholder with a 42 per cent shareholding in the combined business, and 29.9 per cent of the voting rights. And Sainsbury's will pay £2.975 billion of cash to Walmart for the transaction.

Judith will talk about this in some depth later on but Walmart will remain a long-term partner and will have two seats on the PLC Board. I would expect this transaction to go fast track to the CMA phase 2 review and we will anticipate completion in the second half of the calendar year 2019.

So it is worth just standing back for a second, talking about the market and why this transaction is right and right for now. The world that we live in is changing and changing very rapidly. Customers have more choice than ever, whether it is the discounters, whether it is convenience stores or whether it is supermarkets. Whether it is online channels. And of course the rise of digital technology has amplified that and if anything the speed of change is accelerating and not decelerating. And competitors that couldn't have even existed 10 years ago are covetously looking at the markets we operate in and we believe that it is important for this transaction to take place to make our businesses fit for the future.

And you can also say on that side, some of the downsides of not reacting to those market conditions because clearly if you don't adapt and you don't adapt fast enough then ultimately that will lead to businesses going out of business and that is an important factor as well.

We think it is a great deal for everyone. We will create a more dynamic, more adaptable, resilient business. For customers that will result in lower prices, better quality, differentiated ranges and more flexible ways to shop. And the company will be a major contributor to the British economy, it will be a UK listed Plc and one of the top 5 taxpayers, corporate tax payers in the UK overall.

For colleagues it is a stronger business employing over 330,000 employees with more job opportunities and indeed by bringing the businesses together we create more security for both sets of pension holders. And overall there are around 300,000 people who rely on one of the other of the businesses for their future pension provision.

For suppliers we will offer greater efficiency, we will offer the opportunity for differentiated ranges. And of course through the combined entity, the opportunity to grow into the future. And last by no means least, for shareholders we create value. We increase the strength of the balance sheet. The combined business will have very strong cash generation and will have investment grade profile.

So if we look at the shape of the business. Clearly by bringing the two businesses together it will strengthen the overall proposition within the UK market and these market shares are based on the total market. Some of the numbers that get quoted are the Kantar definition of the market which actually takes into account only about 70 per cent of the volume in the food market. So the combined entity will have roughly 25-26 per cent of the grocery market. But of course we will become a much bigger player in the clothing and general merchandise as well. And as you can see from this slide, Asda already has a number two position by volume for the George clothing brand. Sainsbury's has grown the Tu clothing brand over the last number of years and again is number six by volume in the UK marketplace. And the Walmart, Asda scale can bring significant benefits to customers through range and through lower prices to customers.

The other opportunity is through the Argos transaction. We believe there is an opportunity to put Argos stores in Asda stores as well as Sainsbury's stores and that is a well trodden route that we understand and clearly we have modelled that as part of the overall transaction.

The businesses have highly complementary store portfolios, and I think this chart illustrates it brilliantly well. Sainsbury's is strong in the South-east of England and Northern Ireland. Asda is strong in the Midlands, North of England, Scotland and Wales. So a very complementary store portfolio and I think people are surprised by the slide on the left-hand side or the data on the left-hand side. Actually the average store size is almost identical. Sainsbury's stores on average are actually slightly larger than Asda stores. But again if you look at the profile of the size of stores you can see again it is pretty complementary. Now of course that doesn't take into account the Sainsbury's convenience shops, but it gives you an idea of the complementality of both the geographical overlap and also the store size overlap.

I am now going to hand over to Rog who is going to talk a little bit about the Asda business. Roger.

Roger Burnley
Chief Executive Office, Asda
Thanks Mike. Morning everybody. Good to see you all and great to be here this morning. I know quite a few of you but for those I don't, I am Roger, I was at Asda as Mike said for six years, back when I had hair, I then had 10 years on the Board at Sainsbury's and I have now been back at Asda two years, firstly as COO and now as CEO. So that's me. It is fair to say therefore across that I think I am a reasonably good judge of the fit of this combination and I am as excited as anybody about what this means for the newly formed Group.

So first of all a quick overview of Asda. I am conscious it has been a while since you have heard from us. We are for the avoidance of doubt, multi-format already. We are a large-scale national business as Mike said, strength in the North, Scotland, Wales, but we are a national business, we have 19 million customers a week. We are multi-format, our store size goes from 8,000 square feet to 160,000 square feet with the average pretty much bang on identical. We have a grocery online business which is going gangbusters. Growing low in high single digits last year. We have a George.com business which is growing really well at over 30 per cent year-on-year growth last year. And we have 33 Asda the living stand alone general merchandising clothing stores and 18 stand alone petrol filling stations. So we are pretty Omni channel already and that is certainly growing. We have an undisputed EDLP heritage, low prices is in our DNA and that is something we are really getting back to and that is part of our momentum that I will touch on in a second.

We have our strength in general merchandise and clothing, George is a fantastic brand as Mike said, number two for some time now by volume in the marketplace. And our George home business is growing really well, 12 per cent year-on-year market share growth last year in our George home. So strong heritage in general merchandise and clothing. Food sourcing strength too, we have IPL international procurement and logistics which is our fresh food sourcing arm, where we fresh and process across the UK everything from flowers to wine, to protein to produce which gives us significant cost advantage. And of course we have Walmart support that we have touched on which as been there for 20 years across technology and digital, across sourcing, especially general merchandise sourcing and across people and development and talent.

Last but not least, we couldn't do any of that without our talented colleague base with very similar values and culture to Sainsbury's. So that is where we are a great fit. And very last but not least, I have a strong leadership team where we have across my Exec, experience of working in retail across twelve different countries, so a good strong leadership team in the business.

Can't talk too much about our financial numbers, we are not listed and our year end numbers aren't yet audited. But just a flavour, I wouldn't want to not show you the strength of our financial position. So first of all we are delivering growth, we have momentum back, we have delivered four consecutive quarters of like-for-like growth. We have healthy profit margins, healthy profit margins despite a significant investment in the proposition last year. Cash flow generation strong, £4 billion between 2014 and 2016 and that has carried on through last year as well. And last, but not least, with strong asset backing, very low net debt and 75 per cent freehold, our estate. And as I say, very low net debt, a great position for a retailer to be in these days.

And as I said, we have momentum in the business. We have got our mojo back as we say internally. So we have got consistent like-for-like sales growth. First of all that is coming from accelerating our EDLP credentials, getting back to everyday low prices as well as investing in price itself. We are improving quality, we reformulated over 1,400 own label products last year. We won over 700 awards last year as well for our own label products. And we have got back to being first choice destination for big events which has always been our heritage and we have really got back to that last year, finishing the year with a fantastic Halloween and a fantastic Christmas as we got back to being a destination for big moments for people.

We are further developing our digital and online capability as I said, driving more sophistication in our home shopping offers, picture there is a parcel tower, a direct import from Walmart in the US where you can collect your parcels in under 90 seconds. And that continues. We will have scan-and-go in 200 stores by the end of the year which customers really tell us they love and keeps them in control of their shop. So lots more development online and digital capability paying dividends.

And last but not least, we are improving our customer experience particularly our availability. More work to do in both of those areas. So we are moving the dial but still more work to do and more opportunity there.

So we have momentum, we are doing all the right things and our strategy continues to invest in all those things, but no danger this combination really allows us to accelerate that strategy and do a really great job for our customers.

Thank you. Mike

Mike Coupe
Group Chief Executive Officer
So let me put a little bit more colour on the combined businesses. So a dual brand strategy. We will keep both of the brands. Both brands have very distinctive propositions. I saw a number of customer interviews on the TV over the weekend and customers get this. They get what the brand stands for, they have got very clear propositions and they understand how the combinations could work together which is great news. But we will invest in price and we have talked today about the fact that we can see our way to reducing the prices of

everyday items by 10 per cent and that is the aim of the combined entity as we look forward and that is above and beyond the price investments which both businesses are making over the next period of time.

As Roger has already said, there are opportunities to look at sourcing and IPL is an example of that and that could certainly enhance the quality of Sainsbury's products and of course it works the other way round as well. Sainsbury's has a great heritage in fresh foods, a great heritage in added value fresh food products in particular and again that quality and those products can be brought to bear in the Asda business.

And last but by no means least, both businesses are making very substantial investments in helping customers shop more flexibly and of course that is enhanced by the relationship that Walmart has and will have with the Group in the future and Judith will talk about that from the Walmart perspective in a second.

If we look at grocery, both businesses have strong online grocery businesses and have an increase in instore technology and Roger talked about scan-and-go. Sainsbury's has an equivalent which is smart-shop. And increasingly customers will be using those types of digital interactions to shop more flexibly with our types of businesses in the future.

Sainsbury's has a very strong position in convenience stores, 800 convenience shops. The best quality real estate in the industry, a track record of growth and market leading sales densities.

And we mustn't forget the combined strength of the Group as far as general merchandise and clothing is concerned. So with Argos we have a tech led general merchandise business. That brings the third most visited website to the organisation with 60 per cent of sales online and now over 1,000 store points of presence. We also have a strong and fast growing online clothing business in both businesses. So whether that is George online or as already been alluded to by Kevin, the launch of Tu online with Argos. So again not just strength in scale, but also strength in the growing channels to market.

For colleagues there are more opportunities within a larger Group. We have talked about the dual brand strategy, but with 330,000 colleagues in the combined businesses that shows you that there is a huge scale of opportunity for our colleagues at all levels. And the business will be run by the best leaders from both businesses. And as Roger has already talked about, Asda has strength and depth as does Sainsbury's. So again tremendous opportunities for the leaderships of both businesses. And Asda will be run from Leeds and we will keep both Head Offices. Sainsbury's will be run from Holborn, Asda will be run from Leeds by a separate management team.

We have a shared set of values. So both businesses are built on a values based heritage and as one of the largest employers in the UK, we will be a major contributor to the UK economy and a major taxpayer as I have already said. And by bringing the businesses together and by Walmart retaining the Asda pension, that improves the covenant for the Asda pension holders and of course the combined entity will improve the covenant for the Sainsbury's pension holders. So in both cases pensioners for both organisations will be in a better position overall.

For suppliers there is a great opportunity to grow with a larger business. More supply chains mean more efficiencies as far as suppliers are concerned. Both business again have a heritage of bringing new and differentiated products to market and that opportunity will continue in the future. And it will protect choice for customers or we will protect choice for customers in the future.

If I talk a little bit about the buying synergies for the next synergies, the first point I would make is that the gross synergies are substantially higher than the net synergies we are talking about on this slide. The net synergies, the £500 million is what we will deliver to the bottom line of the combined entity at the end of the second complete year of the combination. If I talk specifically about the 500 net synergies, 350 million of those net synergies are coming from the buying synergies and that is primarily focused on the grocery business. And all you have to believe to believe that number is that the best terms for either of the companies will be applied to the overall buying book. It does not take into account any further volume benefits that might be accreted from the combination of the two buying books. And that is backed by a huge amount of analysis and data done by an independent third party.

Within the property synergies, that is mainly on the basis of putting Argos stores within Asda stores. We understand that model and we understand the benefits that will come from reducing rent rates and overall overheads within the Argos portfolio by making those moves. So again we understand those synergies and they are pretty much nailed on.

And the last point is operational efficiencies where again through the Argos transaction we committed to around £70 million of synergies outside the day to day trading of the two businesses mainly around what we would call goods not for resale. So all the things that we buy that we don’t sell, so whether that is energy, whether it is advertising, whether it is IT. So again we believe that the £75 million of savings is more than achievable at a net level. And that is before we get into other potential synergies. So whether that is cross selling within the combined business, leveraging fixed assets, and indeed the benefits of the strategic partnership with Walmart. But I go back and just stress that this £500 million is a net synergy number, there is a gross synergy number which is higher than that and that is what gives us the capacity to invest back into the underlying proposition.

So we would expect those £500 million of EBITDA synergies to drop to the bottom line of the combined entity by the end of the second year. We are assuming £150 million of operational implementation costs and £600 million of capex which is largely on the basis of the investment in systems to bring Asda onto the Sainsbury’s systems platform and off the Walmart systems platform. But also a level of capex in moving Argos stores into Asda stores.

Our phasing assumes that we complete this deal in the second half of the calendar year 2019. So somewhere between 12-18 months from now so actually slightly more than that, 15 and 21 months from now.

If you combine all those numbers, the combined entity compared with Sainsbury’s EPS, we will have double digit EPS accretion. Low double digit ROIC and a substantially reduced level of leverage and that will create value for shareholders.

So just to give a bit of colour to the strength and balance sheet, if you look at the middle chart you can see that the net annual lease charge for the two businesses, and that is a reflection of the fact that the Asda portfolio is around 75 per cent freehold. And even if you make it on a comparative basis, so on a supermarket for supermarket basis, the Sainsbury’s lease charge are about £450 million and so you can see how the freehold/leasehold split will change and strengthen the balance sheet. Walmart will retain the Asda defined pension scheme and therefore there will be a lower lease adjusted net debt to the EBITDA ratio. And the combined Group will be very, very cash generative.

So to summarise, it is a great deal for everyone a more dynamic, more adaptable, more resilient business for the future. Great for customers because of lower quality, sorry lower quality! Lower prices, better quality, I almost got through it! Differentiated ranges, more flexible ways to shop. And we shouldn't underestimate the fact that this will be a British Plc and a massive contributor to the British economy. For colleagues a stronger business with great opportunities all round and greater security for pension holders. For suppliers, greater efficiency, differentiated ranges and an opportunity to grow. And last but by no means least, for shareholders the opportunity of creating value, a stronger balance sheet, stronger cash generation and investment grade credit profile.

So now I am going to hand over to Judith who will talk a little bit more about how Walmart see this deal. Thank you.

Judith McKenna
President and CEO, Walmart International
Good morning everybody. It is great actually to be back in the UK, perhaps not for the weather though, but it is nice to have a decent cup of tea I have to be honest about that. So no, it is great to be here. There are a few familiar faces here today, but for those of you who don't know me, I am a 22 year associate with Asda and with Walmart. So 17 years as a colleague in Asda and the last 5 years working in Walmart in our US business. So I have the unique position of being able to talk to you today both with an Asda hat on but also to represent Walmart as we are going through some of the transaction.

What would I tell you first? Well probably just a quick overview of Walmart. I don't actually how many of you are probably familiar with the details of it. I think the number are pretty well known in terms of the sales and market capital. But what sometimes people don't realise is that we operate across 28 different countries. We have 65 different banners that we operate in. And then we have 11,700 retail units. So about just over 6,000 of those are in our international business and we are serving an outstanding and credible 270 million customers a week.

But Walmart is actually, that is only part of the story because Walmart has in the last few years been transforming itself. You will have read no doubt about our leaning into digital, online and Omni channel. But equally we have been much more open to new partnerships and particularly created two new partnerships. One is Rakuten in Japan and the other one is JD.com in China both of which have really helped us build capabilities in our business that we didn't have previously. And that is important as we think about this combined business. And before I talk you through where are we from a Walmart international strategy, a little bit about the partnership principles that we would apply and how we feel about the new business. Let me just give you the top line of how we look at this.

From Walmart's perspective this is an opportunity, a unique opportunity to create a vibrant and resilient UK business, a Plc of the combined business that will be able to lower the cost of living for UK customers. And it is able to do that and that got us thinking is that these new ways of operating where we shouldn't be wanting to do everything ourselves. We have learnt as a business that we can be mature and that we can actually say we can sometimes add more value by not being in the majority and creating working relationships that have the benefit of the scale of Walmart, but not necessarily having a sort of controlling shareholder within that. That is very unique in the way that we have been thinking, it is unique to this market as well. And speaks very much to how we see the two businesses coming together. And one of the things about that is it allows us not only to unlock value. We have talked about this for customers, for shareholders, for colleagues, I have to remember to say colleagues back in the UK again, it is associates. It took me three years to learn to say it the other way around. For colleagues and also of course for our suppliers.

So we can do that, but not only can we do that, but Walmart can actually maintain an active share in the UK market which is one of the most competitive markets in the world. We can contribute to the new business. And what is really important for us is we think about this as a long-term. Because it is not so much about the deal that is created today, although it is extremely exciting. It is also about the share value that we can unlock in the long-term as the businesses combine.

So if I just touch on how does that fit within the Walmart international strategy. Well many of you will have heard us talking about the fact that we have been very deliberate and thoughtful in our review of the international portfolio. Perhaps in a way that we haven't done before. What you know is that we are transforming the business. And actually this is probably the boldest move that we have made so far as we have looked at that portfolio and thought about the focus for the business overall. This building of innovative partnerships, and strategic partnerships is a key part of what we do and will continue to be a key part of how we operate the international business in the future. And what is really important to us is creating strong, agile, local businesses, locally relevant for customers right around the world.

So as we thought about that and this focus that we have got within the international strategy, we were putting down what are the real partnership principles that are important to us as a business? And the first is really simple, it is all about shared values and around culture. Because what you know is that mergers don't work because of what you write on pieces of paper or what bankers or lawyers contribute on the day that you sign the agreement. They work because of the people involved. And the single most determining factor is do you have a cultural fit between organisations when they come together. And I think you have heard both Roger and Mike talk about how that is a really strong fit for us as a business. That was one of the key principles for us.

The second area which is true to the DNA of Walmart is low prices. And one of the great things about this combination is the ability to lower prices for customers across both of the brands that we will be running. Omni-channel, seamless and convenience. Customers are expecting not just to save money these days, but to save time as well. So one of the partnership principles that we have got is how do we lean in more to an acceleration of omni-channel? You know when you look at these two businesses coming together, you think about the geographic fit for them and you think about the access that gives customers to the combined businesses.

And finally, I have already touched on it, this is all about long-term value creation as well. It is incredibly important to us to not just be about the here and now, but to really think about it for the longer-term and how we can create value and share in value going forwards.

So this for us creates a really dynamic, new player in the market. It is important to create a strong UK Plc independently governed with the backing of Walmart. That is what makes this completely unique. The business will be stronger and it will be healthier and it will be more resilient for the future. And one of the things that we bring to the party is our global expertise. And you are probably asking yourselves well what exactly is that?

Well the key three areas that we would look at. The first is global sourcing. And global sourcing applies. We have a global sourcing business within the international business that operates across the entire business right around the world including the US. General merchandise sourcing is probably our strongest element of that. And you can imagine and unlock for the joint business going forwards.

The other area is technology and again Mike and Roger have both touched on it. You have seen everything from pick-up towers that we have created. But the other thing that when you think about those markets that we operate in and you think about a market like China which is probably one of the most advanced eco systems and e.commerce markets in the world, we operate there. And we operate there effectively. And one of the things that you have to remember there is that six years ago China was cash on delivery if you took delivery of an item that you had ordered online. Today, it is as I said, the most sophisticated market in the world from a financial payments perspective and from an e.commerce perspective. That, Alibaba competing with those kind of people is something that we have really, really got some experience on and hope to be able to bring to bear, not just for this market and you know for Roger and the team and the combined business that right around all of the businesses that we operate in.

So we see this as a real opportunity to create a winning combination. It fits in with our international strategy. It is good for both of the businesses and it means that we can deliver long-term value into our shareholders as Walmart as well.

So with that I am just going to end with where Mike started which is a huge thank you. A massive thank you to both of the teams who have worked so hard on this in the last couple of weeks, but particularly as you can imagine we pulled this forward a little bit in the last couple of days to get this done. And I think what it does show is the confidence that people should have in how the teams can work together in the future as well.

So with that Mike, I will invite you up as well and we will do some Q&A.

Question and Answer Session

Question 1

Bruno Monteyne, Bernstein
Thank you, Bruno Monteyne from Bernstein. Two questions from me. In previous analysts' meetings Mike, we have often discussed the consolidation in the UK and your answer always was whatever pair of UK retailers you took they would take about 20 per cent of disposals which would make it uneconomic. What has changed in your thinking about necessary disposals? Or what has changed you think in the CMA thinking that would suddenly make these disposals less painful?

The second one is you make several times reference to shared cultures and values. But just going back to the horse-gate scandal a few years ago, you made it quite clear that the values and cultures of Sainsbury's was very much focused on the integrity of sourcing, knowing where your food came from and things like that. And therefore you were the only big 4 grocer who didn't have and wasn't tainted by the horse meat scandal. But then you make a big point of how different your culture and values were and how many other retailers just focus on the cost of sourcing their ready meal and that might describe Asda in many people's views. So what has changed in your view in the difference of cultures since those days that you suddenly think it is a good culture fit for the two companies? Thank you.

Answer: Mike Coupe
Thank you. I think you are putting words in my mouth. I don't recall ever using any reference to a number of disposals, certainly not a 20 per cent reference to a number of disposals. And clearly the CMA is a critical part, or the CMA process, is a critical part of this transaction. We go into it with our eyes wide open. A huge amount of work has been done by both companies. And it is very different to the last time this market was investigated which was 2007 or the last time a major transaction took place which was in 2004. And so if you take some precedent transactions, they are not directly applicable. But whether you look at Ladbrokes-Corals or Tesco-Booker, they are significant points of principle that have been established through those transactions. One being for instance that national competition is a result of local competition and therefore you have to aggregate local competition to get to the answer around what you may or may not have to do as a result of the CMA process.

As I say, we go into this with our eyes wide open, we have done a huge amount of work on thinking about the process. In the end the CMA are there to protect consumers and they will look at this deal from that perspective. We think there is a fantastic customer story in this. We have talked about that today. We think ultimately this transaction will act to the customer good. I will finish if I can. And we think that ultimately we will get to or the CMA will get to the right answer for the customers and that should be from our perspective the right answer for shareholders.

We have also been absolutely clear, and this is probably the biggest question I have been asked over and over again on the media this morning, there will be no store closures as a result of this transaction. And indeed the CMA I think would set out with that as an objective as well.

As far as the shared cultures are concerned, yeah we all have our ups and downs in terms of the day to day running of our businesses, but I have worked for Asda, I have worked for Sainsbury's, they are incredibly people centric organisations. They start with people at the heart of the organisation and both businesses believe that if we treat our colleagues right they will serve our customers better and ultimately that will deliver a better outcome for customers and a stronger business and I don't know if Judith will want to reflect at all on that from a Walmart perspective?

Further answer: Judith McKenna
I would agree with you completely. I think in reference to sourcing of food particularly, Walmart has done a tremendous amount of work in the last few years and that Asda team as well to improve the sourcing of our food and the traceability through that as well. So sometimes these things happen and I think what a real measure of the business is, is how you react to situations like that. And what you do as a result of it. So clearly for us, you know we have world class compliance programmes and we are much clearer now in the traceability and the tracking. You might have heard about us doing some blockchain work in China for example. That means that it's just one area, there are far bigger areas as Mike said, it is really about people and what you care about which is people in the organisation and customers.

Further question
Maybe just a small follow-up. No store closures but if there were any store disposals that would be in your expectation of the difference between gross synergies and net synergies, is that correct Mike so there is a scope for disposals which would be planned for?

Answer: Mike Coupe
Yeah we have made some underlying assumptions as you might expect us to. But clearly we can't pre-judge the outcome of the CMA. But we believe that there is a relatively, in fact a conservative case that we put to you today. I am sure you can do your own arithmetic and there are some analogy stills that might give you some clues as to the kind of gross synergies you might expect. And when you net them back to the net synergies that takes into account any outcomes that may come from the CMA and any investments that we need to make in the propositions whether that is price, quality, value or ineed service.

<u>Question 2</u>

Charlie Muir-Sands, Deutsche Bank
Great, thank you. It is Charlie Muir-Sands from Deutsche Bank. The first question, you talked about obviously the ambition to lower your prices on some everyday lines by 10 per cent. You have already reaffirmed full year FY19 guidance despite the let's call it a profit warning in the Bank. So can we expect that that price investment comes when the deal completes?

And then the second question related to the Bank, I think Asda Financial Services which only operates as a Broker, made about £35 million in the last subsidiary accounts that were filed. Do you think that the Sainsbury's Bank would want to take that on or conversely you would want to move back to being a Broker which seems to be a much lower risk, lower catchment type operation?

Answer: Mike Coupe
Yes so in answer to the first question, speaking for Sainsbury's we have a programme of cost reduction of efficiencies and ultimately the re-investment back into underlying pricing and not to put words in these guys mouths, but I expect the same is true of the Asda business and the price reductions we are talking about are post completion as a result of the buying synergies and it often gets confusing, but just because you make savings over here it doesn't necessarily mean that you want to invest those savings over there. You might want to invest your savings somewhere else in the portfolio of products and the things that matter most to people are the things that they buy every day week in, week out. So in terms of the Bank, I am not sure I can speak and maybe ask Judith to talk a little bit about Asda Financial Services?

Further answer: Judith McKenna
Yeah just to go to the first point as well within that which is, we are really focusing on how we can lower prices at Asda. And you have to remember that during the period in which and before the two businesses can combine, we will still be competing with each other. And I am sure, I don't want to speak for Mike either, but I am sure we will both be really focusing with Roger and the team on lowering prices overall.

As far as the Asda Financial Services is concerned, Asda made a decision several years ago to not be within the Banking business. That was an active decision of the portfolio. And interestingly we since disposed of some of our banking businesses in areas like Mexico and some of those. It is just a difference in approach and I think it is one of the things that the combined business will be able to look at in the long-term and see what the right answer is.

Further answer: Mike Coupe
So it is just worth again. We focused on some obvious things about the regulatory situation you know that by far and away is the biggest thing that has concentrated minds over the last period of time. And we focused on the areas where the biggest buckets of synergies and self evidently the biggest bucket of synergy is bringing together the buying books and we have a high level of analysis and confidence in our ability to deliver a gross synergy number as well as a net synergy number. There are a whole bunch of things that we know about that we haven't addressed at all as part of this conversation process. Bank would be a very good example of that. Whether or not you would apply the Nectar scheme to both businesses would be another example of that etc. etc. So there is a long list and I am sure we will get lots of questions, there are probably 20 or 30 items we haven't addressed directly because of the need to get to a position where we were 100 per cent sure that we can deal with the regulatory issues and could stand up the synergy numbers at a high level of robustness. But clearly it goes without saying there is a whole bunch of things that we haven't even factored into our calculations which go way beyond the numbers we talked about today.

<u>Question 3</u>

Dave McCarthy, HSBC
A couple of things. One is currently there is a very wide price differential between your two businesses. How would you see that in the future? Would you look at that to narrow? Would you run the businesses at two different price lists?

And then secondly, on the synergies, have you taken into account any harmonisation arranges, you know you have different pack sizes? You have different promotions at different times? What about Own Label, will you go to the standard supply for, the one supplier for Own Label and just do different labels, different packaging for them? You know there is obviously substantial synergies there, but it has implications for suppliers because they have got to be big enough to supply both of you. So can you talk around all of that please?

Answer: Mike Coupe
I can have a go. I think the first thing to say is 18 months is a long time in grocery retail. So let's caveat anything that is said on the basis that the world will change and a whole bunch of assumptions that might be true today might not be true tomorrow or in 18 months time. I am not going to get into the detailed strategy of what the world might look like post the coming together of the businesses, post merger. What we have talked about is the fact that there is an opportunity to sharpen the proposition for both brands. You can draw your own conclusion as to what that might mean in terms of the relative pricing, quality, service strategies of the two businesses. But beyond that I think it would be giving too much away in terms of what we may or may not do in the future, and indeed to pre-judge in 18 months time what that might look like. I think that would just be a hostage to fortune. So let's not get into that.

As far as the buying terms are concerned, as I have said already, all that the synergies are predicated on is a SKU for SKU comparison, some of which are pretty obvious and pretty easy like you can compare brands. Some are relatively straightforward if you look at the Own Label portfolio where commodities are the same across both businesses. And again you can do a pretty comprehensive job of SKU matching. And then there are some products which are clearly very different in the organisations and that becomes a bit more nebulous. So all that is assumed in the buying synergies is the equalisation of terms on the basis of the best price of either business.

It is worth emphasising that 85 per cent of the volume of both businesses is concentrated in 100 suppliers and those 100 suppliers tend to be large multi-national suppliers, not exclusively branded, but nevertheless large multi-national and largely, not exclusively, branded suppliers which is another important factor in thinking about how the synergies are delivered. But it goes without saying on that basis that there is a best of both strategy in terms of buying and sourcing. You could imagine over time that some products probably starting with things like base commodities could be sourced through one supplier rather than two. But that is not factored into any of the synergy numbers and so you could argue there is another throw of the dice above and beyond just equalisation of terms which is, we have got to combine volumes and therefore there is a future benefit from that. But that is not currently in the numbers.

Further answer: Judith McKenna
And potentially that is where the global source and capabilities of Walmart when it comes into commodities, could help support both businesses and both private label programmes.

<u>Question 4</u>

James Tracey, Redburn
Good morning, James Tracey from Redburn, three questions from me. In the past you have said that the rationale for the Argos deal was that you couldn't consolidate within grocery so that you would consolidate retail sort of horizontally. You talk about cutting prices as a benefit of this transaction, but surely it was always thus. So what has changed in the market that makes you think it will be approved by the CMA?

Can you give us a sense of how many stores you will likely be forced to sell?

And finally can you just talk us through whose idea it was and some of the thinking behind the scenes in what created this deal in the first place? Thanks.

Answer: Mike Coupe
Well as Bruno said at the very beginning, I don't think I have ever shied away from the possibility of the market consolidating, and in fact I have often said it is inevitable that it will in some shape of form. And even before this transaction there is a whole series of things that have happened, Nisa-Co-op, Palmer and Harvey going bust, Tesco-Booker which are forms of market consolidation. And in terms of the sweetheart combination, if you look at the geographical spread, the relative size of the buying portfolios, in this particular case the power and strength that Walmart would bring to the combined combination. All of those things mitigate for this being a great opportunity for both businesses.

And we can argue about the timing of it, but we believe that the timing is right and that is at least in the context of the Competition Authorities. And I go back to what I have said already. In the end the Competition Authorities are there to act on behalf of customers. We have done a huge amount of homework on this and so we are absolutely clear on the perameters that we are dealing with. The CMA is a rational, logical organisation, largely run by economists and as long as you understand the models that you are working with and you have a fair idea of the inputs you are putting into those models, you will get the outputs that you expect and we have done a lot of work on this and we have a lot of understanding about how this will be approached.

I have experienced in the last few years, three transactions, Argos would be another example. I sit on the Board of Greene King, where there is a major transaction that was undertaken and indeed Sainsbury's sold its Pharmacy business to Lloyds. And what I would say is that all my experience would say that despite the fact that you go through a process, you do get to an answer that you first thought of by the end of it. So again that would give me confidence in having some sense of what the outcome might look like. In the end we can't pre-judge this. And we are not going to get into a conversation about disposals or anything else that might be a remedy for this transaction simply because we will engage positively with the CMA, we will engage in a Phase 2 process as quickly as we possibly can and we will get to an end point as quickly as we possibly can. But there are a whole series of assumptions or rather principles which have been established by the Competition Authorities through a number of precedent transactions. I give Ladbrokes-Corals, Tesco-Booker, even Nisa-Co-op and the way that they would look at the competitive environment. And it goes without saying that the market and the competitive environment is changing incredibly rapidly. And even something like Online as an example, representing 7 per cent of the grocery market is a factor that will be taken into account, that wouldn't even have existed as a consideration 5 years ago for instance.

Further answer: Judith McKenna
And I was just going to say on that, the thing what we don't really want to do is to spend the next 18 months speculating on how many that number is going to be. So I think Mike you put it really well, which is just waiting now to see what the outcome is. Assuming that we will have a decision which is positive for customers is the way we are going to look at this.

Further answer: Mike Coupe
On the, whose idea, how did this come about? I am not going to give you a huge amount of colour, but I made reference to Dave Cheesewright at the early part of my Presentation in effect like lots of people in our industry, we bump into each other every now and again and there was a lot of goodwill on both sides to look seriously at this transaction and I credit both businesses, both management teams and indeed the support of both Boards to come to

pragmatic solutions to a whole series of potential hurdles when you are going through the machinations of bringing together two very substantial organisations, one of which is owned by a US parent.

So what I would say, and I hope this augurs well for the future of both organisations is there has been a huge amount of co-operation I mean literally in the last 48 hours, two teams have sat in the same room and have knocked down a whole bunch of hurdles to get us to where we have got to this morning and to be able to make the announcements we made. And that is a credit to a large number of people in this room, but it is also a credit to the approach of both organisations to getting to where we have got to.

Further answer: Judith McKenna
Yes, it is very much a meeting of minds on this one.

<u>Question 5</u>

Dan Ekstein, UBS
Thank you, Dan Ekstein from UBS. I have got three questions. The first one is why did this need to be a merger rather than just a strategic partnership? If I look at where the synergies are coming from, a lot of it is buying terms. Could you not have just formed a procurement partnership? Another bunch is from Argos synergies, could you not have just agreed to open concessions in Asda?

And the reason I ask the question is just you know, given that you are continuing to run two separate businesses, would this have not been a way of getting the upside without the execution risk?

Second question is around Argos. I noticed in the Presentation for the Results that you are now targeting 280 Argos shop in shops by the end of this year, I think the synergy target was underpinned by 250. And yet you haven't upgraded your synergy target. So a synergy is dropping through but they are just being called something else.

And then the third question is on the sort of health of the core Asda business. Healthy profitability was referenced, but it has fallen quite significantly over the past couple of years, initially it appears through deleverage and then through some quite deliberate price investments last year. But another interesting feature I thought was that you said profitability in the first quarter had actually improved year over year. So does that represent the start of a more stable profit outlook for Asda? Thanks.

Answer: Mike Coupe
So if I have a go at the first two and then perhaps Roger can have a go at the third one. I think it would be incredibly difficult and probably impossible to structure the level of deal that we talked about through commercial arrangements. So whilst you are right, you can get some of the benefits potentially through some kind of commercial arrangement with let's say Argos stores in stores, there would be quite an interesting conversation about how you share the value of that. Similarly on the buying books, I think it would be very difficult to structure a deal that would motivate both partners to get to the right answer in terms of what that would look like. And I suspect it would be almost impossible with the oversight of the Competition Authorities to get to something that would work. And you could work in a way that would be allowed under the Competition rules. It is by far and away the best deal we believe and the best way of structuring this deal and we have looked very carefully at what the alternatives would be. So I make the point again that there are a whole bunch of things that both businesses can do that we haven't even scratched the surface of. So if you ended up having to structure a commercial arrangement for the other 20 things on the tick sheet of things we

could be doing together, I think it would just become almost, we would spend so much time in the lawyers offices trying to get to those arrangements, I think it would just be impossible.

Further answer: Judith McKenna
And Mike the thing that from Walmart's perspective, what we wanted to create as I said is a really strong UK plc that could move with speed and agility in this environment. And for us combining Asda into that entity was a really important part of this. But the reason we want to keep 42 per cent which is still a very significant shareholding is that we can unlock value back into the business as well, into the Walmart business.

Further answer: Mike Coupe
As far as the stores in stores are concerned, I think I have said it again before. We would like to draw a line under the £160 million of synergies, we have delivered those more quickly than we said originally, hopefully that augurs well for the transaction that we are also talking about now. And once we have delivered the synergies we won't talk about them anymore because in a business like this there are a whole bunch of, businesses like Sainsbury's there is a whole bunch of moving parts, some which get a little bit better, some which get a little bit worse. So for instance we have talked about the Bank today and clearly that has some drag on future profitability. But that has made up for elsewhere in the P&L and we have effectively confirmed consensus for Sainsbury's as a separate operating entity during the course of this Presentation which will kind of get lost in the noise of today. But within that confirmation of consensus there is a whole bunch of ups and downs which we have talked through and under normal circumstances I am sure you would be quizzing us on in more detail. So we delivered the synergies, we are committing to more Argos stores in Sainsbury's stores but we won't be talking about synergies once we get to the £160 million anymore.

Judith McKenna
Roger were you just going to talk on business?

Further answer: Roger Burnley
Thanks, I was just trying to remember what the question was. I won't comment on Walmart dividends through the years, but you can be assured that last year, sensible reinvestment backing the offer is roughly speaking cast forward as a sensible position for our profit position and investment going forward.

<u>Question 6</u>

James Grzinic, Jefferies
Morning James Grzinic from Jefferies. I have two, one for Mike, one for Judith. Mike can I just clarify, so the half a billion is net of disposal impacts that you've worked out, in your scenarios of what you think you will be forced to sell as part of the conditions to, for a approval?

Answer: Mike Coupe
Yes so we don't quote a gross number but you can take it as read the gross number is..

Further question
Much higher?

Answer: Mike Coupe
Well, higher than the net number [talking over each other] and again you are trying to put words in my mouth. And within the gross calculations, net calculation we have talked about price investment. We have talked about wider investment in the proposition. We haven't talked about disposals, but you could make an assumption about some level of disposals, but that is wrapped up in the underlying number. So one way or another we believe we have

got the bases covered and we have got the bases covered in a relatively conservative fashion. And who knows exactly how it will play out over the next period of time, we can't prejudge the outcome of the CMA but we have made some inherent assumptions in our base case which we are not going to go into any more detail than the detail I have already given you simply because it makes us a hostage to fortune, there are just too many moving parts, but as I say we believe the case that we put today is pretty conservative in its assumptions and I have already talked about for instance the buying synergy number and how that is calculated. And you could very easily get to a number which is substantially greater than that by making a different set of assumptions.

Further question
And my question to Judith was, can you just clarify come 2020 I guess Sainsbury's Asda or Sainsbury's whatever it will be branded will have full access to the global sourcing capability of Walmart?

Answer: Judith McKenna
So there is commercial agreements in place that gives the combined business access to global sourcing from the Walmart business. And that is over a defined period of time. That is a longer period of time than the lock-ups that we have.

Further question
You will do it for a wholesale fee that is not reflected in the Asda standalone business?

Answer: Judith McKenna
You have to have a, well actually if the Asda standalone business today accesses global sourcing, there is effectively a fee that is paid on doing that. This would be a standalone entity effectively even though we would be a shareholder. So you would expect us to do that. It is no different to our business in Mexico which is actually a public company as well. We are a 60 per cent shareholder of that business and is exactly the same way of working for them if they access global sourcing.

Further question
Okay, so next question, obvious question, if the position is very similar in terms of ownership to that of Walmex why did you want a cash component in the deal? Why did you minimise the equity investment, the equity exposure to the deal?

Answer: Judith McKenna
Because actually we didn't want to take a controlling position in this deal, 42 per cent works for us. It gives us the objectives that I talked about in terms of independent UK business, operated through an independent Board and the freedom and agility to operate in this market. We didn't want to go as a higher number and we are very happy with the split that that gives us.

Question 7

Nick Coulter, Citi Group

Hi, Nick Coulter from Citi, four quick ones if I may. Firstly on the underlying trajectory of the Asda business. You seem to be indicating that that has begun to stabilise. But is that on a like-for-like volume basis as well rather than just on taking costs out of the business?

Then secondly, on the Sainsbury business, a similar question. It looks like the underlying like-for-like volume trajectory is still down. When should we expect that to turn and what are the catalysts for that coming through?

And then thirdly, on the Bank, given the volatility of earnings and you continue to allocate capital to the Bank, I think it is 110 next year, and then a hundred million per annum thereafter. And given the sense of the capital allocation today, how do you justify that continued allocation of capital to the Bank?

And then lastly, just to help us with your accretion calculations, could you help us with the cost of debts for the £3 billion? Thank you.

Answer: Mike Coupe
Well I'll give Roger the, answer the first question and then I will probably answer it in exactly the same way. So Roger if you could just…

Answer: Roger Burnley
Yes the volume growth. We have experienced volume growth in the recent past and we are very encouraged by that.

Further question
So is that like-for-like volume growth?

Answer: Roger
Yes.

Answer: Mike Coupe
And you can see from the financial performance of Sainsbury's if we are talking independently we are pretty pleased with the results today. We have seen transaction growth throughout last year. We have made a series of choices of investments. We talked about for instance recently almost a thousand prices coming down and in the end at a high level, both businesses are pursuing not dissimilar strategies in terms of reducing costs and reinvesting that back in the underlying customer proposition and again Sainsbury's as an independent business is confirming consensus today which would imply earnings growth next year which we believe is more than sustainable, otherwise we wouldn't be saying it.

As far as the Bank is concerned, the Bank still is an opportunity. I mean there are still some one-off charges within the numbers that we have talked about. We do get to the end point of the systems investment which has clearly been a challenge for the organisation over the last period of time, but at least we didn't find ourselves in the TSB world of it completely falling over. I mean credit to Peter and the team, although it has been longer and more expensive than we would like, we have done it in a way that hasn't impacted our customers and so we are pleased to, in the next few months, to get to the end of that process. But we still think the Bank is an opportunity, we believe that the incremental capital that we will invest will accrete a decent return on the investments that we have already made. And you kind of have to draw a line under what has gone on in the past. You know there are a few things that we are uncomfortable about and will hold our hands up and say that there are some choices we have made that we would make differently with the benefit of hindsight. But we are where we are and it does not get away from the fact that the Bank represents an opportunity in the future.

On the cost of capital, I am not sure there is a lot we would say. I don't know Kevin if there is anything that would?

Answer: Kevin O'Byrne
We will be starting discussions with our bankers in the next few weeks as far as funding that. Clearly not really intending to sort of say what rate we are expecting to pay. But I think if you modelled a market rate you can work that out.

Further question
Are you talking about an IG rating, shall we assume that that will come through in your gap?

Answer: Kevin O'Byrne
We believe, clearly we won't know until we get there, we believe that this will be investment grade profile and we will get stronger because of the cash generation as we go forward, absolutely.

<u>Question 8</u>

Rob Joyce, Goldman Sachs
Morning, Rob Joyce from Goldman Sachs. Just two from me. So just back on those price investments, I was wondering if you could give us, I think 10 per cent on every day items, what sort of percentage of sales do you envisage that hitting across the two businesses? And maybe just give us some context on that because I think recent price investments from both of you have maybe been larger than 10 per cent on the headline items you have cut?

And the second one is just to confirm, maybe this is one for Roger, did you say that the outlook for the operating profit for Asda going forward was broadly flat versus what you delivered in 2017? Thank you very much.

Answer: Mike Coupe
Thanks Rob. I won't go any further than I have already gone. I mean we are talking about speculating about something that is 18 months down the track. The underlying point is that the focus of the price investment will be on everyday items, commonly bought items without getting into the detail of exactly what proportion of the portfolio that will be. And clearly we will want to have some flexibility or indeed which brand or brands we would invest in. So we would want some flexibility. And the point has already been made that both businesses are investing in price, as you have already said. And it goes without saying that if you think about the market dynamics I think you can draw your own conclusions as to the type of products you might be investing in in the future. And I will leave you to make that link yourself.

I don't know if there is anything you would say about?

Answer: Judith McKenna
So price investment just to say on that one which is remember this is over and above the underlying price investments that both of the businesses were planning to make as well. So that is the other thing you have got to factor in when you think about this. And I am going to save Roger from answering that question, which is, as you know we never give forward guidance as Walmart.

<u>Question 9</u>

Andrew Gwynn, Exane
Morning, it's Andrew Gwynn from Exane. Let's go for two questions. Most of mine have been covered, but just on the systems side of the equation. It is obviously probably the highest risk component, obviously seeing that slip up before specifically with Morrison's and Safeway. So why make the transition? If Walmart is staying a long-term partner why do you need to go down a risky route of integrating the supply chain?

And the second is why are the Head Offices staying fairly independent or is that something to explore at a later date?

Answer: Mike Coupe

I would argue that actually it is probably the best way, running a business from a systems point of view. They will need to be on a common platform and it is different to the Argos transaction in the way that Argos works is a fundamentally different supply chain and so sort of back engineering Argos systems into Sainsbury's systems is near impossible. In the end they are both supermarkets and both businesses do the same kind of stuff. There are clearly some systems which may be better in Sainsbury's and there will be some systems which are better in Asda. But in simple terms we will move Asda stores onto the Sainsbury's systems and it is, to describe it as simple I think is underestimating it. But it is a level no different to opening a new store if you try and think of it like that. And as I say, I am over simplifying it, but it has not got anything like the executional risks that you might have in your mind because they are basically the same types of businesses doing the same kind of things week in week out. Clearly there are training requirements, we will have to invest in some hardware and there will be a whole bunch of conversations about how you actually transition in a systematic and meaningful way. But I don't think there is anything like the risk that you have described. And part of the premise of the deal is that we have two strong brands with two strong customer propositions and this is about strengthening those brands and strengthening those propositions. And I think at least in part that is driven by having a sense of independence by having two Head Offices for the two businesses. So I am sure there are opportunities in the future which we have kind of alluded to as we have had this conversation. But certainly we would all want to keep the brands feeling like they had separate customer facing teams making sure they were doing the best thing for customers week in week out for those businesses.

Answer: Judith McKenna
Interestingly in the US business, the Sam's Club business is run as a completely separate business to the core US business so there are two Head Offices and they both operate independently with the exception of a few group jobs which have some oversight for both of them. So there is a way of working this.

And the other thing I would just say on integration is our experience around the world would be that you need to get on and integrate businesses because actually it minimises the risk of success in the long-term.

<u>Question 10</u>

Stewart McGuire, Credit Suisse
Morning Stewart McGuire from Credit Suisse, two questions from me. Before you purchased Home Retail I think you had 13 Argos stores operating within Sainsbury. Is there any reason why you wouldn't be able to rollout Argos stores within Asda over the next 18 months?

Answer: Mike Coupe
That is part of the synergy calculation.

Judith McKenna
Next 18 months?

Mike Coupe
Sorry. We have to be very careful during the CMA process, the businesses have to trade independently, have to be seen to be trading independently. And we would not do anything to prejudice the CMA process. And so let's start with the premise that once we have left this room we will never speak to each other again until we get to the end of the 18 month process. It won't be quite as blatant as that, but we can't talk about these things and won't talk about these things. And we know the answer to the question in terms of what we think it will look like, but for the sake of this conversation, let's not speculate about doing anything in

the next period of time whilst we see the transaction to completion because it will prejudice or has the potential to prejudice the CMA investigation.

Further question
Second question. On Walmart tech transfer, do you have any agreements in place so that anything that Walmart develops you are able to use on either basic flow through basis or on some sort of commercial terms like the parcel tower things?

Answer: Judith McKenna
Yes so there are some commercial terms that would sit around a bit. Effectively if you think about we are opening the door as Walmart and saying what is there within our organisation that you would like to pull from that would benefit the combined business? And that could be anything from tech towers that we create to smart carts being used as part of the Jet.com platform to something that is being developed in China in terms of picking capability. Equally the UK is one of the most advanced markets for grocery delivery and grocery picking in stores that there is, so there maybe some of the synergies that flow the other way as well. The details of what it is and how it is going to work exactly we will still be working through.

Answer: Mike Coupe
It is a bygone era, it was the year 2000 when Walmart took Asda over but I was part of the leadership team and the Walmart management said at the time we are going to open the doors to the sweetie shop and you come and choose. And that is exactly what the Asda team did at the time. So my experience of Walmart as an organisation is they are very willing and open to sharing learnings with partners if they think you are a partner and clearly we would be more than just a partner, Walmart would have an economic interest in sharing both ways. So you can take it as read that will be the approach taken I think by both sides.

Sorry this has to be the last question, I apologise, so make it a good one.

<u>Question 11</u>

Dusan Milosavljevic, Berenberg
No pressure then, it’s Dusan from Berenberg. I had two questions. The first one, are we right to assume that if Walmart’s stake was any higher in the combined entity Walmart would have to make an offer for the shares to all the shareholders, essentially a takeover offer?

And the second question is does 700 million Asda EBIT the right starting point in the new corporate structure or how should we treat essentially the royalties that Asda is paying to Walmart? Should it be higher than that?

Answer: Mike Coupe
I’ll have a go at answering the first question and then maybe Judith will have a reflection on that. I think she has already answered it from a Walmart point of view and I will let Roger or Judith give you the same answer that has already been given on what they may or may not choose to disclose.

I am not sure I understand fully the technicalities, I will have to talk to my advisers, but I think the structure means that we can give assurance to Sainsbury’s shareholders that Walmart don’t have voting control and there is enough weight in the other side with the other 70.1 per cent of shares to give some sense of independence and the fact that the company will operate as an independent UK plc. But of course 42 per cent gives Walmart a significant economic stake in the future of the organisation and therefore a significant amount of skin in the future game and I think that is effectively what you said in your answer as well?

Further answer: Judith McKenna
Yeah and don't forget we have voting rights to 29.9 per cent actually for exactly that reason that we don't believe there should be anybody within that Board structure that can have too much weight on the overall Board as well.

Further question
The other question was just on how to treat royalties, Asda Walmart?

Answer: Judith McKenna
Yeah I mean clearly without giving any forward guidance on anything or looking at that, which I have got to be really careful with, is there will be a change in the royalties and the structure that that works, but that could well be replaced by some commercial fees for accessing some of the goods and services that are provided.

Closing Remarks
Mike Coupe
Excellent last question. So I apologise, but as you imagine we have got quite a busy day. Roger and Judith are about to shoot off to Leeds to talk to Asda colleagues. So thank you very much and I am sure we will have further conversations about this proposed transaction. Could I just stress the fact that it is a proposed transaction as well. So thank you very much for coming today.

End