

TESCO

A close-up photograph of a man with dark skin and long dreadlocks, smiling broadly with his eyes closed. He is wearing a dark blue patterned shirt and has small hoop earrings. He is holding a white bowl filled with a colorful salad, including fried chicken pieces, avocado slices, arugula, and corn. The background is a solid purple color.

**Serving shoppers
a little better every day.**

Annual Report and Financial Statements 2017

Welcome to our annual report

Strategic report:	
Tesco at a glance	1
Introduction	2
Chairman's statement	3
Group Chief Executive's statement	4
The six strategic drivers	6
Our business model	11
Key performance indicators	12
Financial review	14
Environmental and social review	20
Principal risks and uncertainties	26
Corporate governance	32
Financial statements	79
Other information	166



Find out more online

We have produced a number of short videos that are available at www.tescopl.com/ar2017 and are featured within our report this year, as indicated by the video screen icon.



Tesco at a glance

As a leading retailer, with 460,000 colleagues, we serve millions of customers every week, in our stores and online.

£49.9bn ^{Δ (a)}

Group sales
(exc. VAT, exc. fuel)
(2015/16: £47.9bn)

£55.9bn ^(a)

Statutory revenue
(exc. VAT, inc. fuel)
(2015/16: £53.9bn)

£1,280m ^{Δ (a)}

Group operating profit
before exceptional items
(2015/16: £985m)

£1,017m ^(a)

Operating profit
(2015/16: £1.072m)

£145m ^(a)

Statutory profit before tax
(2015/16: £202m)

7.90p ^{Δ (a)}

Diluted earnings per share
before exceptional items
and net pension finance costs
(2015/16: 5.61p)

0.81p ^(a)

Statutory diluted EPS
(2015/16: 3.22p)

£(3.7)bn ^{Δ (b)}

Net debt
(2015/16: £5.1bn)

6,809 ^{(a),(c)}

Shops around the world
(2015/16: 6,733)

79m ^(a)

Shopping trips per week
(2015/16: 78m)

23m

Meals donated through our food
surplus redistribution work and
Neighbourhood Food Collection

460,000 ^(a)

Colleagues at year end
(2015/16: 471,000)

^(a) Reported on a continuing operations basis.
^(b) Excludes the net debt of Tesco Bank.
^(c) Includes franchise stores.

Δ Alternative Performance Measures

Measures with this symbol Δ are defined in the Alternative Performance Measures section of the Annual Report on pages 170 to 172.

Group income statement

	Notes	52 weeks ended 25 February 2017			52 weeks ended 27 February 2016		
		Before exceptional items £m	Exceptional items (Note 4) £m	Total £m	Before exceptional items £m	Exceptional items (Note 4) £m	Total £m
Continuing operations							
Revenue	2	55,917	-	55,917	53,933	-	53,933
Cost of sales		(52,899)	(116)	(53,015)	(51,124)	35	(51,089)
Gross profit/(loss)		3,018	(116)	2,902	2,809	35	2,844
Administrative expenses		(1,734)	(261)	(1,995)	(1,836)	22	(1,814)
Profits/(losses) arising on property-related items		(4)	114	110	12	30	42
Operating profit/(loss)		1,280	(263)	1,017	985	87	1,072
Share of post-tax profits/(losses) of joint ventures and associates	13	(30)	(77)	(107)	(21)	-	(21)
Finance income	5	109	-	109	29	-	29
Finance costs	5	(630)	(244)	(874)	(658)	(220)	(878)
Profit/(loss) before tax		729	(584)	145	335	(133)	202
Taxation	6	(185)	98	(87)	(8)	62	54
Profit/(loss) for the year from continuing operations		544	(486)	58	327	(71)	256
Discontinued operations							
Profit/(loss) for the year from discontinued operations	7	(37)	(75)	(112)	26	(153)	(127)
Profit/(loss) for the year		507	(561)	(54)	353	(224)	129
Attributable to:							
Owners of the parent		515	(555)	(40)	359	(221)	138
Non-controlling interests		(8)	(6)	(14)	(6)	(3)	(9)
		507	(561)	(54)	353	(224)	129
Earnings/(losses) per share from continuing and discontinued operations							
Basic	9	6.32p		(0.49)p	4.42p		1.70p
Diluted	9	6.31p		(0.49)p	4.40p		1.69p
Earnings/(losses) per share from continuing operations							
Basic	9	6.76p		0.81p	4.06p		3.24p
Diluted	9	6.75p		0.81p	4.05p		3.22p

The notes on pages 91 to 149 form part of these financial statements.

Group statement of comprehensive income/(loss)

	Notes	52 weeks 2017 £m	52 weeks 2016 £m
Items that will not be reclassified to income statement			
Remeasurements on defined benefit pension schemes	27	(3,567)	1,164
Tax on items that will not be reclassified	6	579	(300)
		(2,988)	864
Items that may subsequently be reclassified to income statement			
Change in fair value of available-for-sale financial assets and investments		80	5
Currency translation differences:			
Retranslation of net assets of overseas subsidiaries, joint ventures and associates		764	168
Movements in foreign exchange reserve and net investment hedging on subsidiary disposed, reclassified and reported in the Group income statement		-	(88)
Gains/(losses) on cash flow hedges:			
Net fair value gains/(losses)		385	318
Reclassified and reported in the Group income statement		(384)	(292)
Change in hedge relationship		-	186
Tax on items that may be reclassified	6	(23)	(30)
		822	267
Total other comprehensive income/(loss) for the year		(2,166)	1,131
Profit/(loss) for the year		(54)	129
Total comprehensive income/(loss) for the year		(2,220)	1,260
Attributable to:			
Owners of the parent		(2,206)	1,270
Non-controlling interests		(14)	(10)
Total comprehensive income/(loss) for the year		(2,220)	1,260
Total comprehensive income/(loss) attributable to owners of the parent arises from:			
Continuing operations		(2,096)	1,485
Discontinued operations		(110)	(215)
		(2,206)	1,270

The notes on pages 91 to 149 form part of these financial statements.

Group balance sheet

	Notes	25 February 2017 £m	27 February 2016 £m
Non-current assets			
Goodwill, software and other intangible assets	10	2,717	2,874
Property, plant and equipment	11	18,108	17,900
Investment property	12	64	78
Investments in joint ventures and associates	13	739	785
Other investments	14	823	1,078
Trade and other receivables	16	180	201
Loans and advances to customers	17	5,795	4,723
Derivative financial instruments	22	1,303	1,532
Deferred tax assets	6	707	49
		30,436	29,220
Current assets			
Other investments	14	284	57
Inventories	15	2,301	2,430
Trade and other receivables	16	1,475	1,406
Loans and advances to customers	17	4,166	3,819
Derivative financial instruments	22	286	176
Current tax assets		13	15
Short-term investments	18	2,727	3,463
Cash and cash equivalents	18	3,821	3,082
		15,073	14,448
Assets of the disposal group and non-current assets classified as held for sale	7	344	236
		15,417	14,684
Current liabilities			
Trade and other payables	19	(8,875)	(8,293)
Borrowings	21	(2,560)	(2,826)
Derivative financial instruments and other liabilities	22	(61)	(62)
Customer deposits and deposits from banks	24	(6,687)	(5,906)
Current tax liabilities	6	(613)	(419)
Provisions	25	(438)	(360)
		(19,234)	(17,866)
Liabilities of the disposal group classified as held for sale	7	(171)	-
Net current liabilities		(3,988)	(3,182)
Non-current liabilities			
Trade and other payables	19	(324)	(275)
Borrowings	21	(9,433)	(10,711)
Derivative financial instruments and other liabilities	22	(607)	(889)
Customer deposits and deposits from banks	24	(2,276)	(1,573)
Post-employment benefit obligations	27	(6,621)	(3,175)
Deferred tax liabilities	6	(88)	(135)
Provisions	25	(685)	(664)
		(20,034)	(17,422)
Net assets		6,414	8,616
Equity			
Share capital	28	409	407
Share premium		5,096	5,095
All other reserves		601	(141)
Retained earnings		332	3,265
Equity attributable to owners of the parent		6,438	8,626
Non-controlling interests		(24)	(10)
Total equity		6,414	8,616

The notes on pages 91 to 149 form part of these financial statements.

Dave Lewis
Alan Stewart

Directors

The financial statements on pages 86 to 149 were authorised for issue by the Directors on 11 April 2017 and are subject to the approval of the shareholders at the Annual General Meeting on 16 June 2017.

Group statement of changes in equity

	All other reserves								Total £m	Non- controlling interests £m	Total equity £m
	Share capital £m	Share premium £m	Other reserves £m	Capital redemption reserve £m	Hedging reserve £m	Translation reserve £m	Treasury shares £m	Retained earnings £m			
At 27 February 2016	407	5,095	40	16	211	(401)	(7)	3,265	8,626	(10)	8,616
Profit/(loss) for the year	-	-	-	-	-	-	-	(40)	(40)	(14)	(54)
Other comprehensive income/(loss)											
Change in fair value of available-for-sale financial assets and investments	-	-	-	-	-	-	-	80	80	-	80
Currency translation differences	-	-	-	-	-	764	-	-	764	-	764
Remeasurements of defined benefit pension schemes	-	-	-	-	-	-	-	(3,567)	(3,567)	-	(3,567)
Gains/(losses) on cash flow hedges	-	-	-	-	1	-	-	-	1	-	1
Tax relating to components of other comprehensive income	-	-	-	-	5	(13)	-	564	556	-	556
Total other comprehensive income/(loss)	-	-	-	-	6	751	-	(2,923)	(2,166)	-	(2,166)
Total comprehensive income/(loss)	-	-	-	-	6	751	-	(2,963)	(2,206)	(14)	(2,220)
Transactions with owners											
Purchase of treasury shares	-	-	-	-	-	-	(24)	-	(24)	-	(24)
Share-based payments	-	-	-	-	-	-	9	28	37	-	37
Issue of shares	2	1	-	-	-	-	-	-	3	-	3
Dividends	-	-	-	-	-	-	-	-	-	-	-
Tax on items charged to equity	-	-	-	-	-	-	-	2	2	-	2
Total transactions with owners	2	1	-	-	-	-	(15)	30	18	-	18
At 25 February 2017	409	5,096	40	16	217	350	(22)	332	6,438	(24)	6,414

	All other reserves								Total £m	Non- controlling interests £m	Total equity £m
	Share capital £m	Share premium £m	Other reserves £m	Capital redemption reserve £m	Hedging reserve £m	Translation reserve £m	Treasury shares £m	Retained earnings £m			
At 28 February 2015	406	5,094	40	16	35	(488)	(17)	1,985	7,071	-	7,071
Profit/(loss) for the year	-	-	-	-	-	-	-	138	138	(9)	129
Other comprehensive income/(loss)											
Change in fair value of available-for-sale financial assets and investments	-	-	-	-	-	-	-	5	5	-	5
Currency translation differences	-	-	-	-	-	81	-	-	81	(1)	80
Remeasurements of defined benefit pension schemes	-	-	-	-	-	-	-	1,164	1,164	-	1,164
Gains/(losses) on cash flow hedges	-	-	-	-	212	-	-	-	212	-	212
Tax relating to components of other comprehensive income	-	-	-	-	(36)	6	-	(300)	(330)	-	(330)
Total other comprehensive income/(loss)	-	-	-	-	176	87	-	869	1,132	(1)	1,131
Total comprehensive income/(loss)	-	-	-	-	176	87	-	1,007	1,270	(10)	1,260
Transactions with owners											
Purchase of treasury shares	-	-	-	-	-	-	(5)	-	(5)	-	(5)
Share-based payments	-	-	-	-	-	-	15	273	288	-	288
Issue of shares	1	1	-	-	-	-	-	-	2	-	2
Dividends	-	-	-	-	-	-	-	-	-	-	-
Total transactions with owners	1	1	-	-	-	-	10	273	285	-	285
At 27 February 2016	407	5,095	40	16	211	(401)	(7)	3,265	8,626	(10)	8,616

The notes on pages 91 to 149 form part of these financial statements.

Group cash flow statement

	Notes	52 weeks 2017 £m	52 weeks 2016 £m
Cash flows generated from/(used in) operating activities			
Operating profit/(loss) of continuing operations		1,017	1,072
Operating profit/(loss) of discontinued operations		(117)	102
Depreciation and amortisation		1,304	1,334
(Profit)/loss arising on sale of property, plant and equipment and intangible assets		(78)	164
(Profit)/loss arising on sale of subsidiaries and other investments		3	-
(Profit)/loss arising on sale of joint ventures and associates		(5)	(1)
Impairment loss on goodwill		46	18
Net impairment loss/(reversal) on other investments		(12)	(7)
Net impairment loss/(reversal) on loans/investments in joint ventures and associates		-	1
Net impairment loss/(reversal) on property, plant and equipment, software and other intangible assets and investment property		(5)	182
Adjustment for non-cash element of pensions charge	27	7	(395)
Additional contribution into pension schemes	27	(248)	(223)
Share-based payments		15	283
Tesco Bank fair value movements included in operating profit		98	72
Retail (increase)/decrease in inventories		124	251
Retail (increase)/decrease in development stock		16	99
Retail (increase)/decrease in trade and other receivables		(74)	20
Retail increase/(decrease) in trade and other payables		510	260
Retail increase/(decrease) in provisions		11	(280)
Tesco Bank (increase)/decrease in loans and advances to customers		(1,529)	(868)
Tesco Bank (increase)/decrease in trade and other receivables		(24)	(78)
Tesco Bank increase/(decrease) in customer and bank deposits, trade and other payables		1,474	463
Tesco Bank increase/(decrease) in provisions		25	(35)
(Increase)/decrease in working capital		533	(168)
Cash generated from/(used in) operations		2,558	2,434
Interest received/(paid)		(522)	(426)
Corporation tax received/(paid)		(47)	118
Net cash generated from/(used in) operating activities		1,989	2,126
Cash flows generated from/(used in) investing activities			
Purchase of property, plant and equipment, investment property and non-current assets classified as held for sale		(1,205)	(871)
Purchase of intangible assets		(169)	(167)
Disposal of subsidiaries, net of cash disposed	31	205	3,237
Acquisition of subsidiaries, net of cash acquired	31	(25)	(325)
Proceeds from sale of joint ventures and associates		-	192
Proceeds from sale of property, plant and equipment, investment property, intangible assets and non-current assets classified as held for sale		512	350
Net (increase)/decrease in loans to joint ventures and associates		15	(1)
Investments in joint ventures and associates		-	(77)
Net (investments in)/proceeds from sale of short-term investments		736	(2,894)
Net (investments in)/proceeds from sale of other investments		141	(103)
Dividends received from joint ventures and associates		28	41
Interest received/(paid)		41	3
Net cash generated from/(used in) investing activities		279	(615)
Cash flows generated from/(used in) financing activities			
Proceeds from issue of ordinary share capital	28	1	1
Increase in borrowings		185	586
Repayment of borrowings		(2,036)	(1,328)
Net cash flows from derivative financial instruments		475	154
Repayments of obligations under finance leases		(12)	(17)
Dividends paid to equity owners	8	-	-
Net cash generated from/(used in) financing activities		(1,387)	(604)
Net increase/(decrease) in cash and cash equivalents		881	907
Cash and cash equivalents at beginning of the year		3,082	2,174
Effect of foreign exchange rate changes		(131)	1
Cash and cash equivalents including cash held in disposal group at the end of the year		3,832	3,082
Cash held in disposal group	7	(11)	-
Cash and cash equivalents at the end of the year	18	3,821	3,082

The notes on pages 91 to 149 form part of these financial statements.

Notes to the Group financial statements continued

Note 13 Group entities continued

- since the Group's leases are priced at fair value, and any rights embedded in the leases are consistent with market practice, they do not provide the Group with additional control over the joint ventures or infer an obligation by the Group to fund the settlement of liabilities of the joint ventures;
- any options to purchase the other joint venturers' equity stakes are priced at market value, and only exercisable at future dates, hence they do not provide control to the Group at the current time;
- where the Group has a right to substitute properties in the joint ventures, the rights are strictly limited and are at fair value, hence do not provide control to the Group; and
- where the Group carries out property management activities for third party rentals in shopping centres, these additional activities are controlled through joint venture agreements or lease agreements, and do not provide the Group with additional powers over the joint venture.

Summarised financial information for joint ventures and associates

The summarised financial information below reflects the amounts presented in the financial statements of the relevant joint ventures and associates, and not the Group's share of those amounts. These amounts have been adjusted to conform to the Group's accounting policies where required. The summarised financial information for UK property joint ventures has been aggregated in order to provide useful information to users without excessive detail since these entities have similar characteristics and risk profiles largely based on their nature of activities and geographic market.

	UK property joint ventures		Gain Land Limited	
	2017 £m	2016 £m	12 months to Dec 2016 £m	12 months to Dec 2015 £m
Summarised balance sheet				
Non-current assets ^(a)	4,060	4,158	4,471	4,712
Current assets (excluding cash and cash equivalents)	99	58	2,261	2,047
Cash and cash equivalents	48	38	631	581
Current liabilities ^(b)	(301)	(327)	(6,208)	(5,550)
Non-current liabilities ^(b)	(4,831)	(4,572)	(169)	(153)
Net (liabilities)/assets	(925)	(645)	986	1,637
Summarised income statement				
Revenue	292	296	9,081	8,408
Profit/(loss) after tax	-	(36)	(626)	(341)
Reconciliation to carrying amounts:				
Opening balance	-	49	511	582
Additions/(disposals)	-	(10)	-	-
Foreign currency translation	-	-	47	(3)
Share of profits/(losses) ^(c)	14	22	(125)	(68)
Dividends received from joint ventures and associates	(14)	(29)	-	-
Deferred profits offset against carrying amounts ^(d)	-	(32)	-	-
Closing balance	-	-	433	511
Group's share in ownership	50%	50%	20%	20%
Group's share of net assets/(liabilities)	(463)	(323)	197	327
Goodwill	-	-	236	184
Deferred property profits offset against carrying amounts ^(d)	(63)	(64)	-	-
Cumulative unrecognised losses ^(e)	175	143	-	-
Cumulative unrecognised hedge reserves ^(f)	351	244	-	-
Carrying amount	-	-	433	511

^(a) The non-current asset balances of UK property joint ventures are reflected at historic depreciated cost to conform to the Group's accounting policies. The aggregate fair values in the financial statements of the joint ventures are £5,242m (2016: £5,415m).

^(b) The current and non-current liabilities of UK property joint ventures largely comprise loan balances of £4,121m (2016: £4,151m) and derivative swap balances of £703m (2016: £487m) entered into to hedge the cash flow variability exposures of the joint ventures. The 2016 derivative balance of £487m reflects a £159m reduction due to valuation adjustments for credit risk not included in the prior year.

^(c) The profit for the year for UK property joint ventures related to £14m dividends received from joint ventures with Enil carrying amounts. £21m of losses and £107m of decreases in the fair values of derivatives arising from these entities have been included in cumulative unrecognised losses and cumulative unrecognised hedge reserves respectively. The loss of £1125m for Gain Land Limited includes an impairment loss of £154m treated as an exceptional item. Refer to Note 4.

^(d) Deferred profits that arose from the transfer of properties into the UK property joint ventures have been offset against the carrying amounts of the related joint ventures. £1m relating to The Brookmaker Limited Partnership has been released during the year as a result of the disposal.

^(e) Cumulative unrecognised losses of £3m were disposed of relating to The Brookmaker Limited Partnership.

^(f) The 2016 cumulative unrecognised hedge reserves balances have been reduced by £79m to reflect valuation adjustments for credit risks.

At 25 February 2017, the Group has £103m (2016: £115m) loans to UK property joint ventures and Enil (2016: Enil) to Gain Land Limited.

Note 13 Group entities continued**Other joint ventures and associates**

The Group also has interests in a number of other joint ventures and associates, excluding UK property joint ventures and Gain Land Limited. These are not considered to be individually material to the Group.

	Joint ventures		Associates	
	2017 £m	2016 £m	2017 £m	2016 £m
Aggregate carrying amount of other joint ventures and associates	245	219	61	55
Group's share of profits/(losses) for the year	(7)	23	11	2

Impairment

Management has performed impairment tests and sensitivity analysis on its investments in Gain Land Limited, Trent Hypermarket Limited and Tesco Underwriting Limited. The carrying values of Trent Hypermarket Limited of £112m (2016: £96m) and Tesco Underwriting Limited of £71m (2016: £76m) are included within 'Other joint ventures and associates' as discussed above.

The recoverable values of these investments were estimated taking into account forecast cash flows, equity valuations of comparable entities and/or recent transactions for comparable businesses. No impairment was recognised in the period for these investments. Sensitivity tests for reasonably possible increases in the discount rates of one percentage point would not indicate impairment in any of the investments.

Future changes in estimated cash flows, discount rates, competitive landscape, retail market conditions and other factors may result in impairment losses or reversals of impairment in future periods.

Note 14 Other investments

	2017 £m	2016 £m
Loans receivable	13	30
Available-for-sale financial assets	1,094	1,105
Total other investments	1,107	1,135
Of which:		
Current	284	57
Non-current	823	1,078
	1,107	1,135

The Group holds an 8.8% investment stake in Lazada Group S.A. (2016: 21%), which is also included within available-for-sale financial assets. Refer to Note 31 for details of the disposal of part of this investment during the year.

Note 15 Inventories

	2017 £m	2016 £m
Goods held for resale	2,276	2,390
Development properties	25	40
	2,301	2,430

Goods held for resale are net of commercial income (refer to Note 20).

Note 16 Trade and other receivables

	2017 £m	2016 £m
Trade receivables	490	496
Prepayments	322	319
Accrued income	207	121
Other receivables	483	491
Amounts owed by joint ventures and associates (Note 29)	153	180
Total trade and other receivables	1,655	1,607
Of which:		
Current	1,475	1,406
Non-current	180	201
	1,655	1,607

Trade and other receivables include commercial income (refer to Note 20).

Trade and other receivables are generally non interest-bearing. Credit terms vary by country and the nature of the debt, ranging from 7 to 60 days.

Using the Annual Report for 2017 of TESCO Group, calculate the following ratios:

PROFITABILITY

the return on equity (ROI)

the return on capital employed (ROCE)

gross profit margin (GPM)

LIQUIDITY

The current ratio

The acid test ratio

FINANCING

Gearing ratio

Interest cover ratio

EFFICIENCY

Inventories turnover period

Trade receivables days period

Trade payables payment period

Non-current asset turnover

INVESTMENT

Dividend cover

Earnings per share

Price earnings ratio