29 April 2019

TESCO PLC: 2018/19 FINANCIAL STATEMENTS ON A POST-IFRS 16 BASIS

Tesco is introducing IFRS 16, the new financial reporting standard on accounting for leases, for its 2019/20 financial year. As previously indicated, we are adopting the standard fully retrospectively.

The first accounts prepared under IFRS 16 will be the 2019/20 interim results, published in October 2019, followed by the 2019/20 preliminary results, published in April 2020. In order to help investors and analysts update their models in advance of these results, on 15 February 2019 we issued the first half 2018/19 financial statements on a post-IFRS 16 basis and today we are also issuing the 2018/19 full-year financial statements under IFRS 16.

The headline impacts of IFRS 16 on the 2018/19 full-year financial statements can be summarised as follows:

- Group sales and total cash flow are completely unaffected.
- Group operating profit[1] increases by £401m to £2,607m as rent is removed and only part-replaced by depreciation.
- Group operating margin[2] increases by 63 basis points to 4.08%, including an increase of 64 basis points to 3.62% in the UK & ROI, an increase of 56 basis points to 3.51% in Central Europe, an increase of 68 basis points to 6.55% in Asia and an increase of 19 basis points to 18.14% in Tesco Bank.
- Profit before tax and Diluted EPS[3] both decrease, by £(152)m and (1.39)p respectively, due to the combination of depreciation and interest being higher than the rent they replace. This is due to the relative immaturity of the Group's lease portfolio, with leases being around one-third expired on average. The proportion of EPS dilution will reduce as the portfolio matures and, most notably, as underlying earnings increase.
- Whilst the impact of IFRS 16 would normally be expected to be broadly equal between the first and second half of any given year, the weighting can be affected by one-off items such as foreign exchange movements and gains on termination of leases. In the 2018/19 year, a number of one-off credits of this nature were recognised in the second half.
- Net assets reduce by £(1.3)bn to £13.5bn, as a 'new' lease liability of £(10.4)bn and 'new' right of use asset of £7.7bn are recognised and onerous lease provisions and other working capital balances are derecognised.
- Total indebtedness increases by £(3.3)bn to £(15.5)bn due to lease extensions and contingent commitments being included and lease-specific discount rates being applied.

Further detail on the impact of IFRS 16 on our 2018/19 financial statements can be found in Note 1 of this press release.

Additional information about the implementation of IFRS 16 and the impact of IFRS 16 on the first half 2018/19 financial statements were outlined in the Group's 'Introducing IFRS 16' analyst and investor briefing which was held on 15 February 2019. The relevant release, presentation and webcast of the briefing are available on www.tescoplc.com/investors/reports-results-and-presentations.

1. Excludes exceptional items and amortisation of acquired intangibles
2. Group operating profit before exceptional items and amortisation of acquired intangibles divided by Group Revenue
3. Excludes exceptional items, amortisation of acquired intangibles, net pension finance costs and fair value remeasurements on financial instruments

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Note 1

These condensed consolidated financial statements for the 52 weeks ended 23 February 2019 do not constitute statutory accounts as defined in section 434 of the Companies Act 2006. A copy of the statutory accounts for the 52 weeks ended 23 February 2019 will be filed with the Registrar of Companies following their approval at the AGM. The auditor's report on those accounts was not qualified, did not include a reference to any matters to which the auditor drew attention by way of emphasis without qualifying the report and did not contain statements under section 498(2) or (3) of the Companies Act 2006.

Income statement restatement for the 52 weeks ended 23 February 2019

	52 weeks ended 23 February 2019 (reported)			IFRS 16 impact			52 weeks ended 23 February 2019 (restated)		
	Before exceptional items and amortisation of acquired intangibles £m	Exceptional items and amortisation of acquired intangibles £m	Total £m	Before exceptional items and amortisation of acquired intangibles £m	Exceptional items and amortisation of acquired intangibles £m	Total £m	Before exceptional items and amortisation of acquired intangibles £m	Exceptional items and amortisation of acquired intangibles £m	Total £m
Continuing operations									
Revenue	**63,911**	**–**	**63,911**	**–**	**–**	**–**	**63,911**	**–**	**63,911**
Cost of sales	(59,695)	(72)	(59,767)	394	95	489	(59,301)	23	(59,278)
Gross profit/(loss)	**4,216**	**(72)**	**4,144**	**394**	**95**	**489**	**4,610**	**23**	**4,633**
Administrative expenses	(1,989)	(86)	(2,075)	7	–	7	(1,982)	(86)	(2,068)
Profits/(losses) arising on property-related items	(21)	105	84	–	–	–	(21)	105	84
Operating profit/(loss)	**2,206**	**(53)**	**2,153**	**401**	**95**	**496**	**2,607**	**42**	**2,649**
Share of post-tax profits/(losses) of joint ventures and associates	24	11	35	(3)	–	(3)	21	11	32
Finance income	22	–	22	3	–	3	25	–	25
Finance costs	(536)	–	(536)	(553)	–	(553)	(1,089)	–	(1,089)
Profit/(loss) before tax	**1,716**	**(42)**	**1,674**	**(152)**	**95**[1]	**(57)**[2]	**1,564**	**53**	**1,617**
Taxation	(413)	59	(354)	16	(9)	7	(397)	50	(347)
Profit/(loss) for the year	**1,303**	**17**	**1,320**	**(136)**	**86**	**(50)**	**1,167**	**103**	**1,270**
Earnings/(losses) per share from continuing and discontinued operations									
Basic			13.65p			(0.52)p			13.13p
Diluted			13.55p			(0.51)p			13.04p
Earnings/(losses) per share from continuing operations									
Basic			13.65p			(0.52)p			13.13p
Diluted			13.55p			(0.51)p			13.04p
KPIs and APMs									
Operating margin			3.5%			0.6%			4.1%
Diluted adjusted EPS			15.40p			(1.39)p			14.01p

1. £95m gain relates to a net impairment reversal following our annual impairment review and an onerous lease provision credit.
2. £(57)m PBT impact comprises: £1,060m rental charge removal, £(675)m additional depreciation, £(550)m additional net interest charge and £108m other net gains.

Balance sheet restatement

	As at 23 February 2019			As at 24 February 2018		
	Reported £m	IFRS 16 impact £m	Restated £m	Reported[1] £m	IFRS 16 impact £m	Restated £m
Non-current assets						
Goodwill and other intangible assets	6,264	-	6,264	2,661	-	2,661
Property, plant and equipment	19,023	163	19,186	18,521	191	18,712
Right of use assets[2]	-	7,713	7,713	-	7,527	7,527
Investment property	36	-	36	100	-	100
Investments in joint ventures and associates	704	(38)	666	689	(35)	654
Financial assets at fair value through other comprehensive income	979	-	979	860	-	860
Trade and other receivables	195	48	243	186	31	217
Loans and advances to customers and banks	7,868	-	7,868	6,885	-	6,885
Derivative financial instruments	1,178	-	1,178	1,117	-	1,117
Deferred tax assets	132	119	251	116	285	401
	36,379	**8,005**	**44,384**	**31,135**	**7,999**	**39,134**
Current assets						
Financial assets at fair value through other comprehensive income	67	-	67	68	-	68
Inventories	2,617	-	2,617	2,264	-	2,264
Trade and other receivables	1,640	(90)	1,550	1,504	(89)	1,415
Loans and advances to customers and banks	4,882	-	4,882	4,637	-	4,637
Derivative financial instruments	52	-	52	27	-	27
Current tax assets	6	-	6	12	-	12
Short-term investments	390	-	390	1,029	-	1,029
Cash and cash equivalents	2,916	-	2,916	4,059	-	4,059
	12,570	**(90)**	**12,480**	**13,600**	**(89)**	**13,511**
Non-current assets classified as held for sale	98	-	98	149	-	149
	12,668	**(90)**	**12,578**	**13,749**	**(89)**	**13,660**
Current liabilities						
Trade and other payables	(9,354)	223	(9,131)	(8,994)	221	(8,773)
Borrowings	(1,599)	36	(1,563)	(1,479)	12	(1,467)
Lease liability[3]	-	(646)	(646)	-	(712)	(712)
Derivative financial instruments	(250)	-	(250)	(69)	-	(69)
Customer deposits and deposits from banks	(8,832)	-	(8,832)	(7,812)	-	(7,812)
Current tax liabilities	(325)	-	(325)	(335)	-	(335)
Provisions	(320)	94	(226)	(544)	128	(416)
	(20,680)	**(293)**	**(20,973)**	**(19,233)**	**(351)**	**(19,584)**
Net current liabilities	**(8,012)**	**(383)**	**(8,395)**	**(5,484)**	**(440)**	**(5,924)**
Non-current liabilities						
Trade and other payables	(384)	19	(365)	(364)	-	(364)
Borrowings	(5,673)	93	(5,580)	(7,142)	110	(7,032)
Lease liability[3]	-	(9,859)	(9,859)	-	(9,560)	(9,560)
Derivative financial instruments	(389)	-	(389)	(594)	-	(594)
Customer deposits and deposits from banks	(3,296)	-	(3,296)	(2,972)	-	(2,972)
Post-employment benefit obligations	(2,808)	-	(2,808)	(3,282)	-	(3,282)
Deferred tax liabilities	(236)	187	(49)	(96)	14	(82)
Provisions	(747)	600	(147)	(721)	592	(129)
	(13,533)	**(8,960)**	**(22,493)**	**(15,171)**	**(8,844)**	**(24,015)**
Net assets	**14,834**	**(1,338)**	**13,496**	**10,480**	**(1,285)**	**9,195**
Equity						
Share capital	490	-	490	410	-	410
Share premium	5,165	-	5,165	5,107	-	5,107
All other reserves	3,798	(21)	3,777	735	(18)	717
Retained earnings	5,405	(1,317)	4,088	4,250	(1,267)	2,983
Equity attributable to the owners of the parent	**14,858**	**(1,338)**	**13,520**	**10,502**	**(1,285)**	**9,217**
Non-controlling interests	(24)	-	(24)	(22)	-	(22)
Total equity	**14,834**	**(1,338)**	**13,496**	**10,480**	**(1,285)**	**9,195**
APMs						
Net debt[4]	(2,863)	(10,341)	(13,204)	(2,625)	(10,114)	(12,739)
Total indebtedness[5]	(12,200)	(3,342)	(15,542)	(12,284)	(3,183)	(15,467)

1. After restating for the adoption of IFRS 15 'Revenue from Contracts with Customers'.
2. The right of use assets of £7,713m (2017/18: £7,527m) includes £104m (2017/18: £107m) assets held under finance leases, previously included in PP&E.
3. Total lease liabilities of £(10,505)m (2017/18: £(10,272)m) include £(129)m (2017/18: £(122)m) finance lease liabilities previously included in borrowings.
4. Net debt comprises bank and other borrowings, lease liabilities, net derivative financial instruments, joint venture loans and other receivables/ payables, offset by cash and cash equivalents and short-term investments. It excludes the net debt of Tesco Bank, which has lease liabilities of £35m (2018: £36m).
5. Total indebtedness pre-IFRS 16 comprises Net debt plus the IAS 19 deficit in the pension schemes (net of associated deferred tax) plus the present value of future minimum lease payments under non-cancellable operating leases. Post-IFRS 16, lease liabilities are included in Net debt, replacing the present value of future minimum lease payments under non-cancellable operating leases.

Summary Retail Cash Flow Restatement for the 52 weeks ended 23 February 2019

	52 weeks ended 23 February 2019 reported £m	IFRS 16 impact £m	52 weeks ended 23 February 2019 restated £m
Operating profit before exceptional items and amortisation of acquired intangibles	**2,206**	**401**	**2,607**
Less: Tesco Bank operating profit before exceptional items	(197)	(2)	(199)
Retail operating profit from continuing operations before exceptional items and amortisation of acquired intangibles	**2,009**	**399**	**2,408**
Add back: Depreciation and amortisation	1,214	673	1,887
Other reconciling items	94	(24)	70
Pension deficit contribution	(266)	–	(266)
Underlying (increase) / decrease in working capital	(312)	6	(306)
Retail cash generated from operations before exceptional items	**2,739**	**1,054**	**3,793**
Exceptional cash items:			
Relating to prior years:			
– Shareholder Compensation Scheme payments and SFO fine	(43)	–	(43)
– Utilisation of onerous lease provisions	(81)	81	–
– Restructuring payments	(60)	–	(60)
Relating to current year:			
– Restructuring payments	(68)	–	(68)
Other	15	–	15
Retail operating cash flow	**2,502**	**1,135**	**3,637**
Cash capex	(1,126)	–	(1,126)
Net interest	(283)	(547)	(830)
Tax	(302)	–	(302)
Property proceeds	285	–	285
Property purchases – store buybacks	(136)	–	(136)
Market purchases of shares (net of proceeds)	(146)	–	(146)
Acquisitions and disposals and dividends received	(635)	–	(635)
Add back: Booker acquisition costs (included in Acquisition & disposals above)[1]	747	–	747
Repayments of obligations under leases	(17)	(588)	(605)
Retail free cash flow	**889[2]**	**-**	**889**

1. The cost of major acquisitions and disposals are removed from the Group's definition of free cash flow.
2. Retail cash flow has been redefined to include repayments of obligations under leases due to IFRS 16. This results in a minor adjustment of £17m, restating reported retail cash flow of £906m to £889m. There is no overall impact to cash / cash equivalents at the end of the period.

Segmental reporting

The tables below set out the reported segmental income statement and the IFRS 16 impact, together with the expected comparative period segmental income statement for the 52 weeks ended 23 February 2019.

Segmental income statement

52 weeks ended 23 February 2019 **(reported)** At actual exchange rates	UK & ROI £m	Central Europe £m	Asia £m	Tesco Bank £m	Total at actual exchange £m
Continuing operations					
Revenue	51,643	6,298	4,873	1,097	63,911
Operating profit/ (loss) before exceptional items and amortisation of acquired intangibles	**1,537**	**186**	**286**	**197**	**2,206**
Exceptional items and amortisation of acquired intangibles	(2)	46	(67)	(30)	(53)
Operating profit/(loss)	**1,535**	**232**	**219**	**167**	**2,153**
Operating margin	**2.98%**	**2.95%**	**5.87%**	**17.95%**	**3.45%**

52 weeks ended 23 February 2019 **(IFRS 16 impact)** At actual exchange rates	UK & ROI £m	Central Europe £m	Asia £m	Tesco Bank £m	Total at actual exchange £m
Continuing operations					
Revenue	–	–	–	–	–
Operating profit/ (loss) before exceptional items and amortisation of acquired intangibles	**331**	**35**	**33**	**2**	**401**
Exceptional items and amortisation of acquired intangibles	83	12	–	–	95
Operating profit/(loss)	**414**	**47**	**33**	**2**	**496**
Operating margin	**0.64%**	**0.56%**	**0.68%**	**0.19%**	**0.63%**

52 weeks ended 23 February 2019 **(restated)** At actual exchange rates	UK & ROI £m	Central Europe £m	Asia £m	Tesco Bank £m	Total at actual exchange £m
Continuing operations					
Revenue	51,643	6,298	4,873	1,097	63,911
Operating profit/ (loss) before exceptional items and amortisation of acquired intangibles	**1,868**	**221**	**319**	**199**	**2,607**
Exceptional items and amortisation of acquired intangibles	81	58	(67)	(30)	42
Operating profit/(loss)	**1,949**	**279**	**252**	**169**	**2,649**
Operating margin	**3.62%**	**3.51%**	**6.55%**	**18.14%**	**4.08%**

The table below sets out the segmental balance sheet as at 23 February 2019, restated for the impact of IFRS 16.

Segmental balance sheet restatement

At 23 February 2019 (restated)	UK & ROI £m	Central Europe £m	Asia £m	Tesco Bank £m	Unallocated £m	Total £m
Goodwill and other intangible assets	4,927	27	284	1,026	-	6,264
Property, plant and equipment and investment property	14,017	2,694	2,449	62	-	19,222
Right of use assets	6,537	479	682	15	-	7,713
Investments in joint ventures and associates	12	1	567	86	-	666
Non-current financial assets at fair value through other comprehensive income	3	-	-	976	-	979
Non-current trade and other receivables[1]	100	5	14	19	-	138
Non-current loans and advances to customers and banks	-	-	-	7,868	-	7,868
Deferred tax assets	86	34	71	60	-	251
Non-current assets[2]	**25,682**	**3,240**	**4,067**	**10,112**	**-**	**43,101**
Inventories and current trade and other receivables[3,4]	2,999	482	372	285	-	4,138
Current loans and advances to customers and banks	-	-	-	4,882	-	4,882
Current financial assets at fair value through other comprehensive income	-	-	-	67	-	67
Total trade and other payables	(7,452)	(800)	(1,016)	(228)	-	(9,496)
Total customer deposits and deposits from banks	-	-	-	(12,128)	-	(12,128)
Total provisions	(245)	(27)	(49)	(52)	-	(373)
Deferred tax liabilities	(15)	(24)	(10)	-	-	(49)
Net current tax	(265)	(12)	(11)	(31)	-	(319)
Post-employment benefits	(2,788)	-	(20)	-	-	(2,808)
Assets classified as held for sale	68	30	-	-	-	98
Net debt (including Tesco Bank)[5]	(9,060)	(728)	(682)	(413)	(2,734)	(13,617)
Net assets	**8,924**	**2,161**	**2,651**	**2,494**	**(2,734)**	**13,496**

1. Excludes loans to joint ventures of £105m which form part of net debt.
2. Excludes derivative financial instrument non-current assets of £1,178m.
3. Excludes net interest and other receivables of £1m which form part of net debt.
4. Excludes loans to joint ventures of £28m which form part of net debt.
5. Includes lease liabilities in UK & ROI £9,060m, Central Europe £728m, Asia £682m, Tesco Bank £35m, Unallocated £nil and Total £10,505m.

The table below sets out the expected impact of IFRS 16 on the comparative period cash flow statement for the 52 weeks ended 23 February 2019 and related APMs. IFRS 16 has no impact on total cash flow for the year or cash and cash equivalents at the end of the year. Cash generated from operations and free cash flow measures increase as operating lease rental expenses are no longer recognised as operating cash outflows. Cash outflows are instead split between interest paid and repayments of obligations under leases, which both increase.

Cash flow statement restatement for the 52 weeks ended 23 February 2019

52 weeks ended 23 February 2019	Retail Retail (reported) £m	 IFRS 16 impact £m	 Retail (restated) £m	Tesco Bank Tesco Bank (reported) £m	 IFRS 16 impact £m	 Tesco Bank (restated) £m	Tesco Group Tesco Group (reported) £m	 IFRS 16 impact £m	 Tesco Group (restated) £m
Operating profit/(loss) of continuing operations	**1,986**	**494**	**2,480**	**167**	**2**	**169**	**2,153**	**496**	**2,649**
Depreciation and amortisation	1,292	673	1,965	83	2	85	1,375	675	2,050
ATM net income	(34)	–	(34)	34	–	34	–	–	–
(Profit)/loss arising on sale of property, plant and equipment and intangible assets and early termination of leases	(99)	(24)	(123)	(8)	–	(8)	(107)	(24)	(131)
(Profit)/loss arising on sale of subsidiaries and financial assets at fair value through other comprehensive income	(8)	–	(8)	–	–	–	(8)	–	(8)
Net impairment loss/(reversal) on property, plant and equipment, intangible assets and investment property	(58)	(56)	(114)	–	–	–	(58)	(56)	(114)
Adjustment for non-cash element of pensions charge	45	–	45	–	–	–	45	–	45
Additional contribution into defined benefit pension schemes	(266)	–	(266)	–	–	–	(266)	–	(266)
Share-based payments	82	–	82	(5)	–	(5)	77	–	77
Tesco Bank fair value movements included in operating profit/(loss)	–	–	–	127	–	127	127	–	127
Cash flows generated from operations excluding working capital	**2,940**	**1,087**	**4,027**	**398**	**4**	**402**	**3,338**	**1,091**	**4,429**
(Increase)/decrease in working capital	(438)	48	(390)	(258)	–	(258)	(696)	48	(648)
Cash generated from/(used in) operations	**2,502**	**1,135**	**3,637**	**140**	**4**	**144**	**2,642**	**1,139**	**3,781**
Interest paid	(301)	(550)	(851)	(5)	(3)	(8)	(306)	(553)	(859)
Corporation tax (paid)/received	(302)	–	(302)	(68)	–	(68)	(370)	–	(370)
Net cash generated from/(used in) operating activities	**1,899**	**585**	**2,484**	**67**	**1**	**68**	**1,966**	**586**	**2,552**
Proceeds from the sale of property, plant and equipment, investment property, intangible assets and non-current assets classified as held for sale	285	–	285	1	–	1	286	–	286
Purchase of property, plant and equipment, investment property and non-current assets classified as held for sale – store buy backs	(136)	–	(136)	–	–	–	(136)	–	(136)
Purchase of property, plant and equipment, investment property and non-current assets classified as held for sale – other capital expenditure	(962)	–	(962)	(3)	–	(3)	(965)	–	(965)
Purchase of intangible assets	(164)	–	(164)	(27)	–	(27)	(191)	–	(191)
Disposal of subsidiaries, net of cash disposed	8	–	8	–	–	–	8	–	8
Acquisition of subsidiaries, net of cash acquired	(715)	–	(715)	–	–	–	(715)	–	(715)
Net increase/(decrease) in loans to joint ventures and associates	–	–	–	5	–	5	5	–	5
Investments in joint ventures and associates	(11)	–	(11)	–	–	–	(11)	–	(11)
Net (investments in)/proceeds from sale of short-term investments	639	–	639	–	–	–	639	–	639
Net (investments in)/proceeds from sale of financial assets at fair value through other comprehensive income	2	–	2	(124)	–	(124)	(122)	–	(122)
Dividends received from joint ventures and associates	31	–	31	10	–	10	41	–	41
Dividends received from Tesco Bank	50	–	50	(50)	–	(50)	–	–	–
Interest received	18	3	21	–	–	–	18	3	21
Net cash generated from/(used in) investing activities	**(955)**	**3**	**(952)**	**(188)**	**–**	**(188)**	**(1,143)**	**3**	**(1,140)**

Cash flow statement restatement for the 52 weeks ended 23 February 2019 continued

	Retail			Tesco Bank			Tesco Group		
52 weeks ended 23 February 2019	Retail (reported) £m	IFRS 16 impact £m	Retail (restated) £m	Tesco Bank (reported) £m	IFRS 16 impact £m	Tesco Bank (restated) £m	Tesco Group (reported) £m	IFRS 16 impact £m	Tesco Group (restated) £m
Proceeds from issue of ordinary share capital	60	–	60	–	–	–	60	–	60
Own shares purchased	(206)	–	(206)	–	–	–	(206)	–	(206)
Repayment of obligations under leases	(17)	(588)	(605)	–	(1)	(1)	(17)	(589)	(606)
Add: Cash outflow from major acquisition	747	–	747	–	–	–	747	–	747
Less: Net increase/(decrease) in loans to joint ventures and associates	–	–	–	(5)	–	(5)	(5)	–	(5)
Less: Net investments in/(proceeds from sale of) short-term investments	(639)	–	(639)	–	–	–	(639)	–	(639)
APM: Free Cash Flow*	**889**	**–**	**889**	**(126)**	**–**	**(126)**	**763**	**–**	**763**
Increase in borrowings	704	–	704	271	–	271	975	–	975
Repayment of borrowings	(2,046)	–	(2,046)	(425)	–	(425)	(2,471)	–	(2,471)
Net cash flows from derivative financial instruments	35	–	35	–	–	–	35	–	35
Dividends paid to equity owners	(357)	–	(357)	–	–	–	(357)	–	(357)
Net cash generated from/(used in) financing activities	**(1,827)**	**(588)**	**(2,415)**	**(154)**	**(1)**	**(155)**	**(1,981)**	**(589)**	**(2,570)**
Intra-Group funding and intercompany transactions	**(14)**	**–**	**(14)**	**14**	**–**	**14**	–	**–**	**–**
Net increase/(decrease) in cash and cash equivalents	**(897)**	**–**	**(897)**	**(261)**	**–**	**(261)**	**(1,158)**	**–**	**(1,158)**
Cash and cash equivalents at the beginning of the year	2,755	–	2,755	1,304	–	1,304	4,059	–	4,059
Effect of foreign exchange rate changes	15	–	15	–	–	–	15	–	15
Cash and cash equivalents at the end of the year	**1,873**	**–**	**1,873**	**1,043**	**–**	**1,043**	**2,916**	**–**	**2,916**

* Free cash flow has been redefined to include repayments of obligations under leases due to IFRS 16. This results in a minor adjustment of £17m, restating reported retail free cash flow of £906m to £889m. There is no overall impact to cash / cash equivalents at the end of the period.

Disclaimer