MORRISONS

News Release

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PRELIMINARY RESULTS FOR THE YEAR ENDED 1 FEBRUARY 2009

Strong operating performance confirms broadening appeal of Morrisons

Financial summary

- Turnover up 12% to £14.5bn (2007/8: £13.0bn)
- Like for like sales (ex fuel) up 7.9% (2007/8: 4.6%)
- Profit before tax £655m (2007/8: £612m)
- Underlying profits up 13% to £636m (2007/8: £563m)
- Net debt £642m (2007/8: £543m) after capital investment of £678m
- Gearing of 14% (2007/8:12%) and interest cover of 42 times
- Basic earnings per share 17.4p (2007/8: 20.8p)
- Underlying earnings per share up 16% to 16.7p
- Total dividend for the year up 21% to 5.8p

Operating highlights

- 550,000 more customers per week reflecting broadening appeal
- Optimisation Plan on track
- Programme to freshen up the stores and brand completed
- Continued investment in infrastructure: new abattoir opened, vegetable pack-house extended and regional distribution centre under construction
- Nine new stores opened in 2008/09 and 90,000 sq ft of sales extensions
- Original target of 1.0m sq ft of new store space by January 2010 to be exceeded by 0.5m sq ft with acquisition of Co-op/Somerfield stores completing in the coming year

National to Nationwide

Our performance over the year confirms our broadening customer appeal, successfully delivered in a wide range of stores from 11,000 to 40,000+ square feet. We have identified significant potential to attract new customers and will focus on space growth in order to take us from a national to a nationwide company.

We confirm a new space target of 500,000 square feet in 2010/11.

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Outlook

The Board views both the short and the long term outlook for Morrisons positively. The business is well on track to achieve its goal of being the Food Specialist for Everyone, and the Executive team continues to see opportunities to invest in the business to generate further growth. We expect to open c350,000 square feet of new retail space in the coming year, on top of c500,000 square feet that we have agreed to acquire from the Cooperative Group, reflecting our confidence in the attractions of Morrisons core grocery business.

In the current economic environment we expect the competitive landscape to be extremely challenging. However, the Group's balance sheet is strong, and our financing arrangements are prudent. We will remain focused on delivering freshness and value to our customers.

Commenting on the results, Sir Ian Gibson, Non-executive Chairman, said:

"This was another year of good progress for Morrisons as we continued to grow sales, profits and dividends, whilst also investing to generate future growth."

Chief Executive, Marc Bolland, said:

"Our focus on fresh food and value appeals to shoppers everywhere and provides a strong platform to take Morrisons from national to nationwide."

-ENDS-

Operating and financial review 2009

Chairman's statement

In my first annual statement as Chairman, I am pleased that we are reporting another year of good progress for Morrisons. These are challenging times for the UK economy, but whilst we are not complacent we are confident that Morrisons offer meets and is in tune with the demands of our customers and the economic background.

Profit before tax was £655m compared with £612m last year. This included £2m of property gains, compared with £32m last year. Underlying basic earnings per share increased by 16% to 16.67p, whilst statutory basic eps decreased by 16% due to an abnormally low tax charge last year. The Board is recommending a final dividend of 5.0p per share, to bring the total for the year to 5.8p – an increase of 21%. At this level, the dividend is covered 2.9 times, and we will continue our progressive policy of increasing the dividend by underlying earnings and additionally moving dividend cover toward the average for our sector, which is around 2.5 times, by January 2010.

Cash generation was strong – with cash from operations of £964m, a year on year increase of £208m, or 28%. The Group's pace of investment picked up, with capital expenditure in the year increasing to £678m following the opening of 9 new stores and the acquisition of the freehold of our new distribution centre at Sittingbourne, in Kent. Additionally, we completed the planned second installment payment into our defined benefit pension schemes of £100m and bought back 58m shares in the market for £146m, an average share price of 251p. Following these investments, net debt increased from £543m to £642m. As previously reported, new five year term debt facilities of £1.1bn were agreed in September 2007, and only £250m of this facility was drawn at the year end, leaving gearing at 14%.

As previously announced, Roger Owen, the Group's Property Director, retired at the conclusion of the financial year after 34 years with the Group and 21 years service on the Board. Roger played a major role in building the store estate which forms the backbone of the business, and he goes with our thanks and best wishes for a long, happy and well deserved retirement.

We are pleased to welcome Philip Cox to the Board as a Non Executive Director, with effect from 1 April 2009. Phil is Chief Executive of International Power plc, and a previous CFO of Siebe plc. He will chair the Audit Committee after a suitable period of induction, taking over from Paul Manduca who will continue in his role as Senior Independent Director. The Board would like to record its thanks to Paul for his assured steering of the Audit Committee over the past three and a half years.

Morrisons success in the past year has been recognised with numerous industry awards, including Retailer of the Year from Retail Week, Grocer of the Year from The Grocer and Supermarket of the Year at the Retail Industry Awards. This is welcome recognition of the terrific efforts of all our 124,000 staff, and on behalf of the Board I want to express our thanks for their dedication, hard work and professionalism. I am pleased that our growth in the year will provide a profit share pool for them of £34m, a 13% increase on the previous year.

Our colleagues across the business are always enthusiastic supporters of our charitable activities. Our stores become involved in many initiatives in support of their local communities, such as Remembrance Day collections, and national events like Children in Need where we passed a cheque for £250,000 to the BBC again this year. Our own nominated charity of the year was Protecting Generations for Generations, a partnership between Help the Aged and Childline, and we were delighted to support them with funding of over £930,000 during the year.

Chief Executive's review

Strategy

Our three year strategy, as laid out in our 2007 annual report, is to position the business as the UK's "food specialist for everyone". This builds on our historic strengths of value and fresh food quality, now applied to a national, bigger business following the Safeway acquisition in 2004. As a food specialist, we are clearly differentiated from our larger competitors, all of whom are seeking to expand their non-food credentials. We also emphasise our deep understanding of food: through being closer to source than other retailers, through our unique manufacturing and packing facilities, through the amount of food preparation undertaken in our stores and through the employment of more specialist butchers, fishmongers and bakers than our competitors. We stress that our offer is for everyone, because our great food is also always great value.

Our strategy builds on our strengths, and is in tune with our customers' need for excellent value and their increasing focus on the health, provenance, quality and freshness of the food they buy. In order to deliver our strategy, we have previously outlined the building blocks that need to be put in place, and our plans to do this by 2010. These include freshening up our stores and improving and developing the infrastructure of the business in the key areas of manufacturing, distribution, and operating systems. The operating review of the year, below, highlights our progress towards these goals.

From our position as the fourth largest grocery retailer in the UK, we see significant opportunities to expand our store estate. As the food specialist for everyone, it is our conviction that we offer a real difference in grocery retailing that is highly attractive to a broad range of customers. However, there are many parts of the country where we remain under-represented. We estimate there to be over 8m households in the UK which are not located within a 15 minute drive of a current Morrisons store. This represents a higher target customer base than any of our three larger competitors. Our offer works well in a wide range of store sizes, from 11,000 to over 40,000 square feet, giving us flexibility in site selection. A key part of our strategy, therefore, has been to grow the number of Morrisons stores, and in 2007 we published a target of adding 1.0m square feet of new space by January 2010. Our acquisition of Co-operative/Somerfield stores, completing in the coming year, will see that target exceeded by 0.5m square feet, and we are confident that we will open a further 0.5m square feet of retail space in the year to January 2011.

We believe that delivery of our strategy of expansion and further optimisation of the operation of the business has resulted in strongly improved profit margins for our shareholders, whilst also positioning the Group for long term growth.

The Group is securely financed and has a strong balance sheet. We are confident that our planned investment requirements can be met from existing facilities. We will continue to pursue a prudent approach to financial management which is based on a number of principles:

- We wish to maintain a strong investment grade balance sheet.
- Operational control of our retail stores is fundamental to us.
- We are a prudent organisation and we structure our finances accordingly.
- Our defined benefit pension schemes assets and liabilities are effectively part of our balance sheet, and should be managed as such.

The Board concluded in March 2008 that surplus capital of £1bn should be returned to shareholders during 2008 and 2009, with £500m of that to be delivered in the first 12 months of the programme. Whilst £146m was returned in 2008 through share buybacks, the Board also identified new investment opportunities for the Group, over and above our original plans. These were the acquisition of stores from the Co-operative Group, the purchase of the freehold interest in our planned distribution centre at Sittingbourne and the acquisition of the freehold interest of 4 existing stores which, combined, account for unplanned investments of £460m. The Board believes these growth opportunities represent a more attractive deployment of capital than the planned share buyback. The Board also believes that further

investment opportunities may arise in the medium term and has therefore decided that the capital originally earmarked for share buy backs in the 2009/10 financial year should be retained within the business to give Morrisons maximum financial flexibility.

We have targeted progressive dividend growth in 2008 and 2009, over and above earnings growth, in order to bring dividend cover to a level in line with the average for our sector, which is around 2.5 times, by January 2010. Funding for this enhanced return to shareholders will come from operating cash flow and committed facilities available to the Group.

Operating review of the year

2008/9 was another good year for Morrisons – we made sure that we offered our customers great value everyday, in a rapidly deteriorating economy, whilst still investing for the long term future of the business.

We opened 9 new stores in the year, at Giffnock, Gorleston, Whitefield, Kidderminster, Granton, Northallerton, Blandford Forum, Clifton (Nottingham) and Holyhead. Two of these (Giffnock and Kidderminster) were replacements of existing stores and two (Blandford and Northallerton) were former Safeways, which had been closed since the acquisition due to their small size. Our decision to reopen them reflects our growing confidence in the operation of, and return from, smaller stores, and we have been pleased with their performance. A further two of the stores (Gorleston and Clifton) were previous Co-op/Somerfield stores that we acquired and converted to Morrisons. In both cases we saw very significant uplifts in sales compared to those achieved under their former ownerships, and as a result we were pleased, later in the year, to agree the acquisition of a further tranche of stores from the Co-op/Somerfield that we will open in 2009/10.

We continued our programme of store extensions, with 90,000 square feet added in the year, and ended the year with 382 stores and a total of 11.1m square feet of retail space, growth of 2.7% on the start of the year.

Turnover grew by £1.5bn to £14.5bn, a 12% increase. Part of this increase (c.3%) was due to the very high prices of fuel seen in our forecourts business in the year caused by the worldwide spike in oil prices, and this will unwind again in the coming year as pump prices have come back down. We were pleased with our stores sales growth, which was industry leading and broad based. Like for like sales, the measure of growth in existing stores, increased by 7.9% with customer numbers up 4.2% and average basket spend up 3.6%.

Based on TNS market research data, we believe our grocery market share grew from 12.1% to 12.3% in the year.

	Like for like stores	**Other**	**2008/09 Total**	**2007/08 Total**
Sales of goods (£m)	11,877	317	12,194	11,238
Fuel (£m)	3,523	74	3,597	2,871
Total sales inc VAT (£m)	15,400	391	15,791	14,109
Turnover exc VAT (£m)	14,171	357	14,528	12,969
Sales per square foot (£)	21.65	13.46	21.41	20.18
Customer numbers (m)	500	11	511	482
Customer spend (£)	23.92	21.14	23.86	23.10

Geographically, we grew in all regions, with the South particularly strong as the Morrisons brand continued to become better known. Across our store estate, we grew in all sizes of stores, with smaller stores below 25,000 square feet leading the way. Our market research shows that we won customers from all major competitors in the year. In store, our Market Street ranges did well, responding to our strong emphasis on fresh food preparation. Our own label ranges all showed growth, albeit the strong trends of the previous two years towards premium products slowed, with Eat Smart up 13%, the Best up 5% and Organics up 10%. By contrast, the Value range – relaunched in the year – saw 50% growth.

The growth of the Value range reflected the very difficult economic environment experienced by consumers throughout the year. Commodity price inflation, which began in 2007 but fed through strongly into products during 2008, meant that customers were paying more for their weekly shopping basket for the first time in some years. At the same time, disposable incomes were decreasing due to the impact of high energy prices, reduced availability of mortgage credit, a rising tax burden and increasing unemployment. We were quick to respond to the challenges being faced by our customers. Whilst we maintained our focus on the quality, healthiness and provenance of our food, we also delivered a year of innovative value offers to our customers. We launched over 21,000 price cuts throughout the year, and designed our promotions to help customers save money while eating well. Our £4 meal deals proved very popular, and we switched more of our promotions into "half price" rather than "buy one, get one free" in response to customers' need to spend less each week. We helped customers to treat themselves too, with great value deals such as 2 for 1 offers on party foods, the Mamma Mia DVD for £7 and a range of games for Nintendo Wii at £10. In the run-up to Christmas, we rewarded our most loyal customers with a £20 shopping voucher through the Collector Card scheme.

Our marketing expenditure increased in line with sales, although spread more evenly through the year. In addition to value messages, we continued to profile our unique food production capabilities, in our factories and in Market Street, and our understanding of food provenance. Our broad appeal and community involvement was well illustrated by our new schools initiative, "Let's Grow", which is designed to help schools teach children how to grow food. Over 18,000 schools registered for the scheme, well beyond our expectations, and in February 2009 we began to dispatch free planting and gardening equipment including over 30,000 tools, 29,000 pairs of gardening gloves, 13,000 bags of compost and over 10,000 growing kits.

Our forecourts business grew strongly in the year. As fuel prices moved above £1 per litre, consumers became highly price conscious and shopped around for value. We made sure that our pricing was always highly competitive, and indeed led the market back down below the key £1 price point when oil prices again began to fall. Average unleaded pump prices were 103.5p in the year, compared with 94.9p the previous year. Litreage grew by 11%, in a declining market.

Summary Income Statement	**2009 £m**	**2008 £m**	**Change %**
Turnover	14,528	12,969	12
Gross profit	913	818	12
Other operating income	37	30	23
Administrative expenses	(281)	(268)	5
Property transactions	2	32	-
Operating profit	671	612	10
Finance income and cost	(16)	-	-
Taxation	(195)	(58)	236
Profit/(loss) for the period	460	554	(17)

Gross profit grew in line with the level of turnover growth. The gross profit % of 6.3% was level with the previous year, although lower than it would have been due to the dilutive effect of high fuel sales, which have a very low margin. The impact of this, we estimate, was a 20bps reduction in margin. Offsetting this was the release of a provision first taken in 2005/6 relating to the rationalisation of our distribution infrastructure. The original provision was £75m, and after taking all final costs associated with this restructuring we were left with a balance to release of £8m, which is included in gross profit. Adjusting for these two effects, our gross profit increased by 0.1% despite the headwind effect of high energy costs in

our stores and supply chain. We successfully mitigated these costs through continued delivery of our Optimisation Plan.

The Group's two biggest costs, after cost of goods sold, are store wages costs and distribution costs. After a number of years of strong improvement in store labour productivity, the year under review saw us investing in customer service to support our sales growth. Despite this, labour costs as a proportion of sales improved by 0.5%. The cost to deliver each case through our distribution network continued to fall, despite higher fuel costs, with a further reduction of 2.5% year on year. We gained good benefits from new systems that improved the efficiency of our delivery schedules.

Our administrative expenses were up by 5%, below the rate of the turnover increase, reflecting tight control of our overheads. Marketing costs, which account for over one third of administrative expenses, increased in line with turnover, as we continued to seek, with success, to articulate the Morrisons story to a wider audience.

Optimisation Plan progress

Our aim is to become the "Food Specialist for Everyone", and that means:

"Food specialist"	We really understand food… …we know where it comes from …we pack it and make it in our factories …we make it in our stores … we employ craft skills in every store
"For everyone"	Great food which is also great value Great food which is for everyday, not just special days

Our Optimisation Plan, originally communicated in 2007, set out a number of programmes designed to deliver by our financial year ending January 2010, and we remain well on track. Key elements of the Plan included:

- Refreshed and rebranded stores
- Range extension and product innovation
- Investment in further manufacturing capacity
- An increase in distribution capacity in the South
- In store efficiency initiatives
- Replacement of our systems
- CSR initiatives

Progress in each of these areas is outlined below.

Customers visiting Morrisons today experience a modern and unique food specialist, following the successful completion of the programme to freshen-up our stores and brand. The programme covered the exterior and interior signage of the stores, our Market Street counters, our trucks and our filling stations. All work was completed, on time, at an average cost per store of £0.5m – a very cost effective new design scheme when compared to similar programmes elsewhere. Alongside the physical work, all staff were fitted with uniforms carrying the new brand and over 3,000 own-brand Morrison products received new packaging.

Our product ranges, too, have been extensively reinvigorated. Range development has been particularly strong in "Value" lines; but value and freshness are not incompatible, as seen in the launch of our innovative "Fresh Ideas" ready-to-cook fresh meals, which offer a great value alternative to dining out.

Our control of the fresh food supply chain, through our bakeries, fruit and vegetable packing facilities, meat and cheese processing plant and abattoirs gives us great flexibility to respond to changing customer needs and priorities. The value conscious behaviour that came to the fore in 2008 provided us with the opportunity to use this flexibility to great effect. We led the industry with great value deals on fresh foods, such as our £4 family meal deals which comprised 8 fresh food items for 50 pence each. Such deals, when advertised, create great demand, and it was only our close control of the supply chain that allowed us to cope with the volumes generated without disappointing customers looking for a bargain. Similarly, our abattoir and butchery operations are designed to use the whole animal, with minimal food waste. We have long sold lower priced cuts of meat such as brisket and neck fillet, which make delicious meals at bargain prices. These cuts are once again popular, and Morrisons is best placed to provide such variety and value. Equally, by being close to the source of supply, by being in the livestock markets every day and by only offering fresh fish on our counters, our fresh meat and fish quality cannot be matched even by much more expensive competitors.

Our advertising campaigns built on the previous year's success, with a continuation of the "Fresh Choice for You" message placing emphasis on freshness, in-store production, in-season food and our food provenance knowledge. We continued to use down-to-earth, approachable personalities including Helen

Baxendale and Richard Hammond – the campaign produced the highest consumer recall in 2008 (source: Marketing Magazine - Adwatch). Our research has confirmed that the campaign has significantly increased consumer awareness of Morrisons and what we stand for. To balance the "Fresh" message, we launched a high impact "Price Crunch" campaign in April, which ran through the rest of the year and was used to highlight our great value offers and everyday prices. This, too, struck a chord with our customers.

We continued to invest in our infrastructure as part of our Optimisation Plan. The new distribution centre at Sittingbourne, in Kent, is well underway. It will manage the growing volumes of our business in London and the South East and will open by the end of 2009. We took the opportunity to acquire the freehold of the site during the year, at a cost of £80m, in order to ensure maximum flexibility for the future. We were pleased to open our new abattoir at Spalding during the summer of 2008, and it is already producing at high volumes and very good levels of efficiency. This extra capacity has been key to ensuring that we can offer fresh pork, beef and lamb that is all UK sourced and all processed by us – something unique in British supermarket retailing.

We continue to invest in ways to improve customer service whilst also becoming more efficient in our stores. Following a successful trial, self scan checkouts are now rolling-out to over half our stores. Queue management software, which predicts very accurately the number of tills required to be open to serve the customers in store, is also at an advanced stage of roll out.

The Group's major programme of systems renewal continued to make good progress during the year, with detailed planning completed and Wipro, one of the world's premier computer services companies, selected as our implementation partner. As previously announced, the implementation programme began in late 2008 with the pilot phase of our new HR and payroll system, which will go fully live during 2009. The coming year will see the implementation of financial systems, depot systems and the start of the roll-out of the new point of sale systems into stores. In 2010 we will begin to replace systems in our manufacturing facilities, throughout the supply chain and the product masterfile.

Much of our investment, whilst improving the business, has also improved our carbon emissions. In the past two years we have invested £66m in new, efficient refrigeration capacity in our stores and £18m in new trucks and trailers. These measures have improved our chill chain, and also significantly reduced our emissions. A similar programme to replace all our petrol pumps with new, low emission technology, is well advanced, with 220 out of 287 filling stations having been re-pumped at the year end. As a result of these and other initiatives, our target to reduce our carbon footprint by 36% from 2006 levels has been achieved one year early. We are delighted to be the only grocery retailer to have been awarded the new Carbon Trust Standard for carbon reduction.

The overall investment requirements for the Optimisation Plan, outlined last year, are £450m over and above the normal run-rate of capital investment, and the programme will run to January 2010. In 2008, £182m of this was invested, bringing the cumulative total to £250m.

Alongside the Optimisation Plan, our new space programme laid out a target of opening an additional 1m square feet of retail space in the three years to January 2010. We are well on course to achieve that through our normal pipeline of new stores and store extensions, but over and above this target the acquisition, announced in November, of smaller Co-op and Somerfield stores, which will complete in 2009, will add around a further 500,000 square feet to our estate to bring the total at 31 January 2010 to approximately 12.0m square feet.

Financial review

The Group's results for 2008-09 have been strong once again, building on long term growth and strong cash flow generation.
Cash generated by our operations continue to:

- **Fund capital expenditure**
- **Reduce the pension deficit**
- **Reward our shareholders – total dividend for the year 5.8p per share and capital returns**

The Operating review of the year in the Chief Executive's review provides commentary on the performance of the Group over the past year. The volatility in the financial markets has impacted the economy as a whole and we are pleased that our results remained strong during this time. We have improved operating cash flows during the year and continue to have a strong balance sheet supported by long term financing.

Underlying earnings

Underlying earnings is a measure we use to assess normal underlying business performance and trends. The Group's earnings are adjusted to remove highly volatile or one-off costs. A reconciliation of underlying earnings is provided in note 1 of the financial information.

Underlying earnings before tax increased by £73m to £636m, driven primarily by the strong like for like sales performance. The Chief Executive's review contains further information on turnover, customer numbers and retail space.

Savings from Phase 2 of the Optimisation Plan have helped to mitigate input price inflation pressures and energy cost increases.

Earnings per share (EPS)
Underlying earnings per share is the EPS measure we use to remove the potential volatile impact of property gains and net pension interest income and consequently underlying EPS provides a better measure of the normal underlying business.
Basic underlying earnings per share has increased from 14.38p to 16.67p.

The share buy back (see below) contributed 0.14p (6%) to the increase but the primary reason is the year on year underlying profit growth.

Summary cash flow

	2009 £m	2008 £m
Cash generated from operations*	1,064	856
Interest and tax	(145)	(127)
Capital expenditure	(678)	(402)
Disposal and divestment proceeds	22	94
Pension deficit funding	(100)	(100)
Share buyback and issues	(143)	17
Dividend	(131)	(108)
Long term cash on deposit movement	74	(74)
Financing	246	(269)
Net cash inflow/(outflow)	209	(113)
Net debt	642	543

*before pension deficit funding

Cash generated from operations
Cash from operating activities has increased by £208m (24%) reflecting the strong profit generation of the Group from increased turnover and good profit conversion, combined with cost control throughout the business and improved working capital management.

Interest and tax
Interest received has fallen £21m from last year as the continuing fall in bank interest rates during the year adversely impacted our interest receivable on cash on deposit.

Interest paid has remained at £70m for the year. The revolving credit facility was utilised for the first time in October 2008, resulting in a small increase in floating-rate bank interest payable. Interest paid to bondholders is at fixed rates, and this cost reduced by £8m this year following the maturity of a £250m bond in August 2007.

Corporate tax payable in the year was £104m. This cash outflow represented 50% of the tax bill for the year to 3 February 2008, and 50% of the tax for the year to 1 February 2009, as well as repayments received for prior years.

The effective rate of tax for the year is 30% which is 2% above the prevailing corporate tax rate of 28%. The higher rate is mainly a result of non-qualifying depreciation and expenses where the Group is unable to obtain tax deductions.

The principal objective of the in-house tax department continues to be to pay the appropriate level of tax at the right time. We actively engage with the UK tax authorities and aim to be transparent in all of our activities. The Group is predominantly UK based, operates a simple business model, and does not engage in sophisticated tax planning structures.

Capital expenditure
Capital expenditure cash outflow was £678m, an increase from £402m last year, reflecting additional focus on growing the estate and supporting the Optimisation Plan as well as taking advantage of opportunities arising from the weakening of the commercial property market.

Normal planned capital expenditure
We opened 9 new stores and extended a further 18 stores, as well as a number of projects strengthening the retail estate and the supply chain.

Optimisation Plan investment

The rebranding programme was completed throughout the estate, at an average cost per store of £0.5m. A new abattoir was developed and opened in the year, and a vegetable packhouse extended in order to increase capacity. A group-wide programme to replace our IT systems entered the design phase and we began work on our new distribution centre in the South East of England. Total Optimisation Plan investment in the year was £182m.

Unplanned investments

During the year we took advantage of the weakness of the commercial property market by acquiring the freehold of four stores that were previously leaseholds, as well as the freehold of our planned new distribution centre at Sittingbourne in Kent. The total cost of these investments in the year was £120m. As a result, the proportion of freehold to leasehold properties in the estate grew to 95%, and we regard this as a key strength of the Group's balance sheet.

Pension

Pension deficit bridge

	£m
Net pension deficit at 3 February 2008	(68)
Actual vs expected return on scheme assets	(425)
Higher discount factor	328
Funding above annual service cost	103
Other	13
Net pension deficit at 1 February 2009	(49)

The continuing volatility in the financial markets does not change our view that, on completion of the actions arising from the Pension Review announced last year, these schemes are adequately funded for the long term. The markets will have to be continually monitored for emerging trends to ensure this continues to be the case. The move from a final salary basis to one of CARE (Career Average Revalued Earnings) is the final action planned from the review and is intended to make the schemes affordable for the future. If, following the consultation, the proposals are adopted, then it is anticipated that the valuation of the liability will decrease by c£90m.

Scheme valuations for accounts purposes were inevitably impacted by the turmoil in the financial markets, which had an effect on both the asset values and the liabilities of the schemes. The return on scheme assets was £425m worse than actuarially expected, due mainly to falls in the equity markets. This was offset by the reduced long term value of scheme liabilities resulting from a rise in the long term real discount rate.

The injection, as planned, of £100m of additional funding in the year combined with the move to CARE for future benefit accrual will leave the schemes well funded for the long term and in a small surplus position on current actuarial assumptions.

Net debt

Net debt at the year end increased slightly from £543m to £642m. Increases in capital expenditure, additional pension funding, and the share buy back have required significant cash funds. Much of this has been funded by cash generated from operations, demonstrating our solid underlying cash flow. Despite this high level of investment, we were pleased to have utilised only £250m of the revolving credit facilities at the year end.

Financing

The Group has a £1.1bn revolving credit facility which is not due to mature until September 2012. At the year end £250m had recently been drawn, allowing significant headroom for the Group's activities and investments.

The Group's bonds, originally issued by Safeway plc, were retained in the acquisition of the Safeway Group in 2004. The next bond repayment is due April 2010 for E250m. Moodys' rating of these bonds was upgraded to Baa1 in March 08.

Returns to shareholders

Returning surplus capital to our shareholders

In March 2008 we announced a two year share buy back programme to return £1bn of surplus capital to shareholders with a target of £500 million in the first year. By the end of 2008 we had repurchased and cancelled 57.8 million shares costing £146m. In view of the acquisition of the Co-op stores, the purchase of a number of freeholds and the possibility that further attractive investment opportunities may arise on the medium term, the Board has decided that the capital originally earmarked for share buy-backs in the 2009/10 financial year should be retained within the business to give Morrisons maximum financial flexibility.

Progressive dividend growth

The final dividend is proposed at 5p making the total dividend for the year 5.8p, an increase of 21% on last year.

We have targeted progressive dividend growth in 2008 and 2009, over and above earnings growth, in order to bring dividend cover to a level in line with the average for our sector, which is around 2.5 times. Funding for this enhanced return to shareholders will come from operating cash flow and committed facilities available to
the Group.

Share price and total shareholder value

The company's share price was 270.75p on 1 February 2009, a fall of 9% from the start of the year. This compares with a fall of 31% in the FTSE100 index and 14% in the Food and Drugs sector over the same period.

Over a three year period, the company's share price has risen by 44% compared with a fall of 28% in the FTSE100 index and a rise of 19% in the Food and Drugs sector over the same period.

Key judgements and assumptions

Judgements and assumptions made in the financial statements are continually reviewed. Whilst some outcomes have been affected by the volatility in the financial markets, all judgements and assumptions in the accounting policies remain consistent with previous years. Consideration of impairment to the carrying values of assets has been made and we concluded that the individual carrying values of stores and other operating assets are supportable either by value in use or market values.

Provisions

The property provision of £112m (note 21) includes £75m for onerous leases relating to sublet properties to cover the shortfall between expected rent received and the rent payable, taking into account the vacant tenancy periods during the terms of the lease. The provision assumptions were critically reviewed in the last quarter in the light of worsening market conditions. This resulted in a charge of £5m to cover the additional anticipated risk over the life of the leases.

Store Acquisitions

In December 2008, we agreed to purchase a number of stores from the Co-operative Group, subject to Office of Fair Trading (OFT) approval. The stores have an average retail square foot size of c14,000 and will fit very well within our existing portfolio of around 150 smaller stores.

The acquisition was agreed at a price of £223m, of which a refundable deposit of £22m had been paid by the year end. Should the purchase obtain full OFT approval, the remaining £201m will be paid by installments during 2009, and a store refurbishment programme costing a further £98m will commence in spring 2009.

Optimisation Plan
Our Optimisation Plan is to strongly improve operating margins, whilst shaping for growth.

The Optimisation Plan was announced in March 2006 as a three year plan to bring profitability back in line with sector standards after the integration of Safeway. The objectives were simple – to apply the Morrisons philosophy to the new bigger business while adapting it where necessary. The plan identified areas where savings could be made, or margins improved, as well as areas where investments were necessary to shape the business for growth.

Savings from Phase 1 were achieved in the prior year.

	Savings £m*				**Investment £m**	
		Phase 1 (06 -08)	Phase 2 (07-10)	**Total**		Phase 2 (07-10)
Gross margin	Better buying, sales mix and wastage control	110	100	**210**	-	-
In-store	Realising efficiencies	90	50	**140**	Store refresh programme	180
Manufacturing	Managing capacity	-	15	**15**	New abattoir	70
Distribution	Rationalisation	30	25	**55**	New capacity in the South	90
Centre/IT	Elimination of dual running costs	30	10	**40**	New systems across the business	110
	Total savings	**260**	**200**	**460**	**Total investment**	**450**
The investment of £450 million is in addition to normal planned capital expenditure, including new space, of £400 million annually. *Contributions to EBITDA.						

Consolidated income statement

52 weeks ended 1 February 2009

	Note	**2009 £m**	2008 £m
Turnover	2	**14,528**	12,969
Cost of sales		**(13,615)**	(12,151)
Gross profit		**913**	818
Other operating income		**37**	30
Administrative expenses		**(281)**	(268)
Profits arising on property transactions		**2**	32
Operating profit	4	**671**	612
Finance costs	5	**(60)**	(60)
Finance income	5	**44**	60
Profit before taxation		**655**	612
Taxation	6	**(195)**	(58)
Profit for the financial period attributable to equity holders of the parent		**460**	554
Earnings per share (pence)			
- basic	7	**17.39**	20.79
- diluted	7	**17.16**	20.67
Ordinary dividend per share (pence)			
Interim - paid		**0.800**	0.675
Final - proposed	29	**5.000**	-
- paid		**-**	4.125
Total dividend		**5.800**	4.800

Consolidated statement of recognised income and expense

52 weeks ended 1 February 2009

	Note	**2009 £m**	2008 £m
Actuarial loss arising in the pension scheme (net of taxation)	20	**(72)**	(26)
Cash flow hedging movement (net of taxation)		**8**	7
Foreign exchange movements		**6**	-
Deferred tax on share options	19	**-**	(2)
Net expense recognised directly in equity		**(58)**	(21)
Profit for the financial period		**460**	554
Total recognised income and expense for the financial period attributable to equity holders of the parent	23	**402**	533

Consolidated balance sheet

1 February 2009

	Note	**2009 £m**	2008 £m
Assets			
Non-current assets			
Property, plant and equipment	8	**6,587**	6,205
Lease prepayments	9	**250**	239
Investment property	10	**242**	239
Financial assets	12	**81**	43
		7,160	6,726
Current assets			
Stocks	13	**494**	442
Debtors	14	**245**	199
Financial assets	12	**-**	74
Cash and cash equivalents	15	**327**	191
		1,066	906
Non-current assets classified as held for sale		**-**	4
		1,066	910
Liabilities			
Current liabilities			
Creditors	16	**(1,915)**	(1,679)
Other financial liabilities	17	**(1)**	(77)
Current tax liabilities		**(108)**	(97)
		(2,024)	(1,853)
Non-current liabilities			
Other financial liabilities	17	**(1,049)**	(774)
Deferred tax liabilities	19	**(472)**	(424)
Net pension liabilities	20	**(49)**	(68)
Provisions	21	**(112)**	(139)
		(1,682)	(1,405)
Net assets		**4,520**	4,378
Shareholders' equity			
Called-up share capital	22	**263**	269
Share premium	22	**60**	57
Capital redemption reserve	23	**6**	-
Merger reserve	23	**2,578**	2,578
Retained earnings and hedging reserves	23	**1,613**	1,474
Total equity attributable to equity holders of the parent		**4,520**	4,378

Consolidated cash flow statement

52 weeks ended 1 February 2009

	Note	**2009** **£m**	2008 £m
Cash flows from operating activities			
Cash generated from operations	24	**964**	756
Interest paid		**(70)**	(70)
Taxation paid		**(104)**	(107)
Net cash inflow from operating activities		**790**	579
Cash flows from investing activities			
Interest received		**29**	50
Proceeds from sale of property, plant and equipment		**22**	94
Purchase of property, plant and equipment and investment property		**(678)**	(402)
Net cash outflow from investing activities		**(627)**	(258)
Cash flows from financing activities			
Proceeds from issue of ordinary shares		**3**	17
Shares repurchased for cancellation		**(146)**	-
Finance lease principal payments		**(2)**	(3)
New borrowings		**250**	-
Repayment of borrowings		**(2)**	(266)
Decrease/ (increase) in long term cash on deposit	12	**74**	(74)
Dividends paid to equity shareholders		**(131)**	(108)
Net cash inflow/ (outflow) from financing activities		**46**	(434)
Net increase/ (decrease) in cash and cash equivalents		**209**	(113)
Cash and cash equivalents at start of period		**118**	231
Cash and cash equivalents at end of period	15	**327**	118

Reconciliation of net cash flow to movement in net debt in the period

	Note	**2009** **£m**	2008 £m
Net increase/ (decrease) in cash and cash equivalents		**209**	(113)
Cash outflow from decrease in debt and lease financing		**4**	268
Cash inflow from increase in loans		**(250)**	-
Long term cash on deposit		**(74)**	74
Other non cash movements		**12**	-
Opening net debt		**(543)**	(772)
Closing net debt	25	**(642)**	(543)

General information
Wm Morrison Supermarkets PLC is a public limited company incorporated in the United Kingdom under the Companies Act 1985 (Registration number 358949). The Company is domiciled in the United Kingdom and its registered address is Hilmore House, Gain Lane, Bradford, BD3 7DL, United Kingdom.

Basis of preparation
The financial information set out herein does not constitute the Company's statutory accounts for the periods ended 1 February 2009 or 3 February 2008 but is derived from those accounts. Statutory accounts for 2008 have been delivered to the registrar of companies, and those for 2009 will be delivered in due course. The auditors have reported on those accounts; their report was (i) unqualified, (ii) did not include references to any matters to which the auditors drew attention by way of emphasis without qualifying their report, and (iii) did not contain statements under section 237(2) or (3) of the Companies Act 1985.

Significant accounting policies
The Directors consider the following to be significant accounting policies in the context of the Group's operations:

Revenue recognition
Revenue is recognised when significant risks and rewards of ownership have been transferred to the buyer, there is reasonable certainty of recovery of the consideration and the amount of revenue, associated costs and possible return of goods can be estimated reliably.

a) Sale of goods in-store and fuel
Sale of goods in-store is recorded net of value added tax, staff discounts, coupons, vouchers and the free element of multi-save transactions. Sale of fuel is recognised net of value added tax and Morrisons Miles award points. Revenue is recognised when transactions are completed in-store.

b) Manufacturing sales
Manufacturing sales are made direct to third party customers from the manufacturing companies and are recognised on despatch of goods. Sales are recorded net of value added tax and intra-group transactions.

c) Income from concessions and commissions
Income from concessions and commissions is based on the terms of the contract. Revenue collected on behalf of others is not recognised as turnover, other than the related commission.

Other operating income
Other operating income consists of income not directly related to the operating of supermarkets and mainly comprises rental income from investment properties. Other categories of income included within 'other operating income' are backhaul income and credits earned from the recycling of waste and packaging materials. Details of rental income from Investment Property are provided in note 10.

a) Rental income from investment property
Rental income arising from operating leases on investment properties is accounted for on a straight-line basis over the lease term.

Segmental reporting
Based on the nature of risks and returns impacting the Group's activities, the Directors consider that the primary reporting format is by business segment. The Directors consider that there is only one business segment being grocery and related retailing. The disclosures for the primary segment are therefore given by the primary financial statements and related notes.

The Group's business operations are conducted almost exclusively in the UK so a geographical segment report is not required.

Cost of sales
Cost of sales consists of all costs to the point of sale including manufacturing, warehouse and transportation costs. Store depreciation and a proportion of employee costs are also allocated to cost of sales.

Supplier income
Supplier incentives, rebates and discounts are collectively referred to as supplier income in the retail industry. Supplier income is recognised as a deduction from cost of sales on an accruals basis based on the expected entitlement which has been earned up to the balance sheet date for each relevant supplier contract. The accrued incentives, rebates and discounts receivable at year end are included within prepayments and accrued income. Where amounts received are in the expectation of future business, these are recognised in line with that future business.

Property transactions
Property includes the balance sheet headings of property, plant and equipment, investment property, lease prepayments and non-current assets classified as held for sale. The results of transactions relating to disposal of property are reported in the income statement under 'Profit arising on property transactions'. Depreciation and any impairment charges or reversals are recognised in cost of sales or administrative expenses, as appropriate.

Borrowing costs
All borrowing costs are recognised in the Group's income statement on an effective interest rate basis except for interest costs that are directly attributable to the construction of buildings which are capitalised and included within the initial cost of a building. Capitalisation of interest cost ceases when the property is ready for use.

Deferred and current tax
Current tax payable is based on the taxable profit for the period, using tax rates enacted or substantively enacted at the reporting date and any adjustments to tax payable in respect of previous periods. Taxable profit differs from the profit as reported in the income statement as it is adjusted both for items that will never be taxable or deductible and temporary differences. Current tax is charged in the income statement, except when it relates to items charged or credited directly in equity in which case the current tax is reflected in equity.

Deferred tax is recognised using the balance sheet method. Provision is made for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. No deferred tax is recognised for temporary differences that arise on the initial recognition of goodwill or the initial recognition of assets and liabilities that is not a business combination and that affects neither accounting nor taxable profits. Deferred tax is calculated based on tax law that is enacted or substantively enacted at the reporting date and provided at rates expected to apply when the temporary differences reverse. Deferred tax is charged or credited in the income statement except when it relates to items charged or credited directly to equity in which case the deferred tax is reflected in equity.

Deferred tax assets are recognised to the extent that it is probable that taxable profit will be available against which the asset can be utilised. Deferred tax assets recognised are reviewed at each reporting date as judgement is required to estimate the availability of future taxable income. Deferred tax assets and liabilities are not discounted and are offset where amounts will be settled on a net basis as there is a legally enforceable right to offset.

Accruals for tax contingencies require management to make judgements and estimates of ultimate exposures in relation to tax compliance issues. All accruals are included in current liabilities.

Business combinations and goodwill
All business combinations are accounted for by applying the purchase method.

The assets, liabilities and contingent liabilities of subsidiaries are measured at their fair values at the date of acquisition. Any excess of the cost of acquisition over the fair values of the identifiable net assets acquired is recognised as goodwill.

The goodwill in respect of the acquisition of Safeway was fully impaired in 2006.

Property, plant and equipment

a) Property, plant and equipment are stated at cost less accumulated depreciation and accumulated impairment losses. Costs include directly attributable costs. Annual reviews are made of estimated useful lives and material residual values.

b) Depreciation rates used to write off cost less residual value on a straight line basis are:

Freehold land	0%
Freehold and long leasehold buildings	2.5%
Short lease buildings	Over lease period
Plant, equipment, fixtures and vehicles	14-33%
Assets held under a finance lease	Shorter of life of lease or asset
Assets under construction	0%

Investment property

Property held to earn rental income rather than for the purpose of the Group's principal activities is classified as Investment property. Investment property is recorded at cost less accumulated depreciation and any recognised impairment loss. The depreciation policy is consistent with those described for other Group properties.

Income from investment properties is disclosed in "Other operating income" and details are shown in note 10 'Investment property'. The related operating costs are immaterial and are included within Administrative expenses.

Impairment of non-financial assets

Property, plant and equipment and investment property are annually reviewed for indications of impairment, or when events or changes in circumstances indicate that the carrying amount may not be recoverable. This is performed for each cash generating unit, which in the case of a supermarket is an individual retail outlet. If there are indications of possible impairment then a test is performed on the asset affected to assess its recoverable amount against carrying value. An asset impaired is written down to its recoverable amount which is the higher of value in use or its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

If there is indication of an increase in fair value of an asset that had been previously impaired, then this is recognised by reversing the impairment, but only to the extent that the recoverable amount does not exceed the carrying amount that would have been determined if no impairment loss had been recognised for the asset.

Stocks

Stocks are measured at the lower of cost and net realisable value. Cost is calculated on a weighted average basis and comprises purchase price, import duties and other non-recoverable taxes less rebates. Stocks are primarily goods for resale.

Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs necessary to make the sale.

Non-current assets classified as held for sale

Non-current assets are classified as held for sale if their carrying amount will be recovered through sale rather than continuing use. This condition is regarded as met only when the sale is highly probable and the asset (or disposal group) is available for immediate sale in its present condition. Management must be committed to the sale and it should be expected to be completed within one year from the date of classification.

On reclassification, non-current assets held for sale are recognised at the lower of carrying amount and the fair value less costs to sell. Impairment losses on initial classification as held for sale are included in the income statement, as are gains or losses on subsequent re-measurement. The depreciation of the asset ceases on reclassification. Assets are reclassified from non-current assets held for sale when the above criteria cease to be met.

Leases
Leases in which substantially all the risks and rewards of ownership are retained by the lessor are classified as operating leases; all other leases are classified as finance leases.

Lessor accounting
a) Operating leases
Assets acquired and held for use under operating leases are recorded as property, plant and equipment and are depreciated on a straight line basis to their estimated residual values over their estimated useful lives. Operating lease income is recognised on a straight line basis to the date of the next rent review.

b) Finance leases
The Group does not lease any assets on a finance lease basis.

Lessee accounting
a) Operating leases
Rental payments are taken to the income statement on a straight line basis over the life of the lease. Property leases are analysed into separate components for land and buildings and tested to establish whether the components are operating leases or finance leases. Premiums paid for land are treated as a prepayment of an operating lease rental and recognised on a straight line basis over the life of the lease.

b) Finance leases
The present value, calculated using the interest rate implicit in the lease, of the future minimum lease payments is included within fixed assets and financial liabilities as an obligation to pay future rentals. Depreciation is provided at the same rates as for owned assets, or over the lease period, if shorter.

Rental payments are apportioned between the finance charge and the outstanding obligation so as to produce a constant rate of finance charge on the remaining balance.

Provisions
Provisions are created where the Group has a present legal or constructive obligation as a result of a past event, where it is probable that it will result in an outflow of economic benefits to settle the obligation from the Group, and where it can be reliably measured. The nature of these provisions are:

a) Property provisions
Provisions made in respect of individual properties where there are obligations for onerous contracts, dilapidations and certain decommissioning obligations for petrol filling stations. The amounts provided are based on the Group's best estimate of the likely committed outflow to the Group. Where material, these estimated outflows are discounted to net present value.

b) Restructuring provisions
Provisions are established for announced and ongoing restructuring programmes planned and controlled by management where there is an obligation to make changes to the scope of the business undertaken by the Group or the manner in which business is conducted. The provision includes costs of severance to the affected employees, costs of property closure, and other direct expenditures not associated with ongoing activities.

Foreign currencies
Transactions in foreign currencies are recorded at the rates of exchange at the dates of the transactions. At each balance sheet date, monetary assets and liabilities that are denominated in foreign currency are retranslated at the rates of exchange at the balance sheet date. Gains and losses arising on retranslation are included in the income statement for the period.

Retirement benefits
The Group operates defined benefit and defined contribution schemes. A defined contribution scheme is a pension scheme under which the Group pays fixed contributions into a separate entity. A defined benefit scheme is one that is not a defined contribution scheme. Pension benefits under defined benefit schemes are defined on retirement based on age at date of retirement, years of service and a formula using either the employee's compensation package or career average earnings.

The Group operates two defined benefit retirement schemes which are funded by contributions from the Group and members. The defined benefit schemes are not open to new members. Pension scheme assets, which are held in separate trustee administered funds, are valued at market rates. Pension scheme obligations are measured on a discounted present value basis using assumptions as shown in note 20. The operating and financing costs of the scheme are recognised separately in the income statement in the period in which they arise. Death-in-service costs are recognised on a straight line basis over their vesting period. Actuarial gains and losses are recognised immediately in the statement of recognised income and expense.

The Group has a right to recognise an asset, should one arise, in respect of the Group's net obligations to the pension schemes. Therefore either an asset or a liability is recognised in the balance sheet, calculated separately for each scheme.

Payments by the Group to the defined contribution scheme are charged to the income statement as they arise.

Share-based payments
The Group issues equity settled share-based payments to certain employees in exchange for services rendered by them. The fair value of the share-based award is calculated at the date of grant and is expensed on a straight line basis over the vesting period with a corresponding increase in equity. This is based on the Group's estimate of share options that will eventually vest. This takes into account movement of non-market conditions, being service conditions and financial performance, if relevant. The fair value of equity-settled awards granted is not subsequently revisited.

Fair value is measured by use of a binomial stochastic model. The expected life used in the model has been adjusted, based on management's best estimate, for effects of non-transferability, exercise restrictions and behavioural considerations.

The Group has applied fair values to all grants of equity instruments after 7 November 2002 which were unvested as of 1 January 2005 at each balance sheet date.

Financial instruments
Financial assets and liabilities are recognised on the Group's balance sheet when the Group becomes a party to the contractual provisions of the instrument.

a) Financial assets
i) Trade and other debtors
Trade and other debtors are carried at the lower of their original invoiced value and recoverable amount. Provision is made when there is objective evidence that the Group will not be able to recover balances in full, with the charge being recognised in administrative expenses in the income statement. Balances are written off when the probability of recovery is assessed as being remote.

ii) Cash and cash equivalents
Cash and cash equivalents for cash flow purposes includes cash-in-hand, cash-at-bank and bank overdrafts together with short term, highly-liquid investments that are readily convertible into known

amounts of cash, with an insignificant risk of a change in value, within three months from the date of acquisition. In the balance sheet bank overdrafts are presented within current liabilities.

b) Financial liabilities
i) Trade and other creditors
Trade and other creditors are stated at cost.

ii) Borrowings
Interest-bearing bank loans and overdrafts are initially recorded at fair value, net of attributable transaction costs. Subsequent to initial recognition, any difference between the redemption value and the initial carrying amount is recognised in the income statement over the period of the borrowings on an effective interest rate basis.

c) Derivative financial instruments and hedge accounting
Derivative financial instruments are initially measured at fair value, which normally equates to cost, and are remeasured at fair value through profit or loss.
i) Cash flow hedges
Derivative financial instruments are classified as cash flow hedges when they hedge the Group's exposure to variability in cash flows that are either attributable to a particular risk associated with a recognised asset or liability, or a highly probable forecasted transaction.

The Group has a cross-currency swap which has been designated as a cash flow hedge. This derivative financial instrument is used to match or minimise risk from potential movements in foreign exchange rates inherent in the cash flows of certain financial liabilities. To minimise the risk from potential movements in commodity prices, the Group has fuel price contracts which are also designated as cash flow hedges.

Derivatives are reviewed quarterly for effectiveness. Where a derivative financial instrument is designated as a hedge of the variability in cash flows of a recognised asset or liability, or highly probable forecast transaction, the effective part of any gain or loss on the movement in fair value of the derivative financial instrument is recognised directly in equity through SoRIE.

The gain or loss on any ineffective part of the hedge is immediately recognised in the income statement within finance income/costs in relation to the cross-currency swap and within cost of sales in relation to the fuel price contracts. If a hedge of a forecast transaction subsequently results in the recognition of a financial asset or liability, the associated cumulative gains or losses that were recognised directly in equity are reclassified into the income statement when the transaction occurs.

Net debt
Net debt is cash and cash equivalents, long term cash on deposit, bank and other current loans, bonds and derivative financial instruments (stated at current fair value).

Share capital
Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds.
Where any Group company purchases the Company's equity share capital, the consideration paid, including directly attributable incremental costs, is deducted from retained earnings until the shares are cancelled. On cancellation, the nominal value of the shares is deducted from share capital and the amount is transferred to the capital redemption reserve.

Treasury shares
The Group has an employee trust for the granting of Group shares to executives and members of the employee share plans. Shares in the Group held by the employee share trust are treated as treasury shares and presented in the balance sheet as a deduction from retained earnings.

The finance and administration costs relating to the Executive Share Option Scheme are charged to the income statement. The shares are deducted for the purpose of calculating the Group's earnings per share.

Use of critical accounting assumptions and estimates
Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

The Group makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have significant risk of causing a material adjustment to the carrying value of assets and liabilities are discussed below.

a) Property provisions
Provisions have been made for onerous leases, dilapidations and decommissioning costs. These provisions are estimates based on the condition of each property and market conditions for the relevant location. The actual costs and timing of future cash flows are dependent on future events. Any difference between expectations and the actual future liability will be accounted for in the period when such determination is made.

b) Pension scheme assumptions and mortality table
The carrying value of defined benefit pension schemes is valued using actuarial valuations. These valuations are based on assumptions including the selection of the correct mortality tables for the profile of members in each scheme. All these are estimates of future events. The mortality experience study conducted as part of the Safeway scheme triennial valuation is statistically significant and the longevity assumption is adjusted to reflect its results. As both of the Group’s schemes have a similar composition and type of members, this adjustment is also made to the Morrisons scheme. The mortality assumptions, financial assumptions and mortality experience study are based on advice received from the schemes’ actuaries. Where appropriate these are corroborated from time-to-time with benchmark surveys and ad-hoc analysis.

c) Assumptions relating to tax
The Group recognises expected liabilities for tax based on an estimation of the likely taxes due, which requires significant judgement as to the ultimate tax determination of certain items. Where the actual liability arising from these issues differs from these estimates, such differences will have an impact on income tax and deferred tax provisions in the period when such determination is made.

d) Determination of useful lives, residual values and carrying values of property, plant and equipment, investment property and long leasehold land prepayments
Depreciation is provided so as to write down the assets to their residual values over their estimated useful lives as set out in the accounting policies for property, plant and equipment, investment property and long leasehold land prepayments. The selection of these residual values and estimated lives requires the exercise of judgement.

The Group is required to assess whether there is indication of impairment to the carrying values of assets. In making that assessment, judgements are made in estimating value in use. The Directors consider that the individual carrying values of stores and other operating assets are supportable either by value in use or market values.

Notes to the financial information

52 weeks ended 1 February 2009

1 Underlying earnings

The Directors consider that underlying earnings per share measures referred to in the Chairman's statement, Chief Executive's review and Financial review provide additional useful information for shareholders on underlying trends and performance. The adjustments are made to reported profit to (a) remove potential income statement volatility within net pension interest; (b) remove profits arising on property transactions since these profits do not form part of the Group's principal activities; and (c) normalise the tax charge as required.

In the current period, we have used the actual tax charge as the difference between the actual tax charge and a normalised charge is not significant. In the prior period an effective tax rate of 32% was applied, being an estimated normalised tax rate, since the prior period's effective tax rate was considerably lower than the prevailing rate due to reasons set out in note 6.

	2009 **£m**	2008 £m
Profit after tax	**460**	554
Add back: tax charge for the period[1]	**195**	58
Profit before tax	**655**	612
Adjustments for:		
Net pension interest income (note 5)[1]	**(17)**	(17)
Profits arising on property transactions[1]	**(2)**	(32)
Underlying earnings before tax	**636**	563
Taxation (2008: normalised tax rate of 32%)[1]	**(195)**	(180)
Underlying earnings after tax charge	**441**	383
Underlying earnings per share (pence)		
- basic (refer note 7(b))	**16.67**	14.38
- diluted (refer note 7(b))	**16.45**	14.29

[1] adjustments marked 1 equal £19m (2008: £171m) as shown in the reconciliation of earnings disclosed in note 7(b)

2 Turnover (excluding VAT)

	2009 **£m**	2008 £m
Sale of goods in-stores	**11,378**	10,439
Fuel	**3,069**	2,443
Total store based sales	**14,447**	12,882
Manufacturing sales	**33**	27
Income from concessions and commission	**48**	60
Total turnover	**14,528**	12,969

3 Employees and Directors

	2009 £m	2008 £m
Employee benefit expense for the Group during the period		
Wages and salaries	**1,453**	1,343
Social security costs	**105**	95
Share-based payments (note 26)	**14**	9
Pension costs	**42**	48
Other staff costs	**3**	10
	1,617	1,505

	2009 No.	2008 No.
Average monthly number of people employed by business group		
Stores	**111,462**	104,645
Manufacturing	**5,042**	4,416
Distribution	**4,886**	4,822
Centre [2]	**3,140**	3,571
	124,530	117,454

[2] Centre includes employees on maternity leave and long-term sick leave.

Key management represent Executive and Non-Executive Directors as they have the responsibility of planning and controlling the operations of the business as a whole. The aggregate remuneration paid to or accrued for the Directors for services in all capacities during the period is as follows:

	2009 £m	2008 £m
Directors		
Short term employee benefits	**5.8**	6.8
Pension costs	**0.4**	0.3
Share-based payments	**3.9**	1.5
	10.1	8.6

There are three Directors (2008: four) who have retirement benefits accruing under the Group's defined benefit pension scheme.

4 Operating profit

	2009 £m	2008 £m
The following items have been included in arriving at operating profit:		
Depreciation:		
- owned assets	**282**	280
- assets held under finance leases	**2**	2
Property, plant and equipment	**284**	282
Depreciation of investment property	**6**	7
Charge in the income statement	**290**	289
Foreign exchange differences	**2**	3
Operating lease rentals:		
- minimum lease payments	**35**	38
- sublease receipts	**(5)**	(5)
Value of stock expensed	**11,016**	9,739

Services provided by the Group's auditor

During the period KPMG Audit Plc, the Group's auditor, provided the following services:

	2009 £m	2008 £m
Audit services		
- statutory Group and Company audit	**0.4**	0.4
- statutory audit of subsidiaries	**0.2**	0.2
- audit related regulatory reporting	**0.1**	0.2
Tax services		
- compliance services	**0.1**	0.3
- advisory services	**0.2**	0.2
Other		
- independent project assurance	**0.5**	-
	1.5	1.3

5 Finance costs and income

	2009 £m	2008 £m
Interest payable on short term loans and bank overdrafts	**(3)**	(1)
Interest payable on bonds	**(45)**	(53)
Interest capitalised	**4**	8
Total interest payable	**(44)**	(46)
Fair value movement of derivative instruments	**(8)**	(7)
Other finance costs	**(8)**	(7)
Finance costs	**(60)**	(60)
Bank interest received	**17**	28
Amortisation of bonds	**8**	8
Other finance income	**2**	7
Pension liability interest cost	**(113)**	(99)
Expected return on pension assets	**130**	116
Net pension interest income	**17**	17
Finance income	**44**	60
Net finance cost	**(16)**	-

Interest is capitalised at the bank overdraft rate incurred before taxation which varies in line with the prevailing base rate. Taxation relief is obtained on interest paid and this reduces the tax charged for the period.

6 Taxation

a) Analysis of charge in the period	2009 £m	2008 £m
Corporation tax		
- current period	**145**	142
- adjustment in respect of prior period	**(10)**	(38)
	135	104
Deferred tax		
- current period	**69**	40
- adjustment in respect of prior period	**(9)**	(86)
	60	(46)
Tax charge for the period	**195**	58

b) Tax on items credited/(charged) directly to equity	2009 £m	2008 £m
Tax on hedging instruments		
- current tax	**19**	-
- deferred tax	**(17)**	-
	2	-
Deferred tax credit on actuarial movements	**29**	10
Tax on share-based payments – taken to SoRIE	**-**	(2)

The tax for both periods is different to the standard rate of corporation tax in the UK of 28% (2008: 30%). The differences are explained below:

Tax reconciliation	**2009 £m**	2008 £m
Profit before tax	**655**	612
Profit before tax at 28% (2008: 30%)	**183**	184
Effects of:		
Expenses not deductible for tax purposes	**8**	14
Non-qualifying depreciation	**31**	35
Effect of tax rate changes on deferred tax	**-**	(32)
Deferred tax on Safeway acquisition assets	**(7)**	(11)
Divestment profits not taxable	**(2)**	(11)
Other	**1**	3
Prior period adjustments	**(19)**	(124)
Tax charge for the period	**195**	58

The prior period effective tax rate was 9%. This low rate was as a result of prior period corporation tax and deferred tax provision releases due to closure of negotiations with HM Revenue and Customs on issues relating to the Safeway group prior to its acquisition by Morrisons.

7 Earnings per share

Basic earnings per share are calculated by dividing the earnings attributable to ordinary shareholders by the weighted average number of ordinary shares outstanding during the period.

For diluted earnings per share, the weighted average number of ordinary shares in issue is adjusted to assume conversion of all potentially dilutive ordinary shares. The Company has two (2008: two) classes of financial instruments that are potentially dilutive: those share options granted to employees where the exercise price is less than the average market price of the Company's ordinary shares during the period and contingently issuable shares under the Group's long term incentive plan.

a) Basic and diluted earnings per share (unadjusted)

Reconciliations of the earnings and weighted average number of shares used in the calculations are set out below:

	2009			2008		
	Earnings £m	**Weighted average number of shares millions**	**EPS pence**	Earnings £m	Weighted average number of shares millions	EPS pence
Unadjusted EPS						
Basic EPS						
Earnings attributable to ordinary shareholders	**460**	**2,644.9**	**17.39**	554	2,664.3	20.79
Effect of dilutive instruments						
Share options and LTIPs	**-**	**36.5**	**(0.23)**	-	15.7	(0.12)
Diluted EPS	**460**	**2,681.4**	**17.16**	554	2,680.0	20.67

b) Underlying earnings per share

Given below is the reconciliation of the earnings used in the calculations of underlying earnings per share:

	2009			2008		
	Earnings £m	**Weighted average number of shares millions**	**EPS pence**	Earnings £m	Weighted average number of shares millions	EPS pence
Underlying EPS						
Basic EPS						
Earnings attributable to ordinary shareholders	**460**	**2,644.9**	**17.39**	554	2,664.3	20.79
Adjustments to determine underlying profit (see note 1)	**(19)**	**-**	**(0.72)**	(171)	-	(6.41)
	441	**2,644.9**	**16.67**	383 [1]	2,664.3	14.38
Effect of dilutive instruments						
Share options and LTIPs	**-**	**36.5**	**(0.22)**	-	15.7	(0.09)
Diluted EPS	**441**	**2,681.4**	**16.45**	383	2,680.0	14.29

[1] The calculation of underlying earnings per share in 2008 included a normalised tax charge, see note 1.

c) Adjusted earnings per share

The following earnings per share calculations are for the purposes of the LTIP performance conditions:

	2009			2008		
	Earnings £m	**Weighted average number of shares millions**	**EPS pence**	Earnings £m	Weighted average number of shares millions	EPS pence
Adjusted EPS						
Basic EPS						
Earnings attributable to ordinary shareholders	**460**	**2,644.9**	**17.39**	554	2,664.3	20.79
Profits arising on property transactions [2]	**(1)**	**-**	**(0.04)**	(29)	-	(1.09)
	459	**2,644.9**	**17.35**	525	2,664.3	19.70

[2] Profits arising on property transactions as shown in the income statement after adjusting for tax charges.

8 Property, plant and equipment

	Land and buildings			Plant, equipment, fixtures & vehicles	Total
	Freehold	Long leasehold	Short leasehold		
	£m	£m	£m	£m	£m
Current year					
Cost					
At 3 February 2008	6,142	339	33	1,165	7,679
Additions at cost	380	8	10	286	684
Interest capitalised	4	-	-	-	4
Transfer from assets held for sale	9	-	-	-	9
Transfer to investment properties	(6)	-	-	-	(6)
Disposals	(10)	-	(15)	(2)	(27)
At 1 February 2009	**6,519**	**347**	**28**	**1,449**	**8,343**
Accumulated depreciation and impairment					
At 3 February 2008	566	48	21	839	1,474
Charge for the period	110	10	3	161	284
Transfer from assets held for sale	5	-	-	-	5
Disposals	-	-	(5)	(2)	(7)
At 1 February 2009	**681**	**58**	**19**	**998**	**1,756**
Net book amount at 1 February 2009	**5,838**	**289**	**9**	**451**	**6,587**
Assets under construction included above	**129**	**26**	**-**	**73**	**228**

Included in plant, equipment, fixtures and vehicles are assets held under finance leases at a cost of £22m (2008: £22m). The accumulated depreciation at the end of the financial period was £21m (2008: £19m).

	Land and buildings			Plant, equipment, fixtures & vehicles	
	Freehold	Long leasehold	Short leasehold		Total
	£m	£m	£m	£m	£m
Prior year					
Cost					
At 4 February 2007	6,211	417	18	919	7,565
Additions at cost	252	33	9	116	410
Interest capitalised	7	1	-	-	8
Reclassification	(205)	(69)	6	268	-
Transfer from/(to) investment properties	51	(25)	-	-	26
Transfer to long lease land premium	-	(10)	-	-	(10)
Disposals	(174)	(8)	-	(138)	(320)
At 3 February 2008	6,142	339	33	1,165	7,679
Accumulated depreciation and impairment					
At 4 February 2007	691	47	17	693	1,448
Charge for the period	98	15	4	165	282
Reclassification	(108)	(10)	-	118	-
Transfer from/(to) investment properties	18	(4)	-	-	14
Disposals	(133)	-	-	(137)	(270)
At 3 February 2008	566	48	21	839	1,474
Net book amount at 3 February 2008	5,576	291	12	326	6,205
Assets under construction included above	91	14	-	22	127

The classification of Property, Plant and Equipment (PPE) was reviewed in the prior year as part of upgrading our systems. As a result of this review, it was deemed appropriate to reclassify certain assets that have historically been regarded as intrinsic to the building structure to 'fixtures and fittings' included within plant, equipment, fixtures and vehicles.

9 Lease prepayments

	2009	2008
	£m	£m
Long lease land premiums	**250**	239

The current element of long lease land premiums is included within debtors (note 14). During the period, new long lease land premiums amounting to £13m were paid (2008: £1m).

10 Investment property

	2009	2008
	£m	£m
Cost		
At start of period	**285**	294
Additions	**3**	17
Transfer from/(to) property, plant and equipment	**6**	(26)
At end of period	**294**	285
Accumulated depreciation		
At start of period	**46**	53
Charge for the period	**6**	7
Transfer from/(to) property, plant and equipment	**-**	(14)
At end of period	**52**	46
Net book amount at end of period	**242**	239

Included in other operating income is £19m (2008: £20m) of rental income generated from investment properties.

The fair value of investment properties at the end of the period was £259m (2008: £328m). This valuation has been determined by the Directors based on market comparable information being rent and market rental yield. This reduction in the fair value is due to an increase in market rental yield driven by the deteriorating market conditions.

11 Capital commitments

	2009 **£m**	2008 £m
Contracts placed for future capital expenditure not provided in the financial statements	**321**	102

Included above are capital commitments for investment property of £1m (2008: £7m) and £46m for future capital expenditure on the new IT systems.

During the period, Morrisons entered into an agreement with the Co-operative Group to acquire over half a million square feet of additional selling space through the purchase of a number of Co-Operative Food and former Somerfield stores, at a cost of £223m. A deposit of £23m was paid during the year and has been classified within debtors.

The completion is dependent on obtaining certain approvals and the transaction and associated payments are expected to complete in the next financial year.

12 Financial assets

	2009	2008
	£m	£m
Non-current asset:		
Cross-currency interest swaps maturing 2010	**81**	43
Current asset:		
Long term cash on deposit	**-**	74

a) Cross-currency interest swaps maturing April 2010
The cross-currency interest swaps cover the Group from currency exposure arising from payments of interest and repayment of the principal in relation to Euro bonds.

The notional principal amount of the outstanding cross-currency interest swaps at 1 February 2009 was €250m (2008: €250m).

b) Long term cash on deposit
These were balances deposited with the bank with maturity of over three months from the date of the deposit.

13 Stocks

	2009 £m	2008 £m
Materials and work-in-progress	**13**	8
Finished goods	**481**	434
	494	442

14 Debtors

	2009 £m	2008 £m
Trade debtors	**105**	94
Less: Provision for impairment of trade debtors	**(3)**	(2)
	102	92
Lease prepayment – long lease land premiums	**1**	1
Other debtors	**78**	32
Prepayments and accrued income	**64**	74
	245	199

The Group has recognised a provision of £3m (2008: £2m) for impairment of its trade debtors as at 1 February 2009.

The ageing analysis of trade debtors is as follows:

	2009 £m	2008 £m
Neither past due nor impaired	**79**	70
Past due but not impaired:		
Not more than 3 months	**23**	17
Greater than 3 months	**-**	5
	102	92

As at 1 February 2009, trade debtors that were neither past due nor impaired related to a number of independent customers for whom there is no recent history of default.

The other classes of debtors do not contain impaired assets.

15 Cash and cash equivalents

	2009 £m	2008 £m
Cash and cash equivalents	**327**	191

Cash and cash equivalents include the following for the purpose of the cash flow statement:

	2009 £m	2008 £m
Cash and cash equivalents	**327**	191
Bank overdraft	**-**	(73)
	327	118

16 Creditors - current

	2009	2008
	£m	£m
Trade creditors	**1,443**	1,152
Other taxes and social security payable	**28**	35
Other creditors	**160**	189
Accruals and deferred income	**273**	292
Interest accrual	**11**	11
	1,915	1,679

17 Other financial liabilities

The Group had the following current and non-current borrowings and other financial liabilities:

	2009	2008
	£m	£m
Current		
Bank loans and overdrafts due within one year or on demand:		
Bank overdraft	**-**	73
Other loan notes – 4.19%	**-**	2
	-	75
Finance lease obligations	**1**	2
	1	77

	2009	2008
	£m	£m
Non-current		
£150m Sterling bonds 6.50% August 2014	**155**	156
£200m Sterling bonds 6.00% January 2017	**202**	203
£200m Sterling bonds 6.12% December 2018	**205**	205
€250m Euro bonds 6.50% April 2010	**222**	194
Total non-current Sterling and Euro bonds	**784**	758
Floating credit facility – 2.08%	**250**	-
Other loans – 9.38%	**15**	15
Finance lease obligations	**-**	1
	1,049	774

a) Borrowing facilities

Borrowings are denominated in Sterling and Euros and bear fixed interest rates, with the exception of the floating credit facility which bears floating interest rates. All borrowings are unsecured.

The expiry date for the floating credit facility is consistent with the undrawn element of the facility disclosed below.

In the event of default of covenants on the bank facility, the principal amounts and any interest accrued are repayable on demand.

The Group has the following undrawn floating committed borrowing facilities available in respect of which all conditions precedent had been met at that date:

	2009	2008
	£m	£m
Undrawn facilities expiring:		
Between 3 and 4 years	**850**	-
Between 4 and 5 years	**-**	1,100

b) Finance lease obligations

Payments under finance lease obligations fall due as follows:

	2009 £m	2008 £m
Not later than one year	**1**	2
Later than one year but not more than five years	**-**	1
	1	3
Future finance charges on finance lease obligations	**-**	-
Present value of finance lease obligations	**1**	3

18 Financial instruments

a) Financial risk management

The Group's treasury operations are controlled centrally by the Treasury Committee in accordance with clearly defined policies and procedures that have been authorised by the Board. There is an amount of delegated authority to the Treasury Committee, but all activities are summarised in half yearly treasury reports which are presented to the Audit Committee.

The Group's principal financial liabilities, other than derivatives, comprise bank loans and overdrafts, other borrowings, finance leases and trade and other creditors. The main purpose of these financial liabilities is to raise finance for the Group's operations. The Group has various financial assets such as trade debtors and cash and short term deposits which arise directly from its operations.

The Group enters into derivative transactions, in the form of forward currency contracts, cross-currency swaps and diesel and electricity price contracts. The purpose of these derivative instruments is to manage risks arising from the Group's operations and its sources of finance. The financial derivatives relating to commitments entered into during the year are to manage the risks arising from its usage of diesel and electricity. It remains the Group's policy not to engage in speculative trading of financial instruments.

The objectives, policies and processes for managing these risks, which remain unchanged from the prior year are stated below:

i) Foreign currency risk

The Group makes the majority of its purchases in Sterling however it incurs currency exposure in respect of overseas trade purchases made in currencies other than Sterling, primarily being Euro and US dollar. The Group objective is to reduce risk to short term profits from exchange rate fluctuations. It is Group policy that any transactional currency exposures recognised to have a material impact on short term profits will be hedged through the use of derivative financial instruments. As at the balance sheet date, the Group had entered into forward foreign exchange contracts to mitigate foreign currency exposure on up to 50% of its forecasted purchases within the next six months. Exposure on debt denominated in a foreign currency is fully hedged using cross-currency interest rate swaps.

The sensitivity to a reasonably possible change (+/- 20%) in the US dollar / Euro exchange rate has been determined as being immaterial.

ii) Liquidity risk

The Group policy is to maintain a balance of funding with a range of maturities and a sufficient level of undrawn committed borrowing facilities to meet any unforeseen obligations and opportunities. Short term cash balances, together with undrawn committed facilities, enable the Group to manage its liquidity risk. The Group finances its operations with a combination of bank credit facilities and bonds.

The Treasury Committee monitors rolling forecasts of the Group's liquidity reserve on a quarterly basis, which comprises committed and uncommitted borrowing facilities on the basis of expected cash flow. At the year end, the Group had undrawn committed facilities of £850m (note 17); these facilities remain available to the Group.

The table below summarises the maturity profile of the Group's primary non current financial liabilities based on contractual undiscounted payments, which includes interest payments. Balances due within 12 months equal their carrying balances as the impact of discounting is not significant.

As the amounts included in the table are the contractual undiscounted cash flows, these amounts do not agree to the amounts disclosed on the balance sheet for borrowings. Where borrowings are subject to a floating rate, an estimate for interest has been taken.

	2009 **£m**	2008 £m
One to two years	**438**	46
Two to three years	**35**	188
Three to four years	**35**	35
Four to five years	**35**	35
Five + years	**668**	703

The table below analyses the Group's derivative financial instruments, which will be settled on a gross basis, into relevant maturity groupings based on the remaining period at the balance sheet date to the contractual maturity date. The amounts disclosed in the table are the contractual undiscounted cash flows.

At 1 February 2009	**< 1 year**	**1 – 2 years**	**2 – 3 years**	**3 – 4 years**
Cross-currency swap – cash flow hedges				
Outflow	(11)	(156)	-	-
Inflow	14	235	-	-
Forward contracts				
Outflow	(53)	-	-	-
Inflow	56	-	-	-
Commodity price contracts				
Outflow	(2)	-	-	-
Inflow	-	-	-	-

At 3 February 2008	**< 1 year**	**1 – 2 years**	**2 – 3 years**	**3 – 4 years**
Cross-currency swap – cash flow hedges				
Outflow	(11)	(11)	(156)	-
Inflow	12	12	200	-
Forward contracts				
Outflow	(45)	-	-	-
Inflow	45	-	-	-

iii) Credit risk

Credit risk is managed on a Group basis. Credit risk arises from cash and cash equivalents, deposits with banking groups as well as credit exposures from tenants of investment properties.

The Group maintains deposits with banks and financial institutions with an acceptable credit rating for a period not exceeding six months. Further, the Group has specified limits that can be deposited with any banking group or financial institution at any point. The maximum exposure on cash and cash equivalents and deposits is equal to the carrying amount of these instruments. The Group does not expect any significant performance losses from counterparties.

The Group trades only with recognised, creditworthy third parties. It is the Group's policy that tenants of investment properties who wish to trade on credit terms are subject to credit verification procedures. In addition, receivable balances are monitored on an ongoing basis with the result that the Group's exposure to bad debts is not significant. The maximum exposure is the carrying amount as disclosed in note 14. There are no significant concentrations of credit risk within the Group.

iv) Other risk

Pricing risk: The Group manages the risks associated with the purchase of electricity, gas and diesel consumed by its activities. This does not include fuel purchased for resale to customers. The Treasury Committee reviews the Group's market price exposure to these commodities on a quarterly basis and determines a strategy for utilising derivative financial products in order to mitigate the volatility of the commodity prices.

The Group intends to hold derivatives to maintain cover of its energy purchases of up to 75% over an appropriate timescale.

Cash flow interest rate risk: The Group's long term policy is to protect itself against adverse movements in interest rates by maintaining up to 60% of its consolidated total net debt in fixed rate borrowings over a four year horizon. As at the balance sheet date 74% of the Group's borrowings are at fixed rate, thereby substantially reducing the Group's exposure to adverse movements in interest rate.

Cash and cash equivalents is a significant interest-bearing asset held by the Group. At year end, a 1% movement in interest rate would have had a £2m (2008: £5m) impact on the Group's annual finance income. There are no other significant interest-bearing assets held by the Group.

b) Capital management

The Group's objectives are to safeguard its ability to continue as a going concern providing returns to shareholders, through the optimisation of the debt and equity balance, and to maintain a strong credit rating and headroom. The Group manages its capital structure and makes appropriate decisions in light of the current economic conditions and strategic objectives of the Group. The Group has completed a share buy-back programme in the period, see note 23.

A key objective of the Group's capital management is to maintain compliance with the covenants set out in the revolving credit facility.

The Group's policy is to maintain both a gearing ratio and interest cover, which represents headroom of at least 10% over and above the requirements laid down in the revolving credit facility. Throughout the year, the Group has comfortably complied with this policy.

There has been no change in the objectives, policies or processes with regards to capital management during the years ended 1 February 2009 and 3 February 2008.

c) Fair values

i) Financial assets

All financial derivatives are held at fair value which has been determined by reference to prices available from the markets on which the instruments are traded.

Cash and cash equivalents and Debtors are held at book value which equals the fair value. The values of the financial assets are disclosed within note 12.

ii) Financial liabilities

All financial liabilities are carried at amortised cost. The Euro bonds are retranslated at balance sheet date spot rates. The fair value of the Sterling and Euro Bonds are measured using closing market prices. These compare to carrying values as follows:

	2009	**2009**	2008	2008
	Amortised cost £m	**Fair value £m**	Amortised cost £m	Fair value £m
Total Sterling and Euro bonds – non-current	**784**	**781**	758	693

The fair value of other items within current and non-current borrowing equals their carrying amount, as the impact of discounting is not significant.

d) Hedging activities

i) Cash flow hedge

At 1 February 2009, the company held a cross-currency swap which has been designated as a cash flow hedge. This derivative financial instrument is used to minimise risk from potential movements in foreign exchange rates inherent in cash flow of certain liabilities. To minimise the risk from potential movements in commodity prices, the Group has fuel price contracts which are also designated as cash flow hedges.

The hedged forecast transactions denominated in foreign currency are expected to occur at various dates over the next two years. Gains and losses recognised in the hedging reserve in equity (note 23) on cross-currency swaps as at 1 February 2009 are recognised in the income statement in the period or periods during which the hedged forecast transaction affects the income statement, which is generally once every year over the course of the next two (2008: three) years.

ii) Forward contracts
The Group uses forward foreign exchange contracts to hedge the cost of future purchases of goods for resale, where those purchases are denominated in a currency other than the functional currency of the purchasing company. The hedging instruments are primarily used to hedge purchases in Euro and US dollar. The cash flows hedged will occur within one year of the balance sheet date.

At 1 February 2009, the total notional amount of outstanding forward foreign exchange contracts to which the Group has committed was £53m (2008: £45m). The fair value of these outstanding forward exchange contracts at the balance sheet date was £3.4m (2008: £0.2m).

19 Deferred tax

	2009 £m	2008 £m
Deferred tax liability	**(546)**	(554)
Deferred tax asset	**74**	130
Net deferred tax liability	**(472)**	(424)

IAS 12 Income Taxes permits the offsetting of balances within the same tax jurisdiction. All of the deferred tax assets were available for offset against deferred tax liabilities.

The movements in deferred tax assets/(liabilities) during the period are shown below.

	Property, plant and equipment £m	**Pensions £m**	**Share based payments £m**	**Other short term temporary differences £m**	**Total £m**
Current year					
At 3 February 2008	(554)	19	5	106	(424)
Credited/(charged) to income statement	8	(34)	1	(35)	(60)
Credited/(charged) directly to equity	-	29	-	(17)	12
At 1 February 2009	**(546)**	**14**	**6**	**54**	**(472)**
Prior year					
At 4 February 2007	(629)	59	6	86	(478)
Credited/(charged) to income statement	75	(50)	1	20	46
Credited/(charged) directly to equity	-	10	(2)	-	8
At 3 February 2008	**(554)**	**19**	**5**	**106**	**(424)**

In 2008, other short term temporary differences included £31m of unused tax losses.

The deferred income tax credited/(charged) through the SoRIE during the period was as follows:

	2009 £m	2008 £m
Actuarial gains/(losses)	**29**	10
Share options	**-**	(2)
Short-term temporary differences	**(17)**	-

20 Pensions

a) Defined benefit pension scheme

The Group operates two pension schemes, the "Morrison" and "Safeway" schemes, providing benefits based on pensionable pay of the final years of membership. The assets of the schemes are held in separate trustee administered funds; no part of the schemes is wholly unfunded. The latest full actuarial valuations, which were carried out at 6 April 2007 and 1 April 2007 for the Morrison and Safeway schemes respectively, were updated for IAS 19 purposes for the periods to 1 February 2009, 3 February 2008, 4 February 2007 and 29 January 2006 by a qualified independent actuary.

The Deed and Rules of the Morrison Pension Scheme gives the Trustees power to set the level of contributions. In the Safeway Scheme this power is given to the Group, subject to regulatory override.

The current best estimate of employer contributions to be paid for the year commencing 2 February 2009 is £44 million (2008: £138 million, including a special contribution of £100 million).

b) Assumptions

The major assumptions used in this valuation to determine the present value of the schemes' defined benefit obligation were as follows:

i) Financial

	2009	2008	2007
Rate of increases in salaries	**4.75-5.75%**	5.00 – 6.00%	4.45 – 5.45%
Rate of increase in pensions in payment and deferred pensions	**3.50%**	3.75%	3.20%
Discount rate applied to scheme liabilities	**6.25%**	5.75%	5.00%
Inflation assumption	**3.50%**	3.75%	3.20%

ii) Longevity

The average life expectancy in years of a member who reaches normal retirement age of 65 and is currently aged 45 is as follows:

	2009	2008	2007
Male	**23.5**	23.5	19.9
Female	**25.8**	25.8	22.8

The average life expectancy in years of a member retiring at the age of 65 at balance sheet date is as follows:

	2009	2008	2007
Male	**22.2**	22.2	19.9
Female	**24.7**	24.7	22.8

Assumptions regarding future mortality experience are set based on actuarial advice and in accordance with published statistics. The longevity assumption considers how long a member will live when they reach the age of retirement. Amongst the UK population there is a continuing trend for a generation to live longer than the preceding generation, and this has been reflected in the longevity assumption. This means that a 45 year old today is assumed to live on average longer than a 65 year old today. This particular adjustment, described in the mortality tables below, is known as "Long Cohort" and is in-line with the latest advice from the Pension Regulator.

In calculating the present value of the liabilities the actuary selects the appropriate mortality table that reflects the longevity assumption. The most up to date tables are used in each period. The current mortality table used is PNX00 YOB LC (2008: PNX00 YOB LC and 2007:PA92 C2020). As disclosed in the Critical accounting assumptions, the results of the experience study conducted for the Safeway scheme have been used to adjust the longevity assumption for both schemes.

iii) Expected return on assets

The major assumptions used to determine the expected future return on the schemes' assets, were as follows:

	2009	2008	2007
Long term rate of return on:			
Equities	**7.00%**	7.00%	7.00%
Corporate bonds	**6.00%**	6.00%	5.00%
Gilts	**4.25 – 4.50%**	4.25 – 4.50%	-
Property related funds	**6.00%**	6.00%	6.00%
Active currency management assets	**-**	-	5.25%
Cash	**2.50%**	5.50%	5.25%

The assumptions used by the actuary are the best estimates chosen from a range of possible actuarial assumptions which, due to the timescales covered, may not necessarily be borne out in practice. The expected return on plan assets is based on market expectation at the beginning of the period for returns over the entire life of the benefit obligation.

c) Valuations

Assets of the schemes are held in order to generate cash to be used to satisfy the schemes' obligations, and are not necessarily intended to be realised in the short-term. The allocation of assets between categories is governed by the Investment Principles of each scheme and is the responsibility of the trustees of each respective scheme. The trustees should take due consideration of the Group's views and a representative of the Group attends Trustee Investment Committees. The fair value of the schemes' assets, which may be subject to significant change before they are realised, and the present value of the schemes' liabilities which are derived from cash flow projections over long periods and are inherently uncertain, are as follows:

	2009	2008	2007
	£m	£m	£m
Equities	**592**	1,040	1,208
Corporate bonds	**547**	237	221
Gilts	**545**	531	-
Property and property related funds	**71**	104	260
Active currency management assets	**-**	-	66
Cash	**3**	27	19
Total fair value of schemes' assets	**1,758**	1,939	1,774
Present value of defined benefit funded obligation	**(1,807)**	(2,007)	(1,972)
Net pension liability recognised in the balance sheet	**(49)**	(68)	(198)
Related deferred tax asset (note 19)	**14**	19	59
Net deficit	**(35)**	(49)	(139)

The movement in the fair value of the schemes' assets over the year was as follows:

	2009	2008	2007
	£m	£m	£m
Fair value of scheme assets at start of period	**1,939**	1,774	1,536
Expected return on scheme assets	**130**	116	102
Actuarial (losses)/gains	**(425)**	(113)	78
Employer contributions	**141**	193	94
Employee contributions	**10**	10	11
Benefits paid	**(37)**	(41)	(47)
Fair value of scheme assets at end of period	**1,758**	1,939	1,774

The above pension scheme assets do not include any investments in the Parent Company's own shares or property occupied by any member of the Group.

The movement in the present value of the defined benefit obligation during the period was as follows:

	2009	2008	2007
	£m	£m	£m
Defined benefit obligation at start of period	**(2,007)**	(1,972)	(1,952)
Current service cost	**(38)**	(44)	(53)
Employee contributions	**(10)**	(10)	(11)
Interest on defined benefit obligation	**(113)**	(99)	(95)
Actuarial gain recognised in the SoRIE	**324**	77	92
Benefits paid	**37**	41	47
Defined benefit obligation at end of period	**(1,807)**	(2,007)	(1,972)

The cost of buying out pension benefits with an insurer was estimated in the recent actuarial valuations to be £2,300m at April 2007, versus assets of £1,939m at February 2008. This is a deficit of £361m or solvency funding ratio of 84%.

The cost of providing pensions equivalent to the level of compensation paid by the Pension Protection Fund was estimated to be £1,633m at April 2007, compared with assets of £1,939m at February 2008. This is a Pension Protection Fund surplus of £306m or a funding ratio of 119%.

d) Sensitivities

Below is listed the impact on the liabilities at 1 February 2009 of changing key assumptions whilst holding other assumptions constant:

Discount factor	+/- 0.1%	£39m
Longevity	+/- 1 year	£48m

e) Income statement

The following amounts have been charged in employee benefits as set out in note 3 in arriving at operating profit:

	2009	2008	2007
	£m	£m	£m
Current service cost	**(38)**	(44)	(53)

The amounts for current and past service cost have been charged the following income statement lines:

	2009	2008	2007
	£m	£m	£m
Cost of sales	**30**	35	42
Administrative expenses	**8**	9	11
	38	44	53

The following amounts have been included in finance income:

	2009	2008	2007
	£m	£m	£m
Expected return on pension scheme assets	**130**	116	102
Interest on pension scheme liabilities	**(113)**	(99)	(95)
	17	17	7

f) Actuarial gains and losses recognised in the statement of recognised income and expense (SoRIE)

The amounts included in the statement of recognised income and expense were:

	2009	2008	2007
	£m	£m	£m
Actual return less expected return on scheme assets	**(425)**	(113)	78
Experience gains and losses arising on scheme obligation	**(4)**	83	37
Changes in demographic and financial assumptions underlying the present value of scheme obligations	**328**	(6)	55
Actuarial movement recognised in the SoRIE	**(101)**	(36)	170
Taxation on actuarial movement in the SoRIE	**29**	10	(51)
Net actuarial movement recognised in the SoRIE	**(72)**	(26)	119

	2009	2008	2007
	£m	£m	£m
Cumulative gross actuarial movement recognised in the SoRIE	**(88)**	13	49
Taxation on cumulative actuarial movement recognised in the SoRIE	**24**	(5)	(15)
Cumulative net actuarial movement recognised in the SoRIE	**(64)**	8	34

The actual return on schemes' assets can therefore be summarised as follows:

	2009	2008	2007
	£m	£m	£m
Expected return on schemes' assets	**130**	116	102
Actuarial movement recognised in the SoRIE reflecting the difference between expected and actual return on assets	**(425)**	(113)	78
Actual return on schemes' assets	**(295)**	3	180

The expected return on schemes' assets was determined by considering the expected returns available on the assets underlying the current investment policy. Expected yields on fixed interest investments are based on gross redemption yields as at the balance sheet date. Expected returns on equity and property investments reflect long term real rates of return experienced in the respective markets.

g) History of experience gains and losses

	2009	2008	2007	2006	2005
	£m	£m	£m	£m	£m
Difference between the expected and actual return on scheme assets:					
- Amount	**(425)**	(113)	78	165	60
- Percentage of scheme assets	**(24.2%)**	(5.8%)	4.4%	10.8%	4.9%
Experience gains and losses arising on scheme liabilities:					
- Amount	**(4)**	83	37	14	(33)
- Percentage of present value of scheme obligation	**(0.2%)**	4.1%	1.9%	0.7%	(2.1%)
Effects to changes in the demographic and financial assumptions underlying the present value of the scheme liabilities:					
- Amount	**328**	(6)	55	(219)	(107)
- Percentage of present value of scheme obligation	**18.2%**	(0.3%)	2.8%	(11.2%)	(6.6%)
Total amount recognised in the SoRIE:					
- Amount	**(101)**	(36)	170	(40)	(81)
- Percentage of present value of scheme obligation	**(5.6%)**	(1.8%)	8.6%	(2.1%)	(5.0%)
Total value of schemes' assets	**1,758**	1,939	1,774	1,536	1,217
Present value of defined benefit obligation	**(1,807)**	(2,007)	(1,972)	(1,952)	(1,625)
Net pension liability recognised in the balance sheet	**(49)**	(68)	(198)	(416)	(408)

h) Defined contribution pension scheme

Employees joining the company after September 2000 are no longer eligible to gain automatic entry into the final salary pension scheme. In June 2001 the company established a stakeholder pension scheme, open to all employees, to which the Company makes matching contributions of a maximum of 5% of eligible earnings. Pension costs for the defined contribution scheme are as follows:

	2009 **£m**	2008 £m	2007 £m
Stakeholder pension scheme	**(3)**	(3)	(1)
Life assurance scheme	**(1)**	(1)	(1)
Total costs	**(4)**	(4)	(2)

21 Provisions

	Restructuring **£m**	**Property provisions** **£m**	**Total** **£m**
At 3 February 2008	29	110	139
Charged to the income statement	-	5	5
Unused amounts reversed during the period	(8)	-	(8)
Utilised in period	(21)	(9)	(30)
Unwinding of discount	-	6	6
At 1 February 2009	**-**	**112**	**112**

a) Restructuring

The restructuring of the Group's distribution centres, begun in 2006, was concluded in the year. The original provision made, of £75m, was not fully utilised and an unspent balance of £8m was therefore reversed in the period. The remaining provision at the start of the year, relating to the Group's change in corporate logo, was fully utilised in the year.

b) Property provisions

Property provisions comprise onerous leases provision, petrol filling station decommissioning reserve and provisions for dilapidations on leased buildings.

Onerous leases relate to sublet and vacant properties. Where the rent receivable on the properties is less than the rent payable, a provision based on present value of the net cost is made to cover the expected shortfall. The lease commitments range from 1 to 65 years. Market conditions have a significant impact and hence the assumptions on future cash flows are reviewed regularly and revisions to the provision made where necessary. As noted in the financial review, adjustments have been made to reflect the change in market conditions and the legislative changes in respect of rates charges for empty properties.

Other property provisions comprise petrol filling station decommissioning reserve and dilapidations cost. Provision is made for decommissioning costs for when the petrol filling station tanks reach the end of their useful life or when they become redundant and is based on the present value of costs to be incurred to decommission the petrol tanks. Dilapidation costs are incurred to bring a leased building back to the condition in which it was originally leased. Provision is made for these costs, which are incurred on termination of the lease.

22 Called-up share capital

	Number of shares Millions	Share capital £m	Share premium £m	Total £m
Current year				
At 3 February 2008	2,686	269	57	326
Shares purchased for cancellation	(58)	(6)	-	(6)
Share options exercised	2	-	3	3
At 1 February 2009	**2,630**	**263**	**60**	**323**
Prior year				
At 4 February 2007	2,677	268	41	309
Share options exercised	9	1	16	17
At 3 February 2008	**2,686**	**269**	**57**	**326**

The total authorised number of ordinary shares is 4,000m shares (2008: 4,000m shares) with a par value of 10p per share (2008: 10p per share). All issued shares are fully paid.

The holders of ordinary shares are entitled to receive dividends as declared from time-to-time and are entitled to one vote per share at the meetings of the Company.

a) Potential issues of ordinary shares

Certain eligible employees hold options to subscribe for shares in the Company at prices ranging from 0p to 247p under the share option schemes approved by Shareholders. Options on two million shares (2008: nine million) were exercised in the current financial year.

b) Preference shares

The 5¼% cumulative 282,666 preference shares with nominal amount of £1, amounting to £0.3m have been classified as a current financial liability in accordance with IFRS 7 *Financial instruments: Disclosure*. These preference shares do not carry any voting rights.

23 Reconciliation of movements in capital and reserves

	Share capital £m	Share premium £m	Capital redemption reserve £m	Merger reserve £m	Hedging reserve £m	Retained earnings £m	Total £m
Current year							
At 3 February 2008	269	57	-	2,578	6	1,468	4,378
Share options exercised	-	3	-	-	-	-	3
Shares purchased for cancellation	(6)	-	6	-	-	(146)	(146)
Total recognised income and expense	-	-	-	-	6	396	402
Share option charge	-	-	-	-	-	14	14
Dividends	-	-	-	-	-	(131)	(131)
At 1 February 2009	**263**	**60**	**6**	**2,578**	**12**	**1,601**	**4,520**

	Share capital £m	Share premium £m	Capital redemption reserve £m	Merger reserve £m	Hedging reserve £m	Retained earnings £m	Total £m
Prior year							
At 4 February 2007	268	41	-	2,578	(1)	1,041	3,927
Total recognised income and expense	-	-	-	-	7	526	533
Share issues	1	16	-	-	-	-	17
Share option charge	-	-	-	-	-	9	9
Dividends	-	-	-	-	-	(108)	(108)
At 3 February 2008	**269**	**57**	**-**	**2,578**	**6**	**1,468**	**4,378**

Included in retained earnings is a deduction of £44m (2008: £44m) in respect of treasury shares held at balance sheet date. This represents the cost of 17,641,448 (2008: 17,641,448) of the Company's ordinary shares (nominal value of £1.8m). These shares are held by a trust using funds provided by the Group and were acquired to meet obligations under the share option schemes. The costs of funding and administering the schemes are charged to the income statement of the Company in the period to which they relate. The market value of the shares at 1 February 2009 was £48m (2008: £53m). The trust has waived its rights to dividends. These shares are not treasury shares as defined by the London Stock Exchange.

a) Share buyback

The Company purchased 57,788,600 of its own shares in the open market for cancellation between 31 March 2008 and 21 November 2008 at a cost of £146m. The shares repurchased represent 2.15% of the ordinary share capital at 1 February 2009.

b) Merger reserve

The merger reserve represents the reserve in the Company's balance sheet arising on the acquisition in 2004 of Safeway Limited. In the opinion of the Directors, this reserve is not distributable and accordingly it will be carried forward as a capital reserve.

c) Hedging reserve

This represents the gains and losses arising on the cash flow hedge from the Group's cross-currency swaps, see note 18.

24 Cash flow from operating activities

	2009 £m	2008 £m
Profit for the period	**460**	554
Adjustments for:		
Taxation	**195**	58
Depreciation and amortisation	**290**	289
Profit on disposal of property, plant and equipment	**(2)**	(32)
Net finance cost (note 5)	**16**	-
Other non-cash changes	**17**	6
Excess of contributions over pension service cost	**(103)**	(148)
Increase in stocks	**(52)**	(74)
Increase in debtors	**(44)**	(60)
Increase in creditors	**214**	169
Decrease in provisions	**(27)**	(6)
Cash generated from operations	**964**	756

25 Analysis of net debt

	2009 £m	2008 £m
Cash and cash equivalents (note 15)	**327**	191
Bank overdraft (note 17)	**-**	(73)
Cash and cash equivalents per cash flow	**327**	118
Long term cash on deposit	**-**	74
Interest and cross-currency swaps	**81**	43
Financial assets (note 12)	**81**	117
Other loans	**-**	(2)
Finance lease obligations	**(1)**	(2)
Current financial liabilities (note 17)	**(1)**	(4)
Bonds	**(784)**	(758)
Floating credit facility	**(250)**	-
Other unsecured loans	**(15)**	(15)
Finance lease obligations	**-**	(1)
Non-current financial liabilities (note 17)	**(1,049)**	(774)
Net debt	**(642)**	(543)

26 Share-based payments

The Group operates a number of share-based payments schemes; (i) the Executive share option scheme, (ii) the Sharesave scheme and (iii) an equity-settled Long Term Incentive Plan ("LTIP"). In line with IFRS 2 *Share-based payment*, the Group has fair valued all grants of equity instruments issued after 7 November 2002 which were unvested as of 1 January 2005.

The total charge for the period relating to employee share-based payment plans was £14m (2008: £9m), all of which related to equity-settled share-based payment transactions. After corporation and deferred tax, the total charge in the income statement was £11m (2008: £7m).

a) Share option schemes

i) Executive share option scheme

In May 1995, the Group adopted the 1995 Senior Executive Share Option Scheme which was made available to Directors and other senior employees. The scheme was terminated on 25 May 2005. The scheme offered options at the market price two weeks prior to the date of the grant which are normally exercisable between three and ten years from the date of grant. The maximum exercise value of the ordinary shares subject to options held by an individual must not exceed the greater of four times earnings and £100,000. The exercise of options under the scheme is subject to performance criteria broadly requiring an increase in Group operating profits of at least 20% between the year prior to the date of the grant and its third or any succeeding anniversary. The scheme is equity-settled.

Those options which have been granted after 7 November 2002 have been fair valued using the Binomial stochastic option pricing model. The fair value per option granted and the assumptions were as follows:

Grant date	12 Nov 2004	02 Apr 2003
Share price at grant date	£2.33	£1.81
Fair value of options granted	£1.4m	£1.9m
Exercise price	£2.22	£1.75
Dividend yield	1.43%	1.49%
Annual risk free interest rate	4.61%	4.12%
Expected volatility*	29.4%	29.4%

*The volatility measured at the standard deviation of expected share price returns is based on statistical analysis on weekly share prices over the last six years.

The fair value calculations do not incorporate the effects of non-market vesting conditions, but the charge is adjusted to reflect an estimate of the number of options which vest.

	2009		2008	
	Weighted average exercise price in £ per share	**Options thousands**	Weighted average exercise price in £ per share	Options thousands
Movement in outstanding options				
Outstanding at start of period	**1.90**	**3,223**	1.91	5,901
Exercised	**1.98**	**(1,409)**	1.92	(2,678)
Expired	**-**	**-**	-	-
Outstanding at end of period	**1.84**	**1,814**	1.90	3,223
Exercisable at end of period	**1.84**	**1,814**	1.90	3,223

	2009		2008	
	Weighted average share price at date of exercise	**Number of shares**	Weighted average share price at date of exercise	Number of shares
Share options exercised in the financial period	**£2.84**	**1,409,000**	£3.10	2,678,000

	2009	2008
Share options outstanding at the end of the period		
Range of exercise prices	**£1.75 - £2.22**	£1.75 - £2.22
Weighted average remaining contractual file	**3.8 years**	5.0 years

ii) Sharesave scheme

The Sharesave scheme has been in operation since 18 May 2000 and all employees (including Executive Directors) are eligible once the necessary service requirements have been met. The scheme allows participants to save up to a maximum of £250 each month for a fixed period of three to five years. Options are offered at a discount of 20% to the mid-market closing price on the day prior to the offer and are exercisable for a period of six months commencing after the end of the fixed period of the contract. The exercise of options under this scheme is only subject to service conditions and is equity-settled.

Options granted before 7 November 2002

The Group has not fair valued the Sharesave plan since the grants of the options were all made before 7 November 2002 and remained unvested as at 1 January 2005.

	2009		2008	
	Weighted average exercise price in £ per share	**Options thousands**	Weighted average exercise price in £ per share	Options thousands
Movement in outstanding options				
Outstanding at start of period	**1.79**	**179**	1.80	7,681
Exercised	**1.76**	**(40)**	1.74	(6,570)
Expired	**1.79**	**(139)**	2.20	(932)
Outstanding at end of period	**-**	**-**	1.79	179
Exercisable at end of period	**-**	**-**	1.73	21

	2009		2008	
	Weighted average share price at date of exercise	**Number of shares**	Weighted average share price at date of exercise	Number of shares
Share options exercised in the financial period	**£2.89**	**40,000**	£2.97	6,570,000

	2009	2008
Share options outstanding at the end of the period		
Range of exercise prices	**-**	£1.73 - £1.79
Weighted average remaining contractual file	**-**	1.0 years

Options granted after 7 November 2002

Those options which have been granted after 7 November 2002 to those eligible employees, including Directors, who chose to participate in the scheme have been fair valued using the Binomial stochastic option pricing model. The fair value per option granted and the assumptions were as follows:

Grant date	18 May 2007	24 Apr 2006
Share price at grant date	£3.26	£1.94
Fair value of options granted	£12.3 m	£16.2m
Exercise price	£2.47	£1.58
Dividend yield	1.23%	1.91%
Annual risk free interest rate	5.58%	4.57%
Expected volatility*	23.5%	25.6%

*The volatility measured at the standard deviation of expected share price returns is based on statistical analysis on weekly share prices over the past 3.25 years prior to the date of grant.

The fair value calculations do not incorporate the effects of non-market vesting conditions.

	2009		2008	
	Weighted average exercise price in £ per share	**Options thousands**	Weighted average exercise price in £ per share	Options thousands
Movement in outstanding options				
Outstanding at start of period	**1.84**	**32,335**	1.58	25,754
Granted	**-**	**-**	2.47	10,617
Exercised	**1.61**	**(82)**	1.59	(46)
Expired	**2.01**	**(3,180)**	1.81	(3,990)
Outstanding at end of period	**1.83**	**29,073**	1.84	32,335
Exercisable at end of period	**-**	**-**	-	-

	2009		2008	
	Weighted average share price at date of exercise	**Number of shares**	Weighted average share price at date of exercise	Number of shares
Share options exercised in the financial period	**£2.69**	**82,000**	£3.02	46,000

	2009	2008
Share options outstanding at the end of the period		
Range of exercise prices	**£1.58 - £2.47**	£1.58 - £2.47
Weighted average remaining contractual file	**1.2 years**	2.3 years

b) Long Term Incentive Plans

i) Equity based Long Term Incentive Plan ("LTIP")

In May 2007, a discretionary Long Term Incentive Plan for the benefit of certain employees as approved by the Remuneration Committee was introduced. The awards are free share-based awards, with non-market vesting conditions attached, that accrue the value of dividends over the vesting period.

The maximum total market value of shares over which awards may be granted to any employee during any financial year of the company is 300% of salary. Awards normally vest three years after the original

grant date providing the relevant performance criteria have been met. Employees have six months from the vesting date to exercise their options after which they lapse.

The fair value at the date of grant, which is being charged to the income statement over the three year vesting period, has been calculated based on the following assumptions:

Grant date	14 Oct 2008	14 Apr 2008	24 Oct 2007	6 Jun 2007	24 May 2007
Share price at grant date	£2.42	£2.77	£2.88	£3.13	£3.23
Assumed leavers	5%	5%	4%	3%	3%
Performance criteria achieved	90%	90%	90%	90%	90%
Exercise price	£nil	£nil	£nil	£nil	£nil
Fair value of options granted	£0.6m	£12.5m	£0.4m	£0.1m	£10.5m

	2009		2008	
	Weighted average exercise price in £ per share	**Options thousands**	Weighted average exercise price in £ per share	Options thousands
Movement in outstanding share awards				
Outstanding at start of period	**-**	**4,470**	-	-
Granted	**-**	**6,128**	-	4,470
Expired	**-**	**-**	-	-
Outstanding at end of period	**-**	**10,598**	-	4,470
Exercisable at end of period	**-**	**-**	-	-

	2009	2008
Share awards outstanding at the end of the period		
Range of exercise prices	-	-
Weighted average remaining contractual file	**1.8 years**	2.4 years

27 Operating lease arrangements

a) Lessee arrangements

The Group has outstanding commitments for future minimum lease payments under non-cancellable operating leases, which fall due as follows:

	2009		2008	
	Property £m	**Vehicles, plant and equipment £m**	Property £m	Vehicles, plant and equipment £m
Within one year	**33**	**8**	34	10
More than one year and less than five years	**125**	**19**	127	26
After five years	**422**	**-**	427	-
	580	**27**	588	36

The Group leases various offices, stores and warehouses under non-cancellable operating lease agreements. The leases have various terms ranging from 4 to 11 years for vehicles, plant and equipment and 25 to over 100 years for property (including land), with varying escalation clauses and renewal rights. Generally all property leases are reviewed every five years to align them with market rentals.

b) Lessor arrangements

The Group has non-cancellable agreements with tenants and the future minimum lease income is as follows:

	2009 £m	2008 £m
Within one year	**28**	28
More than one year and less than five years	**94**	93
After five years	**159**	154
	281	275

The Group sub-lets buildings of various nature under non-cancellable agreements. The leases have various terms, escalation clauses and renewal rights.

28 Contingent liabilities

In September 2007 the Office of Fair Trading (OFT) issued a Statement of Objections to a number of grocery retailers and milk producers, alleging collusion in the setting of prices for certain dairy products in 2002 and 2003. Morrisons was accused in relation to one infringement in 2002, and has vigorously denied this. Based on the evidence put forward, the Board do not consider it probable that the Company will ultimately incur a fine, and accordingly have made no provision for any such liability.

The OFT have also raised a legal issue regarding the sale of tobacco and whether established industry practices represented a breach of competition law. It is likely that this can only be settled through a formal judicial process. The Board has not made a provision for such a liability.

29 Post balance sheet events

The Directors are proposing a final dividend in respect of the financial period ending 1 February 2009 of 5.0p per share which will absorb an estimated £131m of Shareholders' funds. Subject to approval at the AGM, it will be paid on 10 June 2009 to shareholders who are on the register of members on 8 May 2009.

A dividend reinvestment plan is available in respect of the final dividend.

The Group have entered into further commodity price contracts since the year end to reduce the Group's exposure to pricing risk arising on the volatility of commodity prices purchased for the Group's own consumption.

30 Principal subsidiaries

Wholly-owned subsidiaries of Wm Morrison Supermarkets PLC	Principal activity
Bos Brothers Fruit and Vegetables BV	Produce wholesaler
Farmers Boy Limited	Manufacturer and distributor of fresh food products
Farock Insurance Company Limited	Captive insurer
Neerock Limited	Fresh meat processor
Wm Morrison Produce Limited	Produce packer
Safeway Limited	Holding company
Rathbone Kear Limited	Baker
Wholly-owned subsidiaries of Safeway Limited	
Safeway Overseas Limited	Grocery retailer
Safeway Stores Limited	Grocery retailer

All of the above companies are registered in England and Wales except Bos Brothers Fruit and Vegetables BV which is incorporated in The Netherlands and Farock Insurance Company Limited which is incorporated in the Isle of Man.

The principal area of trading for all the above companies is the United Kingdom apart from Bos Brothers Fruit and Vegetables BV and Safeway Overseas Limited who also trade in the rest of Europe.

On 3 February 2008, one of the Group's subsidiaries, Holsa Limited, ceased trading and its activities were subsumed within another Group subsidiary.

In addition to the above, the Company has a number of other subsidiary companies, particulars of which will be annexed to the next annual return.