**Possible offer for Home Retail Group plc by J Sainsbury plc**

2 February 2016

For immediate release

The Boards of J Sainsbury plc ("Sainsbury's") and Home Retail Group plc ("Home Retail Group" or the "Company") announce that they have reached agreement on the key financial terms of a possible offer for Home Retail Group by Sainsbury's (the "Possible Offer").

**Terms of the Possible Offer**

Under the terms of the Possible Offer Home Retail Group shareholders will receive per Home Retail Group share:

- 0.321 New Sainsbury's shares; and
- 55 pence in cash.

**Proposed Capital Returns**

In addition, Home Retail Group shareholders will receive payments as set out below (together, the "Proposed Capital Returns") per Home Retail Group share, payable before completion of the Possible Offer, of:

- approximately 25 pence (the "Homebase Capital Return"); and
- 2.8 pence in lieu of a final dividend in respect of the financial year ending 27 February 2016 (the "Additional Capital Return").

The Homebase Capital Return reflects the £200m return in respect of (and conditional upon) the sale of Homebase, announced by Home Retail Group on 18 January 2016 (the "Homebase Sale"). Home Retail Group intends to pay the Homebase Capital Return and the Additional Capital Return (or a final dividend) whether or not the Possible Offer is made or completed.

The Possible Offer implies a value of approximately £1.1bn for Home Retail Group's share capital, based on the closing price of Sainsbury's shares on 1 February 2016. The Possible Offer and Proposed Capital Returns together imply a value of approximately 161.3 pence per Home Retail Group share, based on the closing price of Sainsbury's shares on 1 February 2016, and a value of approximately £1.3bn for Home Retail Group's share capital.

The Possible Offer and Proposed Capital Returns together represent a premium of approximately 63% to the closing price of a Home Retail Group share on 4 January 2016, the last business day prior to the start of the offer period.

The Possible Offer will also include a mix and match facility[1].

Under the terms of the Possible Offer, Home Retail Group shareholders will own approximately 12 per cent. of the combined group (the "Combined Group"), based on the current issued share capital of Sainsbury's and Home Retail Group.

*Note:*

*[1] Satisfaction of elections under the mix and match facility will be subject to equal and opposite elections made by other Home Retail Group shareholders*

**Intention to Recommend**

Whilst the Board of Home Retail Group continues to believe in the prospects for the standalone Company, it recognises that the Possible Offer will provide an attractive opportunity for Home Retail Group shareholders to receive a full valuation for their shares, and, through their shareholding in the Combined Group, also to participate in the value created by the Combined Group from the transaction.

The Board of Home Retail Group has indicated to Sainsbury's that it is willing to recommend the key financial terms of the Possible Offer to Home Retail Group shareholders, subject to its fiduciary duties and reaching agreement on the other terms and conditions and the satisfactory completion of reciprocal due diligence. Any transaction will be subject to regulatory approval and the completion of the sale of Homebase (amongst other conditions).

**Transaction Rationale**

The combination of Sainsbury's and Home Retail Group is an attractive proposition for the customers and shareholders of both companies, establishing a platform for long-term value creation. The combination is an opportunity to bring together two of the UK's leading retail businesses, with complementary product offers, focused on delivering quality products and services at fair prices, through an integrated, multi-channel proposition.

Specifically, the combination of Home Retail Group and Sainsbury's will:

- Create a food and non-food retailer of choice for customers, building on the strong heritages of both businesses whose brands are renowned for trust, quality, value and customer service;

- Deliver profitable sales growth by offering customers the right combination of location, range, speed and flexibility, across a wide range of products;

- Bring together multi-channel capabilities including digital, store and delivery networks to provide fast, flexible and reliable product fulfilment to store or to home across a wide range of food and non-food products;

- Optimise the use of their combined retail space. The combined entity will have attractively located stores across the UK, with an enhanced supply and delivery network and a strong presence across food and grocery, clothing, homewares, toys, stationery, electricals, furniture and other general merchandise;

- Create a financial services proposition that will provide a wider range of customer-centric services including credit cards, loans, deposits, insurance and ATMs; and

- Deliver significant revenue and cost synergy potential, as outlined further below.

**Financial Impact**

Sainsbury's expects the Possible Offer will be accretive to its earnings per share in the first full year following completion. In the third full year following completion Sainsbury's also expects the Possible Offer will result in double digit earnings per share accretion and a low to mid-teens return on invested capital (inclusive of implementation costs)[(2)].

Further to the strategic rationale as outlined in the Sainsbury's investor presentation dated 13 January 2016, Sainsbury's believes that the combination of Sainsbury's and Home Retail Group will generate EBITDA synergies of not less than £120m in the third full year after completion, as described further below. Sainsbury's believes that these synergies further enhance the attractiveness of the Possible Offer.

The constituent elements of quantified synergies, which are in addition to savings previously targeted by Sainsbury's and Home Retail Group separately, comprise the following:

- approximately one-half of the identified synergies are expected to be generated from Argos concessions, arising from (i) cost savings generated from the relocation of certain existing Argos stores into concessions in Sainsbury's stores, and (ii) revenue gains from new concessions within Sainsbury's stores, including but not limited to cross-selling opportunities and the expansion of Click and Collect desks;
- approximately one-third of the identified synergies are expected to be cost synergies generated by removing duplication and overlap from both central and support functions at Sainsbury's and Home Retail Group, together with procurement benefits resulting from the Combined Group's scale; and
- the remainder of the identified synergies are expected to be further revenue synergies, principally from the sale of Sainsbury's clothing, homewares and seasonal and leisure ranges through the existing Argos network.

It is expected that the realisation of the identified synergies will require one-off exceptional costs of approximately £140 million, split equally across the first three full years following completion.

It is also expected that incremental capital expenditure of approximately £140 million will be incurred in the three years following completion, relating to store fit-out expenditure. Approximately 20% of this capital expenditure will be incurred in the first year, with the remainder split equally in the second and third year following completion.

The synergies referred to above are expected to be recurring and are expected to arise as a direct result of the Possible Offer and could not be achieved independently of the Possible Offer. The synergies are also stated net of anticipated dis-synergies, arising principally from potential cannibalisation of Argos store revenue (where an existing standalone Argos store is in the vicinity of a newly established Argos concession store within a Sainsbury's supermarket). For the avoidance of doubt, the EBITDA impact of the synergies as set out above already reflects the impact of these identified dis-synergies.

Please refer to the Appendix entitled "Quantified Financial Benefits Statement" for further detail on the above. The Quantified Financial Benefits Statement has been reported on under the Code by Deloitte LLP, Sainsbury's reporting accountant, and by Morgan Stanley and UBS, Sainsbury's financial advisers, as set out in Part B and Part C of the Appendix to this announcement.

Sainsbury's intends to finance the cash consideration for the Possible Offer through its existing debt facilities and resources, to be entirely refinanced at a later date through the proposed transfer of the Financial Services business to Sainsbury's Bank. This would have the consequence of lowering Group leverage (excluding Sainsbury's Bank) relative to Sainsbury's current standalone Group leverage.

*Note:*
*[2] Return on invested capital defined as acquired post-tax EBIT plus post-tax synergies divided by purchase price plus implementation costs net of tax*

**Reservations**

The Possible Offer does not impose any obligation on Sainsbury's to make an offer, nor does it evidence a firm intention to make an offer within the meaning of the Code. Sainsbury's does not, therefore, regard it as forming the basis for an announcement pursuant to Rule 2.2(a) of the Code.

Sainsbury's also reserves the right:

- to make an offer at any time on reduced terms than 0.321 New Sainsbury's shares and 55 pence in cash for each Home Retail Group share:
  - with the agreement or recommendation of the Board of Directors of Home Retail Group;
  - if a third party announces a firm intention to make an offer for Home Retail Group pursuant to Rule 2.7 of the Code, which, at that date is valued at a lower price than the value of 0.321 New Sainsbury's shares and 55 pence in cash for each Home Retail Group share and the Proposed Capital Returns (less any additional dividends declared, made or paid);
  - if Home Retail Group announces, declares or pays any dividend or any other distribution to shareholders (other than the Proposed Capital Returns), in which case Sainsbury's reserves the right to make an equivalent reduction in its offer price; or
  - following announcement by Home Retail Group of a whitewash transaction pursuant to the Code; and
- to introduce other forms of consideration and/or vary the mix or composition of consideration of any offer.

Any firm offer in accordance with Rule 2.7 of the Code (a "Firm Offer") will be subject to, amongst other things, satisfactory completion of due diligence and the recommendation of Home Retail Group's Board of Directors.

**The Homebase Sale**

Completion of the Homebase Sale is expected to be a condition to a Possible Offer by Sainsbury's. The Homebase Sale is expected to proceed, subject to shareholder approval, as indicated in the Company's announcement of 18 January 2016. A circular containing further details of the Homebase Sale and a notice convening a general meeting will be sent to Home Retail Group shareholders as soon as practicable, with completion of the Homebase Sale expected to occur during the first quarter of the 2016 calendar year.

**Timetable Extension**

In order to facilitate due diligence, the Board of Home Retail Group and the Takeover Panel have agreed to a three week extension of the relevant deadline in accordance with Rule 2.6(c) of the Code. As a result and in accordance with Rule 2.6(a) of the Code, Sainsbury's must, by not later than 5.00 p.m. on 23 February 2016, either announce a firm intention to make an offer for Home Retail Group in accordance with Rule 2.7 of the Code or announce that it does not intend to make an offer for Home Retail Group, in which case the announcement will be treated as a statement to which Rule 2.8 of the Code applies.

There can be no certainty that Sainsbury's will proceed to make a Firm Offer for Home Retail Group. A further announcement will be made in due course.

***[For a full and complete statement, please go to www.homeretailgroup.com]***