

M&S and Ocado announce new Joint Venture

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Press Release

****NEWSWIRE & PRESS CONFERENCE CALL AT 7.20AM.
FULL DETAILS IN NOTES TO EDITORS****

THIS ANNOUNCEMENT CONTAINS INSIDE INFORMATION FOR
IMMEDIATE RELEASE

Marks and Spencer Group Plc Bringing the Best Together: Transforming UK online grocery shopping M&S and Ocado announce new Joint Venture

Marks and Spencer Group Plc ("M&S"), the unique own brand retailer, today announces the creation of a new 50/50 Joint Venture ("JV") with Ocado Group Plc ("Ocado"), the UK's leading pure play digital grocer, that will transform online grocery shopping for UK consumers.

Under the JV, M&S is acquiring a 50% share of Ocado's UK retail business, which will be supported by Ocado Smart Platform ("OSP"), for a total consideration of up to £750m, including a deferred consideration of up to £187.5m, plus interest.

The JV combines the strength of M&S's brand and its leading food quality and innovation with Ocado's unique and proprietary technology to create an unrivalled online offer for our customers. In bringing the

best together the JV will benefit existing and new UK customers, colleagues and suppliers.

The JV will trade as Ocado.com but benefit from access to M&S's brand, products and customer database from September 2020 at the latest, following the termination of the current Waitrose sourcing agreement and migration of JV sourcing to M&S.

Joint Venture highlights

- A strategically compelling route to unlock growth for M&S Food through a profitable, scalable presence in the online grocery market, the UK's fastest growing channel;
- A fully aligned partnership with complementary skills and assets; M&S, one of Britain's highest rated food brands with strong product development capabilities, and Ocado's pioneering OSP technology and operational efficiency;
- Long-term value creation opportunities for both M&S and the JV. Customers will benefit from the broadest range in UK food retail and the JV will benefit from access to over 12m M&S Food shoppers;
- For the 52 weeks ended 2 December 2018, the newly created JV would have generated revenue¹ of £1,468m and EBITDA² of £34.2m, taking into account the newly created OSP contract and other fees and services. Furthermore, under the new sourcing arrangement the JV will no longer incur sourcing fees payable to Waitrose, which were over £15m in 2018.

Transaction highlights

- Significant potential synergies for M&S Food estimated of at least £70m per annum to be achieved by the third year following completion. These are expected to arise from increased buying scale, harmonised buying terms, conversion of M&S customers who currently account for c. one third of online grocery spend, joint marketing, shared innovation, and complementary category and regional mixes;
- The transaction will be primarily financed by equity. The Board intends to conduct a Rights Issue to raise up to £600m, which will be launched in due course, and which is fully underwritten on a standby basis by Morgan Stanley;
- Concurrently the M&S dividend per share is being reset by 40% to a sustainable level from which to grow in line with earnings over time. As a result, we anticipate paying a final dividend in respect of 2018/19 of 7.1 pence per share;
- Current trading remains in line with Board expectations.

Steve Rowe, M&S CEO said:

"I have always believed that M&S Food could and should be online. Combining the strength of our food offer with leading online and delivery capability is a compelling proposition to drive long-term growth.

"Our investment in a fully aligned joint-venture with Ocado accelerates our Food strategy as it enables us to take our food online in an immediately profitable, scalable and sustainable way.

"Combining the magic of M&S Food with Ocado's leadership in online technology allows us to transform UK online grocery shopping by offering customers the broadest, most innovative and relevant range in UK food retail with award-winning service. Our partnership with Ocado will create shared value for our customers, colleagues, supplier partners and shareholders, operating with a common sense of purpose and values.

"This is a transformational step forward in shaping the future of M&S and in becoming a truly digital first retailer with at least a third of the business online."

Tim Steiner, Ocado CEO said:

"We are delighted that our UK retail business will become a joint venture with M&S. This is a transformative moment in the UK retail sector with the combination of two iconic and much-loved retail brands set to provide an unrivalled online grocery offer.

"We believe that this is the best outcome for customers, offering even greater range, service, quality and value; the best outcome for our Ocado Solutions partners, creating a stronger platform from which to innovate and develop our unique and proprietary technology; the best outcome for Ocado Solutions with a further endorsement from another leading global retailer; and the best outcome for our financial stakeholders, unlocking the significant value embedded in Ocado Retail.

"The combination of Ocado and M&S will allow us to grow faster, add more jobs, and create more value, as we lead the channel shift to e-commerce here in the UK. We are very excited by the many opportunities ahead."

Transaction rationale

M&S has embarked on a major transformation programme to reshape its business, organisation and culture. Our objective is to create a profitable, growing family of businesses within three to five years, bound together not only by shared sites but by a shared consumer brand,

colleagues, values, technology and customer data. Our Food business is recognised for its strong focus on quality and innovation; but to evolve with the market we need to broaden our offering and to secure access to the fastest growing channel. This partnership represents a unique opportunity within our transformation programme to unlock growth within our Food business.

M&S's prior online trial was uneconomic due to the high cost of manually picking from store, including costs associated with moving stock from DCs to stores and store replenishment costs. Developing best in class technology and investing in fulfilment centres would delay the implementation of our transformation programme and carry significant execution risk.

The combination with Ocado enables the delivery of a full grocery shop and is the optimal strategy to access online growth, as well as leveraging our existing strengths in food for now and food for tonight through Ocado's delivery innovations, such as the Ocado 'Zoom' trial.

The JV provides M&S with a profitable, scalable presence in online grocery, where currently it has a minimal presence. Online is forecast to be the fastest growing channel, increasing from a £11bn market in 2018 to £17bn in 2023, set to capture over 20% of forecast UK market growth yet still only accounting for 7% of total grocery spending today. The partnership offers a strategically compelling route to accessing this growth channel.

The JV will work as a true partnership aiming to create the UK's leading online grocery business. Ocado is the leading pure play online grocery player in the UK with a 15%³ share of the online UK grocery market, growing at an average rate of 13% over the last three years. Ocado serves over 700,000 customers, offering over 50,000 products and fulfilling over 290,000 orders a week. The Ocado OSP technology provides an infrastructure solution to automate order fulfilment and improve accuracy, whilst also enabling customers to shop online in the most convenient way for them.

The JV will also have access to the c. seven million members of "Sparks", M&S's loyalty programme, and c. three million active M&S Bank customers, together with its growing online database, with the potential to build an integrated loyalty programme with strong insights and personalised rewards.

Building on the strong platform Ocado has developed and leveraging M&S's highly rated Food brand, there are significant value creation

opportunities for the combined businesses. In addition, we expect to generate at least £70m of synergies for M&S by the third year following completion including:

- Meaningful scale boost and improved sourcing economics to M&S own label and branded products. This sourcing benefit will grow as the JV scales;
- Enable faster testing of new product development and significantly reduce trial and development costs.

Other value creation opportunities for M&S include:

- Additional sales from attracting new customers to the JV;
- Use and rebrand Ocado own label as M&S opening price point product in stores;
- Access to the unique range from Ocado's innovative partners to add to our core offer and provide insight and options for greater innovation;
- Spreading M&S's innovation costs over a larger sales and customer base;
- Cross-marketing opportunities for M&S's Clothing & Home and financial services businesses;
- Using M&S's complementary geographic strengths to develop the JV outside of London and the south of the UK.

Transaction Terms

M&S is paying Ocado up to £750m for its 50% stake in the JV; £562.5m on completion and up to £187.5m, plus interest, payable after five years, conditional on reaching agreed financial and operational targets.

Ocado will transfer retail customers, sales and supplier relationships, some vehicle assets and central retail functions to the JV. The JV will carry out all pricing, category management, marketing and brand communications. Ocado will provide the end-to-end e-commerce platform and access to throughput and service levels from CFC technology in return for an OSP fee paid by the JV under a long-term contract. Ocado will provide third-party logistics services to operate the CFCs and driver management for a management fee from the JV. M&S will provide its product range and development capabilities to the JV at cost from September 2020 at latest.

The board of the JV will be shared 50/50 between M&S and Ocado, with each having the right to appoint two directors. For five years from completion, Ocado shall have the right to appoint the CEO, and M&S one of the JV's directors as Chair. The management team of the JV, other than the CEO, will be appointed by the JV Board, with Lawrence

Hene, currently Ocado's Commercial Director, being appointed as interim MD of the JV to lead its establishment.

We expect the Transaction to close in calendar Q3 2019.

Financial Highlights

For the 52 weeks ended 2 December 2018 the JV would have generated revenue¹ of £1,468m and EBITDA² of £34.2m, taking into account the newly created OSP contract and other fees and services. Furthermore, under the new sourcing arrangement the JV will no longer incur sourcing fees payable to Waitrose, which were over £15m in 2018. The value of the gross assets⁴ the subject of the transaction is estimated to be £164m. The investment will be accounted for as an associate.

The JV's investment requirements will include investment in new CFC buildings, refrigeration equipment, spokes and home delivery vans. The JV will also incur a number of transition costs following completion.

Transaction Financing

The transaction will be primarily equity financed. The Board intends to conduct a Rights Issue to raise up to £600m which will be launched in due course following the publication of our audited 2019 financial statements. The Rights Issue has been fully underwritten on a standby basis by Morgan Stanley.

Dividend Reset

We are taking proactive steps to strengthen our balance sheet to provide a secure platform for the Group's transformation programme, and the right balance of investment and shareholder returns.

In addition to the rights issue, the Board is resetting our dividend per share by 40% to a sustainable level, which we aim to grow in line with earnings over time. This will begin with a reduction in the final dividend for 2018/19 to 7.1 pence. The 2018/19 final dividend and prior dividends will be restated in future accounts to reflect the bonus factor adjustment resulting from the rights issue in due course.

Current Trading

On 10 January 2019, M&S announced its trading statement outlining its trading performance for the 13 weeks to 29 December 2018. Since that date, the Group's performance continues to be in line with the Board's expectations. We will report our Full Year Results on 22 May 2019.

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Investor & Analyst call:

A call will be hosted by Steve Rowe and Humphrey Singer at 8am on 27 February 2019:

Dial in number: +44 (0)330 336 9411

Confirmation Code: 5632370

Slides to accompany the call will be available via the following link:

<https://slideassist.webcasts.com/starthere.jsp?ei=1234605>

A recording of this call will be available:

Dial in number: +44 (0)20 7660 0134

Replay Code: 5632370

Newswire and Press Conference Call:

This will be jointly hosted by Steve Rowe, Marks & Spencer CEO and Tim Steiner, Ocado CEO.

Participant Dial In: +44 (0)330 336 9125 Confirmation Code: 5310360

A replay facility of this call will be available.

Replay: +44 (0)20 7660 0134

Replay Passcode: 5310360

¹ Revenue figure derived from unaudited management accounts for Ocado retail business and reflecting JV perimeter adjustments. Unaudited and for illustrative purposes only.

² EBITDA figure derived from unaudited management accounts for Ocado retail business, taking into account the new OSP contract and fees and services anticipated to be payable to Ocado and reflecting JV perimeter adjustments. Unaudited and for illustrative purposes only.

³ Source: Kantar, on the basis of market share by online orders.

⁴ Gross assets figure derived from unaudited management accounts, representing the assets that will form part of the JV, unaudited and for illustrative purposes only.

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- Ends -

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