MORRISONS

Slide 1
Dalton Philips

Good morning, welcome and thank you for being here at our Prelims announcement for the year ended February 2nd 2014.

Given the amount of information we want to share with you this morning, we're going to run slightly longer than we usually do. I hope this is okay with you all.

Last year was a difficult year. That's been reflected both in our top and bottom line. There is a paradigm shift taking place in the market, to which we must respond.

Today we are announcing how we will prosper in this challenging environment. We are putting value at the heart of our proposition. We will be making a significant investment over the next three years, to ensure that we can compete aggressively:

a. We will lower more prices on a permanent basis.

b. We will offer fewer, more impactful promotions.

c. We will invest further in our Own Brand as a real source of competitive advantage.

d. We will continue to improve the overall shopping experience for our customers.

e. We will launch our Morrisons card to deepen our relationship with individual customers and offer personalised value.

f. And we will deliver a more focused, consistent communication drumbeat.

2. To help fund this program, we've identified £1bn of 'self-help' over three years to invest back into our business.

3. These actions will mean a rebased profit outlook for this year with a range of £325M to £375M at an underlying level.

4. Alongside this investment in the core offer, we're going to continue with our aggressive plan in our new channels of convenience and food online.

5. To enable total focus on this plan, we're going to exit all non-core activities, including the sale of Kiddicare and our stake in FreshDirect.

6. We've identified meaningful ways to improve our working capital, reducing it by £600M over three years.

7. Having reassessed our new space pipeline we will be cutting our capex in half going forward. We've also taken a large impairment on both sites and store assets that won't deliver the appropriate return.

8. We've identified £1bn of non-core property disposals over the next three years, but will maintain an overwhelmingly freehold estate.

9. All this will result in free cash flow improvement of nearly £1bn this year, compared to the year we've just finished.

10. And we're also confirming a 5% growth underpin to the 14/15 dividend.

This is a bold plan, which will take time to execute, and the benefits won't be immediate. However, we are taking these decisive steps to get the business firmly back on track in this new environment.

Now let me hand you over to Trevor to take you through the details of the 2013/14 results.

Slide 2
Trevor Strain
Thank you Dalton and good morning everyone.

In this first part of the presentation, I will review our financial performance for the year. Later I will be updating you on our financial strategy and the results of our property review.

Slide 3
Financial summary
I will start with our usual financial summary. Sales of £17.7bn were down 2% year on year. Please note, that last year was a 53 week year. After adjusting for that, total sales were down by 0.6%, which was mainly accounted for by lower fuel sales. At an operating level we made a loss of £94m.

Excluding non-recurring exceptional costs, primarily impairments, which I will come back to later, we delivered an operating profit of £865m. This is down 11% on prior year and is a reflection of our overall sales performance, and the investment we have been making in developing our new business channels. A similar profile is seen in PBT.

In deriving our underlying profit number, which was down 13% in the year, we exclude the cost of the new business channels and impairments, as well as property disposal profits and IAS 19 pension interest. I will provide some more colour around these movements in a moment. Underlying EPS was down by 8%.

In 2011, we set out a policy to deliver annual double digit dividend growth for three years, and in line with that commitment, I am pleased to confirm we have increased our final dividend for the current year by 10%.

Slide 4
Turnover bridge

Moving now into the detail of the results, I will start with our turnover bridge, with which you will be familiar.

So, moving left to right, the impact of 2012/13 being a 53 week year is clearly shown. New stores contributed 2.9% to sales in the year, including the contribution from an accelerating convenience store rollout. Sales from our like-for-like stores fell by £379m, down by 2.8%.

Moving to fuel – sales were down by 6% primarily from lower volumes, the result of reducing our promotions in the year. We also saw an increase in Other sales, driven primarily by managing the capacity of our manufacturing operations, through growing sales to third parties.

Slide 5
Turnover bridge - sales by channel

This next slide breaks out the drivers of growth by channel, excluding fuel. Overall sales were down by £250m, but broadly flat when the impact of the 53rd week is removed. The contraction in our core supermarkets was offset by the significant growth in our M local convenience format, which contributed £52m to our grocery growth in the period.

We are also delighted to be able to flag the first ever contribution from Morrisons.com, our online food operation which traded for the last three weeks of the year.

Slide 6
Sales performance

Here we see the components of our LFL performance. Ex fuel sales were down by 2.8%, with sales including fuel, down by 3.6%. This reflected a fall in the number of customers visiting our stores, and a smaller basket spend. Clearly, our overall sales, which fell away in the second half of the year, were disappointing.

Dalton will update you on the plans we have to address this later.

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Slide 7
Underlying profit bridge

This slide breaks out the key drivers of the reduction in underlying profit in the year.

So, starting on the left hand side with the 2012/13 underlying number of £901m. The 53rd week accounted for £11m. There is a positive impact from new stores of £27m. This has helped to offset the effect of the negative like-for-like growth in stores of £65m. We incurred structural cost headwinds, such as payroll and energy costs, and overall these were £120m in the year. We were able to mitigate these headwinds through the continuing good progress of our self-help productivity and procurement initiatives. These, along with the benefits we're getting from the investments we've been making in our IT systems, helped us realise total benefits of £138m in the period.

The business has a very strong track record on cost control.

Across the three year period since we launched these programmes, we have consistently over delivered against our original targets, and more importantly, we now have the platform we need to further reduce the structural cost base of the business over the next few years. The final, and most significant component of the bridge is our decision to invest £85m at the gross margin level, in order to support our top line momentum.

As we've discussed before, this investment comprised two main elements.

Firstly, we invested in strengthening the communication of our brand messages, which resulted in an increase in marketing spend.

And secondly, we also invested in our base pricing.
It is clear that this investment was insufficient to drive like-for-like sales forward. This learning is the essential foundation for a significant rebasing of the value component of our proposition, which we will be accelerating over the coming months. Moving now to PBT, the largest item is the impact of non-recurring, exceptional costs.

Slide 8
Non-recurring exceptional costs

Having reviewed our business plans going forward, and the balance sheet, there are three main elements of the non-recurring exceptional costs, primarily impairments.

Firstly £163m relating to Kiddicare. This includes a provision of £57m in respect of the leases on the 10 stores we acquired from Best Buy in 2012. The balance principally relates to the write off of the Kiddicare assets, including the goodwill created on acquisition. The Company acquired Kiddicare in 2011 for two reasons.

Firstly to give us the capability to develop an “in house” food.com platform.

And then as a way to build our understanding of, and competitiveness in, what is a key customer segment for us, young families. With the completion of the arrangement with Ocado and the successful launch of Morrisons.com, Kiddicare will not provide the platform for food online. In addition, we have completed a thorough review of the Kiddicare operation. Its performance, particularly that of the Best Buy stores, has been very disappointing. It is now clear that the business is not going to deliver an adequate return and no longer has a strategic role within the Group.

We are consolidating the management of the baby category into our core business, and we will now begin a process to sell Kiddicare. In addition to the impairment, we anticipate incurring a further £20m of trading losses prior to sale.

Moving on now to property. As part of the property review, we have considered the way in which we assess new store opportunities in the core business. We have tightened our basis for appraising investments. We have increased the hurdle rate, rebased margin assumptions, and included an assessment of the ongoing impact of channel shift on our sales expectations. We have reviewed our pipeline and as a result, for the core sites that we no longer intend to build out, have booked an exceptional non-recurring charge of £319m in the year. This is made up of a provision for onerous leases of £38m, impairment and onerous commitments of provisions totaling £281m.

The final element relates to the impairment of trading stores. We have applied the same commercial rationale to that taken in the pipeline review. Specifically, we have taken a realistic assessment of the rebuild of our margin, and of our sales growth potential in future years, given the ongoing impact of channel shift. Accordingly, we have booked an impairment of £379m. I will update you on our future new space assumptions later.

Finally there are £42m of other impairments, including the £27m of online development costs we wrote off in the first half of the year. In total we have taken non-recurring exceptional costs of £903m. We believe this represents a realistic appraisal of the balance sheet.

Slide 9
PBT Bridge
The other items on the PBT bridge include our investment in new business development of £66m, which was in line with our previous guidance. We need to invest in new business development on an ongoing basis. Costs of this nature will naturally be incurred each year. As previously indicated therefore we will include them in our definition of underlying profits from 2014/15 onwards.

Other elements include property disposal profits of £9m and IAS 19 pension interest.

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Slide 10
Underlying earnings

Our calculation of underlying profit is set out here, in the usual format, albeit there are more detail lines than usual. I talked earlier about the key factors contributing to the 13% decline year on year. At an underlying EPS level this translates to a fall of 8%, which reflects the positive impact of the buyback programme completed in March, and a reduction in the statutory rate of corporation tax. From 2014/15 onwards we will adopt a new definition of underlying earnings, as flagged at our interim results in September.

Slide 11
Operating profit

We've extended this familiar slide in order to show operating profit at an underlying level, stripping out the impact of our investment in new business development, and impairments. After adjusting for all new business costs, and non-recurring exceptional charges, we saw 40 basis points of dilution year on year, driven primarily by our investment in gross margin, as I discussed earlier. Allowing for the beneficial impact of the fuel mix in the period, the margin dilution would be around 50 basis points.

Slide 12
Cash flow

Turning now to the cash flow statement. Cash flow from operations fell by £404m, which reflects the reduction in profit, and the one off charges I described earlier. We received £34m of proceeds relating to the disposal of 18 investment properties, with a related profit of £9m.

Total capex and acquisition investment in the year was £1,086m, which includes £177m relating to the completion of our arrangement with Ocado. The period also included the final tranche of £53m of our two year equity retirement programme, which concluded in March 2013.

Slide 13
Balance sheet

Before handing back to Dalton, I will highlight the key points on the balance sheet:
Pensions – in line with our stated policy we continue to have strong, well-funded schemes, with a broadly neutral position.

Our closing net debt was £2.8bn, slightly ahead of guidance but this will reduce in 2014/15, to around £2.4bn - £2.5bn.

During the year, we extended the average maturity of our debt profile with the completion of a seven year bond of 700 million in Euros, or £603m in sterling. We now have a balanced range of funding at good rates, including a revolving credit facility of £1,350m, of which £775m was undrawn at the end of the year.

And, as planned, our gearing increased. We still have relatively conservative leverage ratios, and we continue to maintain a strong cover position.

The decline in ROCE is a function of the reduced levels of profit, and the peak in our capital expenditure programme. This is a key metric for us and we are focused on delivering improved returns over the medium term.

Now, let me hand over to Dalton.

Slide 14
Dalton Philips
Thank you Trevor.

Acknowledging that we've had a difficult trading year, today is about looking forward.

We've made good progress with our strategic goals, not least to overcome our structural weaknesses in online, convenience and in our systems. In what is a structurally different market, our plan now focuses on how we drive our core business. As a value-led, multi-channel grocer, with a unique supply chain, we have a real opportunity to compete with a focused offer.

Slide 15
The grocery market is undergoing structural shifts, requiring changes to our proposition

The online and convenience channels continue to be fast-growing segments of the market. More recently, discounter growth has started to accelerate at an extraordinary pace, whilst growth in core supermarkets is stagnating. To compete in this intense market you have to tap into these growth channels. We are already responding in online and convenience.

Slide 16
We are very encouraged by our customers' reaction to our new online service

In March 2013 we told you we would launch an online food offering that was truly customer-focused and distinctive. It would have fresh food at its heart and be unmistakeably Morrisons.

We did just that. In less than 8 months from finalising the contract with Ocado, we opened our webshop to customers in Warwickshire on plan on Friday 20th December. We delivered our first orders to customers, as planned, on Friday 10th January this year. Since then we have extended our coverage to Yorkshire, and are already reaching 20% of UK households.

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Customers want great fresh products that last longer, so we've introduced a doorstep check for them to check their fresh products when they receive them.

Our 'rejection' rate is very small, at less than 0.4%. And we're already over-indexing the market in fresh sales. Deliveries should arrive when they're expected. We're consistently hitting over 95% on-time delivery and customers want to get every product they ordered.

They want low, or preferably no, substitutions. Our substitution rate since launch is a very competitive 1.5%. These are industry-leading metrics and we're only nine weeks into the journey. Even though the average customer typically only places an order once every six weeks, we've already seen more than half of them reorder.

This coming year it's all about rolling out our service to even more customers and later this year we'll be trialling an innovative 'click and collect' format. A solution that we believe resolves a key point of friction for customers, not currently addressed by any existing market offering. We'll exit this year with an annualised sales run rate in excess of £200m per year.

Slide 17
We now have over 100 M locals in our store network, and we will add up to 100 stores this year

Over 60% of our stores are in the South, expanding our footprint where we're underrepresented and we're now welcoming *over* half a million customers a week. To serve these customers, we've recruited and trained approximately 2,000 colleagues. We opened our second Convenience Distribution Centre in Bury, and now have the infrastructure in place to access 48% of the UK population. We're offering an expanded range of fresh meat and fish, all produced by our own butchers and fishmongers at our manufacturing sites and over 50% of our sales are in fresh.

As our estate has expanded, we've established standardised layouts for stores, and tailored our operating procedures. We've taken 16% off store opening costs, and cut the time to open by two weeks. There will be no let up on our growth plans this year, as we look to open up to 100 new stores. We expect to be welcoming one million customers per week, double what we see today and we'll exit the year with an annualised sales run rate in excess of £350m per year.

We've made excellent progress in capturing the growth in online and convenience, to overcome the real structural headwinds that we face, but we must now address the more recent structural change within the market.

Slide 18
Whilst we've held our own with the Big 3, we've consistently lost share to the discounters

On this chart, the top line shows our switching gains from the Big 3 throughout the calendar year. If I now take you to the line dipping in Q4, the real driver of that was in December, when we had a particularly poor Christmas. Whilst we went into Christmas feeling confident in our proposition, our rudimentary systems weren't able to match the aggressive personalised couponing from our competitors. 1 in 4 baskets in the market were completed with a coupon, up 50% year on year. This resulted in the reversal of our switching gains into switching losses to the Big 3.

We had a double whammy of being hit by vouchers from the Big 3 on one side, and Discounter pricing on the other. The bottom line shows our switching losses to the Discounters over the same time period. You'll see that these have consistently outweighed gains from the Big 3. This is obviously a huge challenge for us and it's an issue affecting all traditional grocery players.

We're all losing sales to the Discounters.

Slide 19
This is not cyclical; there has been a fundamental shift in how consumers view discounters

Consumers are no longer going to the Discounters out of necessity. Over the last two years, they have started to shop in the same way they would in a traditional supermarket. The perception of them has changed. Today, consumers are effectively using discounters and supermarkets for the same purpose... to do a full shop. We need to recognise that this is a paradigm shift.

Slide 20
The rules of the game have changed: there is a new price norm

Consumers used to measure value credentials in the context of the Big 4. Today, that is no longer the case. Given the propensity of consumers to shop in all formats, they have a new expectation of price. An expectation set by the Discounters.

This chart shows the substantial price perception gap the Discounters have versus the Big 4. Price is not the only driver of store choice, but given its significance as the number one driver, it's something that we need to face into.

The good news is, there are other key drivers where we at Morrisons do significantly differentiate, like in the quality of our fresh food and our Market St expertise. We have been building on these in recent years with our strategic plans and we now have an opportunity to really leverage them further.

I'll come on to explain this in more detail later.

Slide 21
When we narrow the price gap, customers evaluate the rest of our proposition and shop with us

We do not need to match the Discounters outright on price, because we offer so much more. We've seen that, over the past year, when the price gap increases, so does customer switching and when we come closer on price, they come back.

We need to narrow the gap to the right tipping point, where we're close enough on price that customers come to us for the additional benefits we offer. Like the unique provenance across our Market Street ranges. We have an opportunity to compete with an overall offer that others will find hard to replicate.

Slide 22
We are responding to this changing marketplace by lowering prices and reinforcing our proposition

We will be bold in the value we offer. We will significantly invest in our pricing to narrow the gap. We'll support our pricing with a smarter, tighter and stronger promotional programme and across the other five store drivers, we will continue to build on our strengths to offer an improved proposition. We'll make our stores even easier to shop. We'll continue to offer great quality fresh food. We will simplify our overall range, focused on the products customers want most, and offer a competitive Own Brand. We'll build on the success of Fresh Formats, looking for new ways to make our stores even more interesting and pleasant places to shop.

In addition, we're launching our Morrisons card, to get to know our customers much better, on a 121 basis and offer them personalised value and we'll communicate all of what we offer more clearly and consistently. Combining our strengths of fresh and service... with highly competitive prices, we can have a winning proposition. To do all of this, we must further change how we operate.

Slide 23
We have a proven track record in achieving aggressive savings targets over the last three years.

In that period we delivered over £300m. This includes over £100m through store productivity initiatives. Our Evolve IT re-platforming delivered a further £100m and we delivered over £100m through tackling indirect procurement. We are well placed to attack our current cost base and bring it in line with industry norms. We will not become a Discounter. We will carve out a clear position as a value-led grocer focused on fresh food, with friendly service.

Slide 24
We've identified where we can generate £1bn over the next three years to strengthen our business

Let me talk you through the three major sources.

The first of these is improving our end-to-end operations. We will save approximately £300m over the next 3 years by being smarter and simpler in how we operate.

The second of these is indirect procurement and loss prevention to save a further £200m.

And finally, an additional £500m will be generated by our commercial investment choices.

We will focus our promotional investment appropriately and reduce our sourcing costs. We'll come back in September with the key metrics against all of these initiatives, so that you can see the detail of our progress. Now let me take you through the £1bn in more detail.

Slide 25
We will use our uniquely vertically integrated business model to optimise what we make where

As Britain's second largest fresh food manufacturer, we've invested over £200m during the past three years in expanding, and modernising, our manufacturing capability. We now operate across 18 sites, producing 60% of the fresh food we sell. This capability is really coming into its own. It's fundamental to both our growth in online and convenience, and to change our proposition in stores. We can now leverage our manufacturing capability to optimise what we make where. Let me give you an example.

We historically used our fishmongers in store to pin-bone salmon. This was a time intensive process, carried out away from the counter. By moving this to an automated process at Grimsby, we not only improved salmon yield we also freed up time for our fishmongers to focus on added-value tasks for the customer at the counter. We can now move more tasks upstream which customers don't value when they are conducted in a store environment; allowing our skilled craftspeople the time to focus on serving the customer.

Slide 26
We will further enhance our end-to-end product flow and processes

Making use of the new systems we've been putting in place, to fundamentally shift how we order and flow stock. In the short term, we'll introduce simple changes to our electronic order pads. But by 2017, we'll be using sales based ordering; centralising our demand forecasting and order replenishment to increase accuracy and availability, unlocking efficiency benefits across the entire supply chain. Selected, high volume lines will be moved to become stockless, improving product flow. Stock will be increasingly centralised, moving from regional into national distribution centres, to create a single point of delivery for suppliers and with our new systems we will change how we operate in store.

We will introduce dynamic allocation of hours to reflect the changes in trading patterns throughout the day, in place of manual scheduling and new technology on our checkouts will make them easier and quicker to use, simpler for the operator, and significantly better for our customers.

Slide 27
We will realise further savings across indirect procurement and loss prevention.

With our centralised team now in place, we have a clear line of sight to unlock a further £100m across indirect procurement in the coming 3 years.

We are also targeting loss prevention. Retail shrink, waste and markdown, cost us around £450m. We can now use system enabled performance tracking to identify areas of greatest opportunity. We'll be focusing initially on our high risk product categories, increasing the level of product protection used. In our spirits category, for example, this will prevent over 100,000 bottles from being stolen each year. Altogether this creates another £100m saving over the next 3 years.

Slide 28
We will focus our promotional investment and reduce our sourcing cost

rebalancing our commercial investments to generate a further £500m of opportunity.

We currently spend some £1.5billion pounds every year on promotions. New systems-enabled promotional tools will direct our investment to where it has the biggest impact and we can work with our supplier partners to get the appropriate funding for all components of our value strategy. We will cut the tail of promotions that don't offer incremental benefit, and remove duplicative deals. Overall, we'll reduce promotions by 10% this year.

We will also reduce our sourcing costs. By simplifying our range by ~20% over the next three years, our volumes will be concentrated over fewer SKUs, helping us get the best prices from our suppliers. It will also make it easier for customers to shop the products they want, and buy, most often.

For every product group reviewed so far, 10% of SKUs have been taken out. As you know this a combination of art and science. It's extremely complicated. Casper's experience from Ahold is proving invaluable and this programme also extends into Own Brand. We'll use our dedicated Own Brand sourcing team to work directly with our suppliers, optimising price and quality across our range. We've already started through re-sourcing efforts in our tuna; we were able to cut 17% off the cost base without compromising quality or sourcing principles.

We'll also work with our key branded suppliers via our M Partners programme, to drive improved category management throughout the year, with short term and longer term strategic plans.

Slide 29
We will use the £1bn to strengthen our business over the next three years

The first, and major use is investment in our core proposition. We will reinforce our position as a value-led fresh food grocer. I will take you through the detail of this in a moment.

Secondly, we will use some of the £1bn we generate to offset our annual structural cost headwinds.

And thirdly, we will use it to support earnings growth.

Trevor will touch on these latter two later in the presentation.

Slide 30
We will lower more prices on a permanent basis

Continuous, incremental repositioning of price is now not enough. Our customers want great value for money. We need to be distinctive. We will be making significant investment in lowering our prices permanently. We will narrow the gap.

We've already started with our core fresh Market Street categories. We are leveraging our manufacturing to significantly cut prices on key produce lines. Since we started this investment four weeks ago, we've seen strong volume uplifts in these products. We're selling almost five times the number of peppers since we lowered the price from £1.75 to 99p. We're also investing in meat and poultry. Our Chicken Breast Fillets, at only 2 for £7.50, are the cheapest in the market, with sales up 37%.

Alongside our investment in fresh, we're driving down prices on hundreds of core grocery lines. The products our customers buy week in, week out and we'll keep those prices consistent, with fewer price changes. This is just the start of the journey.

Slide 31
We will offer fewer, and more impactful promotions.

Promotions are important for our customers. We will have a smarter, more compelling promotional package. We're cutting the duplicative promotions that cause customer confusion. We'll put that investment into fewer, deeper promotions that create excitement and drive footfall. The right product, with the right mechanic, at the right time for our customers. Offers like Persil and Princes Tuna, both better than half price and just yesterday, we launched our latest offer "Buy two Easter eggs for £1.50" offer. With our manufacturing capability, we've stunning deals across all our fresh departments. All part of a single, coordinated trade plan which brings the best of our Market Street and branded promotions together.

Slide 32
We will make Own Brand a competitive advantage by simplifying the range and improving value

Our value proposition extends beyond price and promotions. For customers to reappraise our offer, we also need to focus on our Own Brand. Three years ago, we had own label products that weren't credible in the market. Today, we've 10,000 re-launched SKUs and our Own Brand participation has grown nearly 200bps to 48.8%. But, as customers' perception of value has evolved, so too have their expectations of Own Brand ranges.

We will be investing aggressively to leverage our Own Brand asset. We will reduce complexity and remove duplication, creating a brand hierarchy better suited to customer expectations. We will reengineer our price/value equation, resulting in an Own Brand that is significantly more competitive in the new market conditions.

Slide 33
We'll continue to improve product quality, and make our stores even easier, more pleasant places to shop

Our fresh food is a key strength of this business. We will continue to invest in it as a point of difference. Further investment in our chill chain, combined with the improvements to product flow and range reductions, will drive higher volumes, leading to even better availability, longer shelf life, and better quality and our store environment is a fundamental point of difference for us too.

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In our Fresh Formats stores we've taken down the walls, removed the barriers, and dramatically increased the visibility of our fresh food proposition. There are, however, areas where we can do more. Areas that matter a lot to our customers. We will remove unnecessary aisle clutter. We'll review product adjacencies so items are easier to find and we'll further invest in customer facilities, making our stores easier, nicer places to shop.

Slide 34
We will launch our Morrisons card, this year

We currently don't know our customers well enough. This lack of knowledge, combined with very limited systems capability, has made it much harder for us to compete. We felt the effects over Christmas, with the intensification of personalised vouchering. We do, however, already have a loyalty scheme, Morrisons Miles, which rewards five million customers who buy our fuel. A huge number, however the problem is, we don't know who those individual customers are. We're turning that problem into an opportunity, starting with registering our Morrisons Miles customers this quarter.

The bigger opportunity lies in the 12m customers who shop with us in store. Getting to know them as individuals – who they are and what they want – will enable us to serve them a lot better. We've spent the last year developing the technology platform. This year, we're launching our Morrisons card. In the same way we did with food online, we have examined solutions worldwide. We have learnt lessons from the best in class through to the high fixed-cost programmes and we will be running trials over the coming months. Clearly, for commercial reasons, I can't talk to you about the scheme in detail yet, but we are very close – it will be unique to the market, customer-focused and distinctively Morrisons.

Slide 35
We will deliver focused and consistent communication so our customers know what we stand for and reappraise us.

This year our tactical marketing will focus on our lower prices and winning promotions. We'll link that communication to our brand advertising to highlight what we offer. Fantastic value, supported by unrivalled service and skill in making and selling great quality fresh food. Food where we can guarantee the provenance because we make it. As we become a true multi-channel retailer, we'll continue to adapt our communication approach.

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Slide 36
This is the right proposition for our business and for our customers in this new market

We are a supermarket that has always been built on the strengths of value, fresh and service. Today we're showing boldness in our ability to adapt to this changing market. We're drawing on those strengths and leveraging them in a way that will encourage our customers to reappraise what we offer. We are a value-led grocer. We will be a different kind of supermarket, built on the traditional strengths of Morrisons. Not a discounter, not a hypermarket, a value-led grocer, with fresh, great quality food, where you can do your full shop with ease. Offering value without compromise.

Now let me hand you back to Trevor

Slide 37
Trevor Strain
Thanks Dalton.

Dalton has set out our opportunities and the plans we have to reshape our cost base. In this section I want to set out our approach to cash and capital. I will update you on how we will step change the Group's sustainable free cash flow, and how we will drive the capital intensity of the business, specifically:

- our plans to reduce capex
- the improvements we will deliver in working capital
- the outcome of our property review
- cashflow guidance for 2014/15

I will then bring this all together with the plans Dalton has set out to reduce costs and invest in our proposition, into a consolidated view of our guidance for the coming year.

Slide 38
Financial objectives and principles
First though, in September we set out our financial objectives and principles.

We reaffirmed our commitment to the conservative principles that have long underpinned this company – and you can see these on the slide.

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Slide 39
Reducing capex

As previously discussed, with our investment in IT platforms behind us, online food now trading, and a firm brake on new space investment, 2013/14 was our peak year for capital expenditure. As a result of this, and in line with our commitment to capital discipline, we will more than halve our future capex investment. In 2014/15 we expect it to be circa £550m after which it will fall to around £400m per annum. We have reduced our previous guidance of £850m for 2014/15, by circa £300m. We've done this by removing planned new core space purchases, and by maintaining a strong capital discipline.

Looking now at our space guidance going forwards, in relation to core supermarkets we expect to open 330,000 sq ft in 2014/15, all of which is sites already in the process of being built. In 2015/16, we will build out the remaining 300,000 square feet of the pipeline. Beyond that, we will only acquire new supermarket sites in exceptional circumstances. In convenience we will add about 250,000 square feet annually.

Over and above capital expenditure, we expect to incur a cash outflow of c100m in 2014/15, relating to the exit of some of the onerous capital commitments, following our review of the new space pipeline.

Slide 40
Working Capital

In September we indicated that we could see major opportunities to improve working capital in the group, leveraging the significant improvements we have made in our technology platform in recent years.

As example to illustrate the opportunities, first, looking at our depot stock position.

At the year end we had over 14 days of stock, which is actually a small improvement over last year. But that's still about five days above the "industry average". The programme Dalton set out will help us reduce this "gap" significantly.

Looking next at payment terms. The distribution curve at the bottom of the chart shows the range of payment terms the business has historically run with, and the simplification opportunity that gives us. We are launching a supply chain finance initiative, which we expect to deliver a "win win" for both us, and those of our suppliers who choose to participate. Dalton has already set out how we will reshape our operating model end-to-end. That, combined with new technology and the work we are doing to reduce our range, gives us significant opportunities to improve our inventory management.

Overall, we expect to improve working capital by £600m over the three years, with £200m being generated in 2014/15.

Slide 41
Property review
The third area of opportunity we flagged in September, was a review of our property.

We have opportunities to realise value, in a disciplined way, consistent with the Company's conservative approach to capital structure. At the time, we gave a clear commitment to maintain an overwhelmingly freehold position. We firmly believe that freehold ownership at both a company, and at an individual asset level, provides a high degree of insulation, particularly at times of structural change in the industry. It also gives us a high degree of operational flexibility.

We indicated then that we do not foresee the freehold percentage of our core estate falling below 80%, by far the highest ratio in the sector. That commitment has not changed today. However, having reviewed the portfolio in depth we believe that we have opportunities to monetise value from certain parts of the estate, specifically:

- our development assets
- some of our newer distribution assets
- our investment properties, and in a small number of cases where it makes sense to do so, the associated stores

In the current market we would expect to generate proceeds of circa £1bn over the next three years, with between £4-500m in 2014/15. Beyond that, we will provide further specific guidance at the start of each financial year. Monetising value from non-core assets, whilst maintaining the benefits of an overwhelmingly freehold estate, in a time of change for consumers, and the sector, is the right approach for us to adopt.

Slide 42
Free cash flow
I will now consolidate these opportunities into a view of the Group cashflow for 2014/15.

In the last financial year, net debt increased by £600m. In 2014/15, and despite the reset of our earnings expectations for the year, we expect an improvement in our cash flow of around £1bn when compared to the previous year. This is driven by significant reductions in capital expenditure, an improvement in working capital, and by property disposals.

In all we will generate some £6-700million of free cash flow before dividends, which will enable us to reduce net debt by £3-400million in the year and we expect to deliver not less than £2billion of free cash flow over the next three years.

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Slide 43
Dividend

2013/14 was the final year of our 10% dividend underpin.

In September we set out our commitment to a progressive dividend policy, moving towards two times cover over time. We recognise the importance of the dividend to our shareholders. In the light of the business' strong cash generation opportunities, the Board has confirmed its commitment to a progressive dividend. In 2014/15 this will not be less than 13.65p, a 5% growth underpin.

Slide 44
Summary

To put this in the context of the capital allocation framework we set out in September.

- 2014/15 will be a year in which we find the self-help within our business to invest in our proposition
- We will reduce capex to £550m
- We are committed to the principle of a strong investment grade credit rating.

In the coming year, we will use the positive cash flow we generate to reduce our debt levels

- We will maintain a progressive dividend policy with a 5% underpin in 2014/15.

With reduced levels of capital investment, further property disposals and improvements in working capital to come, we will generate significant levels of sustainable free cash flow from operations. This will enable us to reduce our debt and then, at the appropriate time, return surplus capital to shareholders. The timing of that return will be kept under review.

Slide 45
2014/15 guidance

This slide sets out our headline guidance for 2014/15. Further details are in the back of your packs.

Building from our 2013/14 underlying profit of £785m. We will invest £300m in our overall proposition. We will have to absorb around £200m of structural cost and trading headwinds and offset this by £200m of self-help as Dalton set out earlier. We therefore expect our core profits to be in the range of £460m to £510m. New business development costs will be £65m, in line with current year and we will also incur around £70m of "one off" costs, relating to ongoing losses in Kiddicare pre sale, the launch of our loyalty programme and some restructuring costs. We will report these costs within underlying profit. Overall we expect underlying profits to be in the range of £325m - £375m.

And so, looking forward, In 2015, we expect NO one-off costs and a reduction in our new business development costs.

Over the next two years we have £800m of self-help which we will use to:

- Invest in the proposition
- Mitigate structural cost increases
- And grow earnings

We have a strong balance sheet,
We are focused on costs and cash,
We will maintain a strong capital discipline.

Thank you and now let me hand you back to Dalton to summarise how this whole plan comes together.

Slide 46
Dalton Philips

Thank you Trevor

Slide 47
In summary

Despite the huge progress we made in our systems platform and new channel development, last year saw disappointing performance out of our core stores. There has been a structural change in the market place and today we are addressing that.

1. We're absolutely focused on making our core supermarkets prosper. That means a substantial investment in our proposition.
2. We've two great formats in online and convenience and we're committed to growing them aggressively.
3. To support these three formats, we are removing all non-core distractions.
4. In addition, we've found meaningful ways to strengthen our financial position, through working capital improvements, reducing our capital expenditure, and maximising value from our property portfolio.
5. This is all designed to put us on the right footing to compete, and grow, in this challenging market.

This is a bold and decisive plan, that will make Morrisons truly fit for the future. Now, let me open it up to your questions.

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