Richard Pennycook
Group Finance Director

Good morning ladies and gentlemen. This morning we are pleased to be reporting a solid set of interim results. We continue to deliver on our promises, in a marketplace which is more difficult by the day. Our focus remains on delivering our 2010 Plan and making Morrisons the Food Specialist for Everyone. Inevitably, in the short term, we are having to adapt to the changed economic circumstances that have put great financial pressures on our customers and great pressures on our costs. Marc will talk later about how our value credentials are now very much to the fore.

The numbers themselves are pretty straightforward this time, and really the only complication is that we are reporting a 26 week interim period whereas last year it was 25. To help you with your models, there are full sets of prior year P&L's, balance sheets and cash flows on a 25 and 26 week basis on the web. All the numbers I present this morning will be after restating the prior year to a 26 week period.

Slide 4 – Financial summary

In today's economic circumstances, the picture painted in this slide is about as good as one could hope for:

- Top line growth over 13%,
- Profits up in line with this,
- Operating margins improved and
- A strengthened balance sheet...

... all signs of a business very much on the right course.

Two years ago, when we were recovering our profitability strongly, I made clear that we had an economic tailwind helping us along. Today, of course, it is a pretty strong headwind.

Slide 5 – Turnover bridge

This chart, I think, helps to show both the strength of our performance and the battering being taken by the consumer. £73m of sales from new stores was pleasing, showing that we are growing our estate again, and of course the £389m of like for like store sales, equating to 7.6% growth, was a highlight of these results. The £308m of fuel price inflation, however, provided us with no meaningful profit contribution – it was cash straight out of our customers' pockets and on to the oil companies and sovereign wealth funds. So whilst it contributed 4.9% of sales growth for us, it did little for our bottom line.

Slide 6 – Underlying earnings

Last year we introduced a measure of underlying earnings, in order to eliminate one off gains, the oddities of pensions accounting and to smooth out fluctuations in the tax rate. This chart lays out the calculation for the half year.

As we previously indicated, property gains have reduced significantly – the number of surplus properties carried forward from the Safeway acquisition is now very small.

Our normalised tax rate benefits from the 2% reduction in Corporation Tax rates this year.

Hence our underlying growth in earnings per share of 22% is well ahead of both the statutory PBT growth of 13% and underlying profits growth of 18%.

Slide 7 – Operating profits

I mentioned previously that operating margin had grown, and this chart breaks out the 20 basis point improvement. Our gross profit margin was flat year on year. But bear in mind that the strong rise in fuel sales, which I addressed a few moments ago, had a "drag" effect on our margin. We calculate this to be 40 basis points, at both the gross profit and operating profit lines.

You also need to bear in mind that in the prior year we took accelerated depreciation on our old brand assets, and you can see the effect of this in a reduced depreciation charge this year. I estimate that this accounted for approximately 15 basis points of gross profit margin improvement this time.

Allowing for the net of these two effects, our underlying gross profit margin was up by approximately 25 basis points half on half, reflecting continued delivery of our Optimisation Plan targets. This was after a strong headwind with respect to energy costs, which were up £19m half on half. We expect this trend to accelerate in the second half as forward cover rolls off. We will offset these costs with savings elsewhere – but undoubtedly our earnings upside is limited for this year whilst these high energy costs persist.

Our administrative expenses were up by 6% year on year, and the biggest component of this was marketing costs. If you recall, in the first half last year we flagged that our marketing was unusually low, as we had not re-launched the brand. This year, our marketing costs are spread more normally through the year.

Slide 8 – Operating profit notes

I'm conscious that there are a number of moving parts in the operating profit performance, so this slide is just a reminder of the key components:

- The fuel mix effect, which diluted gross profit percentage by approximately 40 bps.
- Accelerated depreciation last year, which flatters this year's performance by circa 15 bps.
- Energy costs up £19m this time

Slide 9 – Balance Sheet

If I turn now to the balance sheet, there are a few points to note here:

On fixed assets, given the state of the commercial property markets I want just to remind you how our asset values are carried. The values of original Morrisons stores are stated at depreciated historic costs – we do have, for example, some large superstores stated in the books at £250,000. They are therefore highly prudent. The ex Safeway stores are stated at values attributed at the time of the acquisition in 2004. Thus they are pretty current, but were certainly not valued at the absolute top of the market.

You will notice that there is no pensions deficit at the half year. This reflects the previously announced injection of a further £100m into our defined benefits schemes. Despite the current turmoil in the equity and bond markets, we are confident that we have taken the right, prudent actions to deal with the long term funding requirements of our schemes. Our pensions funding assumptions are amongst the most prudent in the FTSE.

Net debt, and therefore gearing, continued to decrease in the half, to £458m. Because of our bonds in issue, of £760m, this in fact meant that we continue to deposit substantial sums of money in the short term banking markets. [We are frequently depositing between £300m and £400m a night into the markets, and as you can imagine we evaluate the creditworthiness of our counterparties carefully.]

Slide 10 – shareholder returns

We announced our balance sheet strategy in March, and this will carry us through to 2010. As a reminder, I've set out our balance sheet principles in the supporting slides on the web.

Our strategy includes a strong dividend policy of targeting progressive dividend growth in the coming two years, over and above earnings growth, in order to bring dividend cover to a level in line with the rest of our sector.

At this interim stage, we have increased the dividend by 18.5%, following last year's increase of 20%. This gives a level of dividend cover of 3 times at consensus earnings for the full year. We will review the level of cover at the finals stage.

A second feature of our balance sheet strategy was the return of surplus capital to shareholders. As previously indicated we plan to return £1bn to shareholders during 2008 and 2009.

Slide 11 – Cash flow

The half saw another period of strong cash generation, leading to a reduction in net debt of £24m. Cash from operations was up 6% to £521m, despite the additional pensions funding of £100m, reflecting good control of working capital.

Disposal proceeds and tax receipts arising from prior years were both down substantially, as expected.

Capital expenditure was up year on year, at £238m, reflecting the activity being undertaken in relation to phase 2 of the Optimisation Plan. You will recall that this phase of the programme has additional capital investment, over and above our normal run-rate. In the half, we invested £50m in relation to the Optimisation Plan, as well as £188m for normal capex.

Our expectation for the full year is for total capex of around £600m, of which £200m will be Optimisation Plan investment.

I would expect our second half cash inflow before buyback to be around £200m

Now let me hand you over to Marc for the operational review.

<u>Marc Bolland</u>
<u>CEO</u>

Slide 12 -

Thank you Richard.

Good morning ladies and gentlemen. Let me first give you some background on the market, a topic we've been hearing a lot about in recent weeks. A background of inflation in particular, is what everybody's talking and thinking about, so let me first give you an overview of what we see.

Slide 13 – Market background

In the first half of the year, the period we're reporting on, we saw significant commodity inflation year-on-year, but also at the same time strong fluctuations in the market. So if you look at the chart here for example, it highlights different commodity price changes year-on-year to July.

However there have also been strong fluctuations. For example take the example of wheat, it is up here year on year by 23% but when you look at it over the year, there has been times when it was up over 100%.

Slide 14 – Market background

More recent developments, as an example the oil price reducing, will have a wide reaching impact. If you consider the effect of commodities, take fertilizers as an example, it will be impacted by the oil price but with a time lag of something like six months.

The declining pound however, which we've seen recently, will offset some of these oil price benefits.

Slide 15 – Market background

In the coming six months we see an easing of commodity pricing due to two important factors. One is an increase in acreage devoted to commodity production of roughly 3% worldwide. Even here in the UK the commodity acreage has increased. Secondly this season we have better harvests.

Taking the example of wheat again. Wheat this year has had a very good crop in Australia, a very good crop in the Ukraine and a good crop in Northern America. But for the longer term, the outlook remains that stock levels are very low. Where stock levels on wheat traditionally were always 120 days, they're now at 60 days.

This actually means, therefore that crop harvests will become more important over the coming years, I'm not just referring to the second half of this year because as I've said we have a positive outlook on the current global wheat harvest, but when we look at the years ahead, the surplus that we see being produced this year is not enough to build up stocks back to the required 120 days. So the market will stay volatile over the short term.

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Slide 16 – Market background

Looking now at inflation, there's a number of different measures we can consider as a grocery retailer. One of our most important benchmarks is the TNS grocery inflation which measures our industry. If we look at TNS grocery inflation over the last 24 weeks to August 10, (so effectively our first half year), it's 6%.

If we compare that with Morrisons own measured inflation figure, where we are actually managing our inflation down in store, it's a slightly different picture.
As I shared with you, during our call ahead of our AGM in June, we are re-investing in prices. So, we see inflation is at a lower level than TNS.

In addition we expect inflation to ease off over the winter due to commodity influences and annualisation. As I indicated there is always a time lag in terms of changes to worldwide commodity price changes coming through the supply chain, but as we see commodity influences coming through in December/January, and at the same time annualisation kicks in, we'll see an easing off of the rate of inflation.

Slide 17 – Background – consumer confidence

Consumer confidence however is at the lowest ever recorded. It's 4 points lower now than March 1990, just ahead of the last recession, and that was an historic low. Recently conducted consumer research confirms research previously carried out in the early 90's about the key things which consumers are most likely to doing recessionary times. Consumers indicate that one of the first things they cut back on is dining out, and they will as a consequence therefore dine more at home. The second thing is there will be less discretionary spend on non-food.

Slide 18 – Consumer shopping trends

Take a look at this chart, and I think it's an important chart on consumer behavior, so let me take some time to take you through it. Let's look at what is happening at store level in our industry. The chart shows the growth percentage level on the vertical axis over the last seven months. The value own label is the red line, premium own label is the green one, standard own label in the blue one, and branded products are in yellow. What you see is the growth trend. They are all still growing but the strongest gain is in value products.

Now we know value products come from a lower base, because in all food retailers it's only a small proportion of the business, but they are growing fast.

There's growth as well in standard own label rising from 4% to roughly 8%.
We see branded growth is about level and we see a decline in premium own label down from a growth rate of 10% to 2% recently.

Slide 19 – Consumer shopping trends

So we see clearly the first effects of the down trading in stores and in the retail industry in the UK.

What is the trend at Morrisons?

At Morrisons our trend is broadly in line with the market. The exception is that brands are holding up more strongly at Morrisons since we use them more prominently in our promotional package.
And we will continue to use them in the promotional package.
Brands are strong for us. Brands are still being supported; therefore we envisage brand performance will remain at a level somewhat stronger than the average in the market.

So, down trading in store is now evident. But we also see a trend that customers are switching retailers in search of value. So you have two industry down trading effects; one in store and one between stores. So clearly consumers are managing their own inflation to a certain extent.

Slide 20 – Morrisons brand values

Now if we go back to Morrisons, I shared with you 18 months ago the three clear distinct values our business is about. Morrisons is about fresh, it's about value, and it's about service.

Our distinctive vision has been recognised by consumers. 63% of all shoppers believe that we prepare more food fresh in store than any other supermarket, so our message is getting through to the consumer.

Shoppers say on value that Morrisons leads the industry for great promotions. The value credential is again coming through very strongly.

Service and food skills are a part of the DNA of Morrisons, so that's the thing we are not touching. Not just service but also food skills are something that we want to be famous for.

But the brand values of Fresh and Value give us the opportunity to fine tune our proposition. Internally I say we have two buttons. If the economy had strengthened we could have played the Fresh button much more strongly. For example we could have added a few thousand additional fresh premium lines. A sophisticated environment matched with sophisticated lines.

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If however the economy weakens, and it clearly has, we can play the Value button stronger and we will, as we are doing, bring more value items in store. It doesn't mean that we don't regard our fresh credentials as being strong, because we still play that button and I'll show you that in a second. We don't have or want a dashboard of 25 buttons, there's two of them and therefore it allows us to react very quickly to market circumstances.

Slide 21 – Value – what we are doing

This slide allows me to tell you what we're doing on Value, I'll talk about price cuts, I'll talk about promotions, I'll talk about value and I'll talk about tertiary brands.

Value remains at the heart of what we do, so we are, as I said earlier, reinvesting in price and value. We're making another 4,000 price cuts in September, 2,000 price cuts last week, the remaining 2000 over the next week or so, so overall 4,000 price cuts this month. This follows the 4,000 price cuts during June and July. So are we aggressive on price, are we sharp on price, and are we meeting the tightening belts of the consumers? Yes we are!

Next, promotions with great, £4. fresh food deals. We started them over the summer and ran them, every second week. Past examples have been a full barbeque or a full lunch, a full picnic, and more recently a full lunch package for the children to take to school for £4. We can do this because we have the supply chain. We were able to react very quickly and produce the strongest family food offers in this country over the summer.

Next we have re-branded and extended our Value range. This was part to program we started a year ago; we had Bettabuy which we re-branded Morrisons Value. And now we are further extending these ranges.

Finally, we are also growing our tertiary brands produced by our own manufacturing capabilities. So in addition to the great £4 promotions we are able to use our own supply chain to put more emphasis on tertiary brands. Let me give you two examples. We produce bread under the tertiary brand name, Newtown and we sell 0.5 million units per week. It's a brand that wouldn't ring bells with you but it's a very, very, strong offer.

On bacon, we have Fresh Choice of which we sold 800,000 units in the last few weeks. So we have tertiary brands that in contrast to others are produced through our own supply chain.

We are therefore well positioned in value for the future.

Slide 22 – Fresh – what we are doing

Looking now at Fresh. The underlying consumer requirements remain.
Fresh will still be important; health will still be important in the country, and we are seeing that our Fresh participation is up 10% in value terms. So whilst we are bringing the customer these very strong deals at strong prices, at the same time our Fresh offer is growing 10%.

We have strong deals for those dining at home, for example on salmon and on beef, playing to that opportunity that we see from the consumer research. We are also focusing our product development work on alternatives for people who want to dine more at home.

So on fresh Morrisons is also well positioned for the future.

Slide 23 – Recent sales performance

Now let's move to the numbers. As Richard said, there are two sets of prior year numbers available to you in your packs. This is the 26 week view. It shows 2.7% growth LFL growth, ex fuel, in H1 07/08..

Slide 24 – Recent sales performance

Then as we reported to you at the AGM. quarter one growth was 7%.

Slide 25 – Recent sales performance

In the second quarter we show our very strong sales continuing at 8.2%.

Slide 26 – Recent sales performance

It adds up to first half sales of 7.6%, this continues the growth seen since September last year.

Performance was particularly good in Scotland and in the South, as we reported last time. The interesting thing for you is that it has been very strong in London, where we have 22 stores. So for us that's very encouraging.

Slide 27 – Customer footfall

As I told you in March, increasing customer numbers is key to our growth, I'll take you through that again to be consistent with our last presentation. We have 0.5 million additional customers still coming through our door. These new customers are not just buying promotions. Our promotional growth compared to our competitors in the market is in fact lower; we are getting our growth from full baskets. So that is for us again very encouraging.

These new customers are spending as much as existing ones. We're gaining them across the whole country, and the latest data shows that the gains are from all our competitors. In general these new customers have a younger profile and there are more families.

But what is interesting in terms of the numbers and in terms of the publicity everybody gets, is net switching gains; in fact Morrisons net switching gains are larger than the gains of the total discount segment. So while they always hit the news, we're pleased with our progress.

Let's now go through to the Optimisation Plan.

Slide 28 – Optimisation Plan update

<u>Store refresh program</u>
Last time I shared with you we wanted the Refresh programme to be completed by July, and we did it. 370 stores and 286 forecourts are now totally re-branded, refreshed.

<u>New space</u>
We're on track to deliver 1 million square feet over three years.

<u>Manufacturing</u>
We opened our Spalding abattoir which allows us to process in-house all British meat that we buy and send to store. So we have the traceability capability and a provenance that nobody has in this country.

Slide 29 – Optimisation Plan update

<u>Distribution</u>
Sittingbourne. I said last time that we were starting with Sittingbourne and it's progressing well and on track to be opened in the first half of 2010. Previously I mentioned that it would be on stream on 2010, I'm now confirming that it will be the first half of 2010.

<u>CSR</u>
We have achieved a carbon reduction of 25%, so a very positive step and carrier bag usage is down 22%, where in the past we were not very famous for our environmental steps, and haven't talked much about it. We are doing well and quietly getting on with it!

<u>IT systems</u>
Our integration partner is selected and the first planned launch will be the new payroll and HR system at the end of this year.

In March I'll give you a further update on the other items of the 2010 program and the Optimisation Plan.

Slide 30 - Summary

Finally in summary, we have strong like-for-likes that we have seen over the last half year. Underlying profits are up 18.5%. We have a very healthy cash flow and all the programs are on track.

Moving to the outlook. The second half of the year is going to be highly competitive but the first half year profit performance gives us confidence that we will deliver our profit expectations for the year. Thank you.