Preliminary Results 11 March 2010

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Slide 2 - Sir Ian Gibson, Chairman

Good morning everyone and welcome to our preliminary results announcement for the year ended 31st January 2010.

Slide 3 – Overview 2009/10

I'm delighted to report that in a difficult period for the UK economy and for the consumer, Morrisons has had another good year, with market beating sales growth, a 19% rise in Underlying Profits to £767m and, in line with our policy of reducing dividend cover to sector average, a 41% increase in the dividend. Once again our focus on fresh food and great value resonated with shoppers everywhere and ensured we welcomed more customers through our doors than ever before as we continued on our journey to take the business from National to Nationwide.

These results are testament to all our people who enabled us to establish another set of Morrisons records. But this year I'd also like to thank the senior team for their focus and commitment through a period of CEO transition; you've met some of them before, and I'll ask them to stand as I can thank them on behalf of the board and shareholders for a successful year.

Concluding that transition you know we appointed Dalton Philips as new CEO and he takes over at the end of this month.

During the year, of course, Marc Bolland left us and we thank him for his contribution and leadership through a key phase of Morrisons development and wish him well in his new role - As part of our board succession planning, there were also some changes in our Non-Executive ranks. Susan Murray retired in December and I'd like to thank her for her contribution to the business over the past four years. Penny Hughes and Johanna Waterous joined us earlier this year. Both bring a wealth of experience and I'm pleased to welcome them to the Board.

As usual our colleagues and customers have given generously of their time and money to support charitable causes this year with over £2.5m being raised for Children in Need, the Haiti earthquake appeal and our charity of the year, Cancer Research. I thank them for their continuing generosity.

Looking ahead, we expect the economic environment to remain challenging, with disposable incomes under pressure and value remaining a high priority for consumers. Against this background, Morrisons unique offer of high quality, fresh food at great value prices puts us in a strong position to continue to win customers from our competitors and drive further growth in market share. I'd now like to hand over to Richard who will take you through the results and our plans for the future in more detail.

Slide 4 – Richard Pennycook, Group Finance Director

Thanks Ian. Good morning ladies and gentlemen.

Slide 5 - Review

This morning I am presenting both the financial and operational reviews, and I will do it in the usual order – so financials first, followed by the operational highlights under the key headings shown here….

Slide 6 – Results

… and so turning to the results….

Slide 7 – Financial summary

2009 was a vintage year for Morrisons. We strongly outgrew the market for the second successive year, whilst investing for future growth and delivering a significant profits upgrade.

Turnover was up 6%, despite a large negative fuel impact which I will break out in a moment. We were delighted with our operating profit growth of 21% to £812m.

Net debt increased as anticipated, because we invested in 45 new stores and a new RDC in the year.

Slide 8 – Sales performance

Turning to the detail, and starting with the top line, you can see here the split of the 6% like for like sales increase between customer numbers, up 2.3%, and spending growth per customer which rose 3.7% to just above £23. We saw an average of 10.5m customers per week in the year, an increase of 1.3m since we relaunched the brand in 2007.

Slide 9 – Turnover Bridge

As usual, we break out here the component parts of the turnover growth in the year. This has taken on a new shape for us. The key element remained the like for like store sales growth of 6% -

contributing £686m of sales to the business. But new space also contributed £359m, accounting for 2.5% of our total sales growth. The biggest element of this, of course, was the 34 Co-Op and Somerfield stores opened approximately mid-year – they delivered £230m of sales in the year.

Fuel once again had a significant impact – average pump prices were around 5% lower than the previous year resulting in the price related decline of £143m. Volumes were also marginally down, reflecting the recessionary impact of people driving less.

Slide 10 - Underlying Profit

Underlying profit was up by 21%, with only very small adjustments this time for property profits and pension scheme returns. The major adjusting item was the exceptional pensions credit of £91m which we dealt with fully at the interim stage, so I don't propose to repeat any of the detail here.

With a normal tax charge, underlying basic earnings per share were up 23% to 20.5p. The dividend was up 41% with dividend cover of 2.5 times. This fulfilled our commitment made in 2007 to bring our dividend cover in line with the European grocery sector average by January 2010.

Slide 11 – Operating Profit

Operating profits grew by 21% to £812m, equivalent to 5.3% of sales. This percentage is slightly ahead of the level we anticipated when we first launched the Optimisation Plan, reflecting both over-performance of individual Plan elements and the operational leverage benefits of the strong volume growth we've delivered.

The gross profit increase to 6.9% of sales reflects this leverage, but the year on year increase of 60 basis points is also flattered by approximately 30 basis points reflecting the mix effect of fuel.

Administrative expenses were up 12%, well below the level of profit growth as one would expect. Our marketing activity increased, but was offset by reductions in the cost of advertising in the marketplace. Also included in this line are the LTIP costs from the maturity of the Group's first LTIP launched 3 years ago – this will reward approximately the top 650 managers in the company for their role in turning around the business.

Slide 12 – Cash Flow

Turning now to cash flow, 2009 was a peak year of investment for us. Operational cash generation continued to be strong, despite the need to stock-up a new RDC, with the result that cash from operations was £1.0bn – some £40m ahead of the year before.

Capital expenditure of £906m included £520m for the opening of new stores, £50m for Sittingbourne RDC and £57m for the continuing systems programme.

Despite the big investments, net debt increased by less than we had originally anticipated, due partly to improved buying power as a result of the recession and also the tight internal control on our cash flow.

Our net debt continues to be at very comfortable levels. At the year end, we had £650m headroom against our revolving credit facility, and this does not expire until September 2012. We continue to be rated A3 by Moody's, one of only 3 retailers in Europe to enjoy this strength of rating.

This concludes the financial review…

Slide 13 - Optimisation Plan

I will start the operational section with our Optimisation Plan.

The Plan was launched in March 2006, with a second phase presented in March 07. The Plan was always due to conclude by January 2010, and so this is an opportunity to wrap it up formally.

As you all know, this was basically a turnaround plan designed to put Morrisons back on the very successful course it had been on before the Safeway acquisition. It was comprehensive, involving a complete revamp of the product range, the segmentation and rebranding of our stores, a complete new marketing approach and a number of initiatives designed to reduce cost to serve through the supply chain.

Before concluding on the Plan, I will just update you on progress in the past year.

Slide 14 – Optimisation Plan - space

As you all know, grocery space in the UK is hard to come by. The fact that we were able to cherry-pick nearly 500,000 square feet of space as a result of the Co-Op / Somerfield acquisition was great news for us. The result was that we out-performed our space target by 40%.

Slide 15 – Optimisation Plan – latest in store

Our various initiatives to improve store productivity continued in the past year, with great success from rolling out self-scan checkouts and intelligent queuing systems. These are good examples of how coming from behind in technology terms can actually be a benefit – we believe our self-scan units are the most user friendly in the market, and they are also the most efficient because they recycle the cash put into the machines by customers to be used as change for the next customer in line.

Slide 16 – Optimisation Plan – distribution

We talked at the half year about the opening of our new RDC in Sittingbourne, and many of you have seen it during our investor day last October. We are delighted with it, and it is delivering all the benefits we had planned. This has filled a major gap in our infrastructure, and future investments will be brought on stream as our growth requires. We have a site in Bridgwater which we expect will become our South West RDC during 2011/12 - the next point at which we will face capacity constraints. We anticipate a total investment in this site of c£100m.

Slide 17 – Optimisation Plan – systems

Much of our systems work under the Optimisation Plan to date has been in the design and development phases. The major roll-outs will take place in the coming three years, although we did see good delivery of early stage elements this year as well. Our HR, payroll and financial systems all commenced delivery and are performing well. The pilot of the new EPOS system has been very well received by the business and will ultimately replace 5 separate systems in store. It represents another example of our ability to use latest technology to become industry leading. The new system is processing card transactions 40% faster than the existing systems, taking us from slowest in the industry to quickest.

Slide 18 – Optimisation Plan – CSR

We have previously confirmed that all our key CSR targets for 2010 have been achieved. Today I will just highlight two other initiatives in this arena. The first is the Morrisons Academy, our training programme for staff. To support our Food Specialist for Everyone agenda, we have to deliver better and more knowledgeable service in store than anyone in the industry. The Academy offers this training and progression for all our staff, enabling them to grow from shop floor to top floor, a route taken by many of our most senior Directors. Others talk about having food skills in-store – the difference is that we really do, in numbers. Many of you know that we employ more trained butchers, bakers and fishmongers than any other retailer. You may not know that last month we were awarded Educator of the Year by the Wines and Spirits Education Trust in recognition of the trained wine advisors we have in every store. No other supermarket in the UK has this award, or provides this level of skill in store.

The second area I want to mention is the Morrisons farm, a joint venture entered into this last year. We want to use this as a base for research, and are already involved in a number of projects. One example is the comprehensive review we have undertaken into the potential for cross-breeding dairy cows to improve sustainable production – which has been widely praised by dairy farmers. Most of the areas that we research will look at the sustainability of food supplies or the efficiency of agriculture. Our research will provide economic benefits to our business, but will also strengthen our relationships with the farming community and make us all the more authoritative with customers.

Slide 19 – Optimisation Plan conclusion

So, to conclude the Optimisation Plan. We always believed the targets we had set ourselves were ambitious. In summary, they were:

- To grow the top line ahead of the market
- To improve EBITDA by some £460m per annum
- To open 1m square feet of new space in the three years to 2010

- To reduce our carbon footprint by 36% by 2010
- To grow the dividend strongly

I am delighted to say that we have delivered all of our promises, and more. This has been a significant driver of growth in shareholder value over the past 4 years.

Slide 20 – Optimisation Plan – shareholder returns

You can see that here – the increase in Operating Profits driven through the business over 4 years has been £700m, and over £500m of that came through the Optimisation Plan. The strong cash generation that went alongside it has funded our dividend growth, and in combination we have delivered an annual shareholder return of 16%. That seems a fitting note on which to conclude the Optimisation Plan.

Slide 21 – Food Specialist for Everyone

In looking forward, I suggest we start with our continuing vision – to be The Food Specialist for Everyone. This is a vision which really resonates with customers – we are different from our competitors, and as number 4 in the market that is pretty important.

Slide 22 - Food Specialist…

Our market research shows us clearly where we have succeeded in moving customer perceptions. Through a combination of in-store initiatives and effective advertising we have created market leading perceptions in all the areas shown on this chart. When we started the journey we would not have been seen as leading in any of these.

Slide 23 – Food Specialist…

There are still many important areas where we do not lead, and where as the Food Specialist we should. A number of examples are shown here. Our progress to date gives us confidence that we know what needs to be done, and we are at varying stages of making the change happen.

Ready meals is a good example – we know from our taste tests that our ready meal range is now every bit as good as our competitors, but this is not yet fully appreciated by customers. We haven't yet communicated this, and it is on our programme for 2010.

Slide 24 - ….for Everyone

Our food specialist credentials have moved forward strongly, whilst our reputation for great value continues, and clearly that is even more vital through the recession. The whole industry has been shouting about value, and we do that in ways that are different, and that customers perceive to be different. Some examples are shown here:

- Our 30p deals represent the lowest price fresh fruit and veg in the marketplace. We provide them through our own packhouses, so that the economics can work for us – it is very difficult for competitors to follow. So we are providing customers with their 5 fresh fruit and veg items in a day at the best value available.

- Our meal deals are provided through our manufacturing facilities – the Christmas family meal deal was a £12 value for £4 and it flew off the shelves.

- Our Christmas collector card worked really well for us again this year – it rewarded our loyal shoppers in a very immediate way and the £25 voucher provided many of our hard-pressed customers with food treats that they might not otherwise have been able to afford.

It won't surprise you to know that we will continue to keep value to the forefront, that we will continue to use our vertical integration as a competitive weapon and that we will continue to do things that take our competitors by surprise.

Slide 25 – National to Nationwide

Space growth is a key objective for us, and we had a great head-start last year…

Slide 26 – Potential to become Nationwide

… Our potential to expand throughout the UK remains a significant opportunity for us, as the map shows.

Slide 27 – National to Nationwide

Having successfully opened over 40 stores last year, and with the strength of our balance sheet, you will appreciate that the only constraint we face in our space ambitions is finding the right sites. We will not compromise on this – the space has to be right – but our flexibility in being able to operate from 10,000 to 40,000 square feet is opening up opportunities that in the past would not have been there, and as a result we are now confident that we can open a further 1.5m square feet of space in the coming 3 years of which 400,000 will be delivered in 2010/11, 500,000 in 2011/12 and 600,000 the following year.

Slide 28 – Forward plans and outlook

We are in the fortunate position of having a very strong business that has performed well through the recession. We can look through the economic downturn and invest for the long term, as our space expansion plans show.

Slide 29 – Current market background

In the short term, we expect 2010 to be every bit as tough as 2009, with increasing pressure on disposable incomes. We are very pleased that the inflationary pressures in store have eased for customers, although it is disappointing that the same cannot be said at the forecourts.

In trading terms, we will not change our stance at all in the coming year. Nearly everything we do will have a value slant, and we will continue to have the same focus on the core business that has served us so well. Promotions are a key part of our overall value offer, whether funded ourselves through our vertical supply chain or by suppliers.

Slide 30 – Continuing to invest

In the coming three years, we will make further significant investments in the business in areas where we see attractive returns. We've already talked about space.

In manufacturing, we will invest further in order to support our retail growth. We will need additional fruit and vegetable packing capacity in the South West alongside the new RDC. We also hope to expand further into other categories which suit our manufacturing skills, as we did recently by building an artisan bread line in our Wakefield bakery.

I will touch on distribution and systems in more detail in a moment.

In combination, these major areas of investment plus normal capex will require a total of around £2.2bn of capital for the business over the coming three years.

Slide 31 – Start of the logistics Optimisation Plan

We came out of the Safeway integration with a complex and costly distribution network, and our team has made great strides in sorting it out over the past four years.

Slide 32 – Completion of the Plan by 2011

The opening of our grocery shed in Swindon in 2007 and then the new RDC at Sittingbourne last year have put us in good shape, and the remaining major piece of the puzzle is to build another RDC in the South West. In volume terms, we need this in place by the end of 2011.

Slide 33 – IT programme

We are now well into our systems renewal programme – and we have a clear view right through to 2013 in terms of its completion. So far, delivery has been good, and the business is already seeing real benefits from the new technology.

Our key objective with the programme is to ensure that the front-end of the business hardly even knows that it is happening. In the past year, for example, two thirds of our staff moved onto new payroll systems – they all carried on being paid on time and accurately. At the same time, our wide area network has been changed and our mainframe systems upgraded, without the business even noticing. And our general ledger and fixed assets systems have been replaced without any impact on the timing of delivery of these results.

This, for me, is the first sign of a successful change programme. Change is happening without the business really noticing. We will continue in the same vein in the year ahead, with big systems roll-outs starting in stores, warehouses, manufacturing sites and in starting the build the new product file. I expect, in a year's time, to be talking not just about the implementation being smooth but also about what business benefits we are starting to drive through the new tools available to us.

Slide 34 – Summary

So to conclude, we look back on a highly successful period for Morrisons – one where we had our doubters, but were clear on what we wanted to achieve.

We remain clear about the next stage of the journey – we have a full programme for 2010 and many interesting opportunities for the longer term. By the time we see you in September, Dalton will have had a chance to take a good look at the business and he will of course give his perspective on the next key steps for Morrisons.

And now, Ian and I will be happy to take your questions.