MORRISONS

INTERIM RESULTS 2014/15 FULL SCRIPT

Slide 1
Sir Ian Gibson

Slide 2
Overview

Good morning everyone and welcome to our Interim results announcement for the six months ended 3 August 2014.

This is a period of unprecedented change for our industry and in recognition of that, we announced a fundamental reset of our business at the Prelims in March. Our first half results clearly reflect that reset.

Turnover was down 4.9% to £8.5bn and underlying profits were down by over a half, as expected, to £181m.

However in line with our previous commitments, the Board's confidence in the strength of our business, and our ability to deliver our ambitious cash generation targets, we have increased the interim dividend by 5% and confirm our commitment to pay a total dividend for 2014/15 of not less than 13.65p.

Delivering sustainable growth is a long term process and there is still a lot to do. We are still very much a work in progress. But although our like-for-like sales performance is yet to improve, some of the early positive trends in lead-indicator KPIs such as Items per Basket, are cause for some cautious optimism. Our profit expectations remain on track.

It's also been a period in which we have made significant progress on the range of strategic and operating initiatives we set out in March, particularly around cash, and Dalton and Trevor will go through these in more detail later. We'll take your questions at the end as usual.

You will have seen our announcement that Andrew Higginson joins the Board as Non-Executive Deputy Chairman and Chairman Elect on 1st October. Andy, who has had a distinguished executive career at the forefront of UK retailing, is well known to many of you, and I am sure he will be a huge asset to Morrisons. I am looking forward to working with him to ensure a smooth transition before I retire next year.

And now let me hand you over to Dalton.

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Slide 3
Dalton Philips

Thank you Sir Ian.

Good morning everyone.

In March we set out an aggressive plan, which included:

The operational transformation of our core supermarkets and a substantial investment in our proposition;

Significant sales growth through new channels;

And, a very disciplined approach to how we manage capital, including the delivery of £2bn of free cash flow over the next three years.

We're two quarters through this three-year programme.

As Sir Ian said, it's clearly very early days, and there will be a lag before we see an impact on our top line.

However, I'm pleased to report that we have made a good start to the plan we laid out in March, and that our profit guidance for the year remains unchanged.

This morning I'll elaborate on all aspects of our operational transformation and investment in our proposition; including the major price reset we've undertaken, improvements to our stores, and the very real progress we've made in addressing our cost base, which allows us to invest with confidence.

In addition, I'll update you on our online and convenience businesses, which continue to progress well.

Before I do that, let me hand you over to Trevor who will talk you through the financial health of the business, including the significant improvements we have made in our cash management.

Slide 4
Trevor Strain

Thank you Dalton, and good morning everyone.

This morning I will be reviewing our financial performance in the period, and providing an update on the range of initiatives we set out in the financial strategy at the Prelims. As Dalton said, it's early days, but I'm really pleased at the good progress we've made, particularly around cash.

So, moving into the detail of the results.

Slide 5
Financial summary

I will start with our usual financial summary.

Total turnover of £8.5bn fell by 4.9%, with both in-store, and fuel sales, down year on year.

Operating profit fell by 25%, to £287m. PBT of £239m was down by 31%.

As we set out back in March this reflects the significant investment we've been making in our proposition, the cost of developing our growth channels, convenience and online, and the impact of one off costs in the period.

Under our revised definition of underlying profit, which now includes new business development costs, underlying profit of £181m was down 51%.

Underlying EPS was down by 52%.

I will provide some colour around all of these movements in a moment.

Net debt has reduced by £209m since year end, as we focus on our plan to deliver £2bn of free cash flow over 3 years. In that context, and in line with the commitment we made in March to provide a dividend underpin of 5% growth in the current year, we have increased our interim dividend to 4.03 pence per share.

Slide 6
Turnover bridge

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

Moving left to right.

We saw a contribution of £203m from new stores, including a growing contribution from our convenience store rollout, and the impact of the 4 new core stores we opened in the period.

In all, new stores contributed 3.0% to sales.

Sales from our like-for-like stores, which includes online, fell by £501m, down by 7.4%. The headline LFL performance in Q2 was minus 7.6%, or, minus 8.0% after excluding the impact of food dotcom, a deterioration of 50 points versus Q1. This reflects the deflationary impact of the price investments we have been making over the period.

Moving to fuel – sales fell by £163m, down 7.9%, as a result of volume decline and average retail selling prices coming down.

Other sales were up by £19m, primarily from sales to 3rd parties as we manage the capacity utilisation in our manufacturing facilities.

Within “other”, Kiddicare sales were flat versus last year in the first half. However, there will be a year on year sales impact of £49m in the second half, as a result of our disposal of this business in July.

Slide 7
Turnover bridge - sales by channel

The next slide breaks out the elements of growth in our total store sales, excluding fuel, which fell by £298m in the period.

As you would expect, the core supermarkets business was the key driver of this decline.

However, we are pleased with the increasing sales contribution from our new business channels. Convenience, where we ended the half with 119 M locals open, and of course online, which we are effectively reporting for the first time today.

Slide 8
Sales performance

This slide sets out the components of our LFL performance.

Our Group first half like-for-like sales were down 7.4%.

In our supermarkets, sales per customer, or basket size, was down 3.6% to £21.38

Dalton will set out some of the more granular metrics we are using to monitor the impact of the investments we've been making in our proposition. There is obviously much more to do as we are still in the early stages of a three year investment programme. Whilst we are beginning to make progress, it will take time for the benefits of the various investments we've been making to flow through.

Slide 9
Underlying profit bridge

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

So starting with the half 1 underlying profit in 2013/14 of £371m. This is restated in line with our current definition.

There is a positive impact from new stores of £12m.

This has helped to partially offset the impact of the negative like-for-like growth in stores of £85m.

Like all retailers, we are faced with structural cost increases, primarily payroll and property costs, a headwind which added £44m in the period.

The impact of the investments we have made in our proposition was £135m in the first half. We expect the total impact in the year to be around £300m, as previously guided.

As planned, we were able to partially mitigate these headwinds through the progress that we have made in delivering the self-help programme that we outlined in March. Collectively, across the programme we have made savings of £105m in the period, and Dalton will update you on our progress in each of these areas in more detail later.

In the half we incurred £35m of one off costs, our full year guidance of £70m in total is unchanged.

And finally, the net cost of our investment in the new convenience and online channels, which we are now including in underlying profit, increased by £8m compared to last year. We expect the total full year outturn for new business development costs to be around £65m, in line with the guidance we gave in March.

Slide 10
PBT bridge

Building from the previous slide, this shows the components at a PBT level.

The first building block relates to the profits on the property disposals we recognised in the period. I will update in more detail on our progress with this programme in a few moments.

The second block relates to a small improvement in our expectations of the net impact of the complete exit from the Kiddicare business. We are working to re-assign the 10 store leases as the sites are vacated and believe that the balance of the provision that we created last year will cover our remaining costs.

We will update you on the progress with this in March.

This brings us to a PBT for the period of £239m.

Slide 11
Underlying earnings

Our calculation of underlying earnings is set out on this slide

I've talked through the key factors contributing to the 51% decline in underlying profit year on year.

At an underlying EPS level, this translates to a fall of 52% to 5.74 pence, the difference between the two percentages being accounted for by the expected increase in the underlying rate of tax in the period.

Slide 12
Operating profit

At a headline level, operating margin fell by around 90 basis points to 3.4%. Stripping out the benefit of property disposals, and adjusting for the impact of impairments last year, our underlying margin fell by around 190 basis points.

Although not on the slide, the lower fuel mix in the period boosted the operating margin by about 20 bps, compared to the first half last year.

Slide 13
Cash flow

Turning now to the important topic of cash flow. As we planned, there has been a significant improvement in the Group's cash flow.

Cash flow from operations of £551m fell by 10% compared to last year. This includes the impact of the fall in profits that I've been describing, but to a large degree, this impact has been offset by the benefits that are coming through from our working capital improvement programme, through a greater focus on stock, debtors and terms.

The improvement in operating working capital was £145m. This was partially offset by a reduction within creditors which was driven by the outflow of £25m for onerous property commitments. Within the cash flow from operations note, you will see a net working capital movement of £120m. Full year guidance of £200m of operational working capital improvement and £100m outflow relating to onerous property commitments is unchanged.

However, whilst we have made significant progress in delivering operational working capital, about £20m of the movement in the period has been driven by a temporary timing benefit, which will unwind by the year end.

We are on track to deliver our three year working capital improvement target of £600m, with £200m due this year.

In the period we realised £200m in cash proceeds from our property disposal programme. A further £80m was received just after half year.

In the half year, total capex was £257m, slightly below our plan. Full year capex is expected to be around £550m, in line with existing guidance.

Overall, net debt reduced by £209m in the period, with the net cash flow improving by £531m, compared to the equivalent period last year.

Slide 14
Balance sheet

To highlight a few points:

Pensions – our policy is to have strong, well-funded schemes, with a broadly neutral position. All based on prudent assumptions. The triennial pension valuation, which we completed in July, has confirmed that our three defined benefit schemes, with a combined funding deficit of £40m, and funding of over 97%, are in a strong position.

In the period our strong cash flow enabled us to reduce net debt by £209m to £2.6bn. We expect a broadly similar performance in the second half, with the year end position in the range of £2.4bn - £2.5bn. This is in line with previous guidance and our commitment to the conservative principles that have long underpinned this business.

Slide 15
Improved funding profile

So, our cash flow performance in the period has been good.

In addition, we have further strengthened our funding profile by extending the average maturity of our debt. In June, we issued a £300m 15 year sterling bond at competitive rates. We have also replaced our £1.2bn revolving credit facility, with a £1.35bn facility for a further five years, which has options to extend.

Slide 16
Property disposals

In March, I set out our plans to monetise value from our non-core assets whilst maintaining the strategic benefits and flexibility that an overwhelmingly freehold estate brings.

This involved realising some £1bn over three years from our development assets, some of our newer distribution assets, our investment properties and, in a small number of cases where it made sense to do so, the associated stores.

We have made an encouraging start to the disposal programme, recognising disposals of £280m in the half year, and we have achieved strong yields and also secured balanced lease structures.

Our commitment to maintain an overwhelmingly freehold estate in our core supermarket business is unchanged.

We confirm our full year guidance for £4 to £500m, and our plan to monetise £1bn over three years is on track, subject of course to the continuation of the current market.

Slide 17
Working capital

Turning to working capital. We have over the last year, step-changed the level of focus we place on operational cash flow throughout the organisation. Stock, debt and supplier terms are now established as a very prominent part of the weekly management agenda.

We delivered an improvement of £145m in operating working capital in the period. However, as I flagged earlier, around £20m of this is a temporary timing benefit that will unwind by year end.

On stock, the most meaningful area of improvement has been in our depot stockholding. We have been able to implement a large number of relatively small projects that have collectively enabled us to reduce depot stock cover by over 2 days year on year. Importantly, this has been achieved without detriment to our on-shelf availability.

On creditors, we have started a phased rollout of the supply chain finance initiative that I described in March. This is progressing well with a very good take-up from our suppliers. We expect the scheme to continue to roll out for around another 12 months.

Further working capital benefits will come in years two and three of the overall programme, as initiatives like sales based ordering start to land.

Our rigorous focus on cash management enables us to confirm our full year guidance of £200m of benefit from working capital, with confidence. And we are well on track to realise our target of £600m over three years.

Slide 18
Summary of free cash flow

In March, we set out this slide, whereby we would generate £6 - £700m of free cash flow this year, before dividends. This translates to a reduction of £3 - £400m in net debt over the year.

We have made good progress on all the key drivers in the first half, and confirm our target to deliver not less than £2bn of free cash flow over the three years to 2016/17.

Slide 19
Profit guidance

Turning now to the headline guidance slide.

In March we said that we expected our underlying PBT for the year to be in the range of £325m to £375m.

That headline guidance is unchanged.

However, there are changes to some of the elements within this.

We now expect the impact of trading and structural costs to be around £220m in the year, £20m higher than March.

The progress we have made in the first half on the self-help programme enables us to increase our guidance on benefits in the year to be around £220m, an improvement of £20m. Dalton will expand on this progress in a moment.

Our full year depreciation guidance is now expected to reduce by £10m to around £390m, primarily reflecting the progress we have made in bringing down the capex run rate faster than we had anticipated.

We are increasing our interest guidance by a net £10m, to between £95 and 100m. This reflects the completion of the new bond.

The guidance of £70m of one off costs for the year is unchanged. Within it, Kiddicare trading losses were £10m less than we had planned. However, that saving will be offset by higher costs in relation to restructuring.

Slide 20
Summary

So, in summary, whilst trading performance in the period has been difficult, we have made good progress across all the elements of our financial strategy:

- the pension triennial valuation has been completed
- our debt maturity profile has been extended
- strong working capital improvements have been delivered
- the property disposal programme is progressing well
- our debt reduction programme is in line with the plans we set out last March

Now, let me hand you over to Dalton.

Slide 21
Dalton Philips

Thank you Trevor.

I'm now going to talk to you about three things:

- Firstly, about our trading over the period;

- Secondly, I'll update you on the progress we are making on the three year plan we outlined in March;

- Thirdly, I'll close with an update on our new channels.

Slide 22
Tackling our underperformance

Let me start by briefly talking about our trading over the period.

Our like-for-like performance of -7.4% was behind the overall market, which remained an extremely tough environment in which to operate.

Two additional headwinds have impacted the performance of our business, over and above our main competition.

Firstly, our lack of scale in online and convenience remains a drag, despite our growth in these channels.

Secondly, the price cuts we made in the second quarter have had a significant deflationary impact.

Allowing for these structural headwinds, we believe that this leaves us with an underperformance of our core bricks-and-mortar stores of around 2-3%
relative to our closest competitors.

In March, we announced a bold and aggressive strategy to target this underperformance and reinforce our position as a value-led, fresh food grocer.

We are addressing the structural shifts in the market by resetting our price position and making sure that price is never a reason for customers to shop elsewhere.

This will allow the rest of our proposition, which we are also heavily investing in, to really shine through – things like the quality and provenance of our fresh food and the skill of our Market Street butchers, bakers and fishmongers, which we believe no-one else can match us on.

This investment is enabled by the significant self-help we are generating by transforming the operational model of our business.

Slide 23
We are seeing early signs of relative improvement

It's very early days, but we are seeing clear signs that this strategy is starting to work in a number of key performance indicators.

Most significantly, we are beginning to improve our negative volume trend.

This is the key lead indicator that customers are starting to notice our price investment and put more items in their baskets.

In terms of sales, the latest two Kantar periods show us moving back into the pack, though I wouldn't use that as an indicator for the future as this does include incremental promotional activity this year.

Although we've made a good start on each of the initiatives we outlined in March, we don't expect them to start to really begin to impact our like-for-like sales until the back-end of this year.

We are on a three-year journey and it will take time for customers to fully reappraise our offer.

We are in line with our expectations at this stage of the journey—and with other comparable retailers who have made similar price investments:
there is always a significant lag before sales improve.

It just takes time.

Slide 24
Operational metrics are also improving

In March we committed to sharing with you a number of operational metrics on an ongoing basis, which are shown in this table.

These show the good early progress we have made:

- Our items per basket, was down by 3.2% compared to the overall business like-for-like of -8.0%;

- We have removed over 1,500 SKUs since the end of the last financial year; strong progress towards our three-year target of removing 5,000 SKUs

- And we have already achieved our target of having 10% fewer items on promotion, with an almost 13% reduction year-on-year in the last quarter—whilst our promotional participation came down by 140 basis points in the same period.

This is very solid progress, however there is still a lot of hard work ahead.

Slide 25
We are generating £1bn over the next three years to reinvest into our business

Now let me remind you of the strategy we set out in March.

We committed to delivering £1bn of self-help over the next three years through three key work streams:

- Firstly, further enhancing our end-to-end product flow and processes;

- Secondly, realizing further savings across indirect procurement and loss prevention;

- And thirdly, focusing our promotional investment and reducing our sourcing costs.

We said we'd invest this £1bn in three ways:

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- Firstly, and most significantly, in our proposition;

- Secondly, in offsetting our annual structural cost headwinds;

- And thirdly, in supporting earnings growth, in line with the financial strategy Trevor outlined.

This plan is only possible because of the investment we have made in our systems, which has totalled over £300m in the last three years.

Whilst we still have work to do, we are starting to see these benefits shine through, as they enable us to execute this plan.

Now, let me now take you through the detail, starting with the self-help we have generated from three main work-streams.

Slide 26
We are improving our end-to-end operations
Work-stream one further enhances our end-to-end product flow and processes.

Within this I'm going to talk about three initiatives.

Firstly, a major management restructure in our core stores.

We have placed 15,000 managers in consultation, which will result in around 2,600 redundancies.

This restructure will simplify responsibilities and ultimately improve our customer proposition, and will be operational in over 80 stores by the end of this year.

In parallel, we've made similar structural changes elsewhere in the business, with around 300 roles removed from Logistics and Head Office.

Much of this has been enabled by the implementation of our new IT systems, which allow us to work much more efficiently.

New systems are also improving the way we flow products through our network, which is our second key initiative.

This includes:

- Continuing the journey to automated sales-based ordering, which will start with Frozen in H1 2015, before rolling out across all categories.

- And reducing our stock holding, which we have already taken down by over £170m this year.

- The third key initiative is leveraging our vertically integrated supply chain.

Our world-class manufacturing operation is an integral part of our business and we are focused on maximising its benefits.

We're still doing far too much non-value-added production in our stores, which takes our skilled craftspeople away from actually serving the customer.

So we're moving more tasks from our stores into our manufacturing sites.

Initiatives like this are a win-win.

For example, in June we launched our new Signature beef range.

It's cut and shrink wrapped by Morrisons butchers in our manufacturing sites, rather than in stores, increasing shelf-life from around 3 to 14 days.

A win for customers because it's a better product that lasts longer; and a win for us because it's easier to stock and reduces markdowns.

More importantly it means our butchers spend more time doing the things that customers really value, like cutting steak to order or preparing a Sunday roast.

Over time we are moving from having over 60% of our meat packaged in-store to around 20%, and we have further efficiency gains to come as we apply the same model across Market Street.

In total we have achieved £35m of self-help in the first half of this year and we confirm our £300m three-year target from this work-stream.

Slide 27
We are improving indirect procurement and loss prevention

The second cost work-stream; indirect procurement and loss prevention, is also on track.

Our new systems and processes are allowing us to focus attention on those areas where we have the greatest loss prevention opportunities.

For example, our increased use of security tagging, which we have extended into health and beauty in H1 and will deliver savings of almost £10m in shrink this year.

We are also making progress with regard to indirect procurement.

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So far this year we have reduced the amount we spend on in-store packaging for our Market Street products by over 10%.

In total we have achieved £20m of self-help in the first half of this year and we confirm our £200m three-year target from this work-stream.

Slide 28
We are improving promotional investment and reducing sourcing costs

Our third key cost work-stream is to make our promotional investment work harder, and to improve our product sourcing.

I said in March that we would reduce the number of SKUs on promotion by cutting the tail of minor deals by at least 10%.

And we have already achieved this; in Q2 total SKUs on promotion were down 13% year-on-year.

In Own Brand, we've totally re-engineered our product sourcing capability in H1, developing a dedicated team and best-in-class processes.

For example, in canned tomatoes we have made an annualised saving of around £1m without changing product quality.

We've also doubled the amount we source through the European buying group AMS to over €650m, which will grow to over €1bn by 2016.

We have had some quick wins in reducing our range, removing duplication and the number of variants, whilst retaining choice.

We have removed over 2,000 items since we launched the programme, with hundreds more to come in H2.

By the end of this year we will have achieved over 50% of our target of a reduction of 5,000 SKUs over three years.

This helps concentrate our volumes with suppliers, helps simplify our network and makes our stores easier to stock.

In total we have achieved £50m of self-help in the first half of this year and we confirm our £500m three-year target from this work-stream.

Slide 29
We are generating £1bn over the next three years to reinvest into our business

Overall, we have made a great start to each of the three big cost work-streams.

We generated £105m of self-help in H1, and we now expect to deliver £220m for the full year, up from our original target of £200m, due to a slightly earlier phasing of our three-year plan.

I am very confident we will generate £1bn over the next three years as our new systems enable us to realise savings which other retailers have benefitted from for some time.

Now let me turn to our customer proposition and our investment across seven key work-streams.

Slide 30
We have lowered more prices on a permanent basis

I'm going to start on price, because this has been our largest area of investment.

We said in March that price was the single biggest reason for customers choosing where they shop, and we had to recognise there was a new price norm in the market.

That's why in the early part of the year, we started systematically reducing prices on key Fresh items.

Then, in May, we launched the 'I'm Cheaper' campaign, lowering 1,200 products across the store by an average of 17%.

This was followed by further reductions, including another 135 lines lowered by an average of 14% in June.

Customers have really noticed our new prices and we've seen volume increase significantly across the I'm Cheaper lines, as we focus on building total items per basket.

For example in Produce, one of our key focus areas and where we have been lowering prices for longest, our average price per pack is now 17% cheaper year-on-year, and Produce items per basket has declined by just 0.4% vs. total business items per basket of -3.2%.
And these aren't promotions, these are permanently lower prices; as committed we haven't raised a single 'I'm Cheaper' line since we launched the campaign in May.

Neither have we compensated for this elsewhere.

In fact we raised fewer than 300 items last quarter across the entire store, compared to an average of nearly 2000 in our competitors.

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We're making our customers total shopping baskets cheaper.

And we're so focused on transparent, lower, prices, we launched the first price transparency website by any supermarket in this country – so customers can see any price moves we make for themselves.

I appreciate it's hard for you to see our pricing in action and for competitive reasons I clearly can't show you our internal index, but we've made real improvements and we're very happy with our current position.

You can see this in external benchmarks – for example in the last ten weeks we've won The Sun basket league nine times and been first or second in The Grocer 33
seven times.

And we're going to continue to invest in our base pricing.

Last month we lowered our mid-tier own brand bacon to £1.99 a pack or two for £3.50, it's now the cheapest of the multiples and the multi-buy matches the discounters.

We've still got more to do, but we want to make sure that price is never a reason for customers to shop elsewhere.

This will allow our other points of difference to shine through, like the quality and provenance of our fresh food and the skill of our Market Street butchers, bakers and fishmongers, which no-one can match us on.

Slide 31
We are offering fewer, more impactful promotions

Although we've been focusing on investing in our base prices, strong promotions remain an important part of our offer, and this half we've been working hard on developing a smarter, more impactful promotional package.

To achieve this we've been cutting minor and duplicative promotions.

The total number of SKUs on promotion was down over 10% in Q2 year-on-year, and promotional participation was down 140 basis points in the same period.

But we are still offering big deals that customers know and expect from Morrisons, be it the great offers we have on brands, like our confectionary tins at two for £8 this week, or our 500g minced beef, made in our own abattoirs and manufacturing sites, on a permanent deal at two for £3.50.

Slide 32
We are turning Own Brand into a competitive advantage

As I have said, we won't win by price alone, so we've been dialling up other areas of our proposition where we can clearly differentiate, such as Own Brand.

We've been simplifying our ranges, making them easier and more intuitive to shop; removing 8% of SKUs, whilst in parallel making our high-quality, mid-tier range significantly more competitive.

By using our vertically integrated business model we are able to improve our quality and at the same time bring prices down.

We've increased the number of SKUs we make in our own Manufacturing sites from 1800 last year to 2000 this year.

Clearly we've got more to do, but our Own Brand is now a much stronger offer for our customers.

This year we have won nearly 200 awards for our Own Brand products, up from 56 last year and like-for-like sales volume of our mid-tier is well ahead of our total business.

Slide 33
We are continuing to improve product quality

Another area where we can clearly differentiate our proposition is delivery of the very best fresh food.

This year we're spending £20m on improving our chill chain.

We're putting additional refrigeration on the shop floor, in our stockrooms, and in our manufacturing facilities, which will ensure we have an uninterrupted chill chain for our 150 most sensitive Produce items.

We're upgrading 20 stores per week, with the whole estate to be completed by November.

We've also stepped up our international sourcing efforts.

For example, we now purchase our blueberries directly from suppliers in South America and package them in our own manufacturing sites, instead of buying them ready packaged from third parties.

This has shortened our supply chain enabling us to get the freshest product, and in blueberries alone is producing a £2m annualised saving.

Slide 34
We are making our stores even easier and more pleasant places to shop

We also have a point of difference in our supermarkets.

At an average size of 28,000 square feet, they are big enough to do a full grocery shop, but small enough for customers to easily and quickly get around.

Since March we've been making a number of major changes to make our stores easier to shop.

And to put some real weight behind this, we've changed the way we incentivize store managers to make a portion of their bonus directly linked to customer service metrics for the first time.

And last month we extended the opening hours of 230 stores.

And we've backed this up with a number of smaller changes:

- We've removed locks from 150,000 trolleys at 290 stores;
- We're upgrading baby changing facilities and washrooms in 100 stores;
- And we've reduced queuing times, particularly at the weekend.

In Q1 we removed some of the tables, pallets and pick-up bins that were blocking our aisles and making our stores harder for customers to get around.

Whilst customers loved the clearer aisles, it impacted sales of some impulse lines.

In Q2 we rebalanced, re-allocating some sales space, but retaining our easier-to-shop stores.

As a result of all these changes we've seen our 'ease of shop' score, measured by Millward Brown, increase by seven points in the first half.

Slide 35
We continuing to develop our Morrisons card

We are close to launching our Morrisons card.

Clearly, due to commercial sensitivities I can't go into details about the actual proposition, but we are very confident this card will be a real game-changer for our customers.

Over the summer we have successfully trialled a number of different propositions and registered over 500k Miles card holders to help accelerate our launch, all of this enabled by the major systems upgrades that we have been rolling out.

The card will benefit us in three clear ways:

- Firstly, it will further reinforce our value credentials and strengthen our customer proposition;

- Secondly, it will allow us to communicate directly with customers for the first time, offering them the kind of personalised vouchers our competitors have been benefiting from for some time;

- And finally, over time it will dramatically increase our customer insight and allow us to make more informed, customer-centric decisions.

This will be a major weapon in our arsenal as we approach the crucial Christmas period.

Slide 36
We are delivering more focused and consistent communication

We are very clear what we stand for, and in the first half of the year we have made a number of changes to reinforce our position as a value-led, fresh food grocer.

We need to back this up by stepping up how we communicate.

Externally we've been focused on communicating our price investments through our 'I'm Cheaper' campaign, which was one of the biggest we've ever done.

And in-store, new systems have now allowed us to totally re-format our shelf edge labels, more than doubling the size of our prices, to back up our value message.

And in the second half of the year we will make further changes to clearly communicate our points of difference, focusing on Market Street.

Whilst we develop our Morrisons card, we've been innovating in other ways.

Our meat and produce vouchers which appeared in The Sun have been very successful in attracting new customers to experience our great fresh food – both the quality and the price.

And the five million packs of playing cards we have given out as part of our Summer Collector Scheme have helped us to attract more young families, a key target segment, and increased our big basket sales by over 5% during the summer.

Overall we've made significant changes to our supermarket proposition, and we're feeling confident about our offer.

We're making strong progress, and the leading indicators show we're going in the right direction.

Slide 37
M local is now at scale and continues to grow

Turning now to our new growth channels.

In Convenience we have opened 17 stores, ending H1 with 119 M locals and over 800k customers per week.

Later this year we'll be opening a new capital light distribution hub in the South West, which utilizes existing space in our Bridgwater distribution centre at times of the day when it has excess capacity.

And we're continuing to improve our proposition.

We have reviewed the range of every single category to further tailor it to the convenience customer and we've also improved our Fresh offer by repackaging around 100 lines to convenience-specific pack sizes, which has increased freshness and reduced waste and markdown.

This year we will open between 60 and 70 new stores, short of our original target of up to 100.

This shortfall was caused because a store package that we had anticipated purchasing, ultimately did not meet our strict investment criteria.

We will not open stores just for the sake of numbers.

As a result our end of year run rate is expected to be around £300m rather than the £350m we previously indicated.

However, our ambitions to rapidly grow our convenience business remain unchanged.

We are very encouraged by our progress, and have grown our M local property team to continue to drive the business forward.

Slide 38
Customer response to our new online service remains strong

Finally in Online, I'm pleased to report we are making excellent progress.

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We are very happy with our proposition as we enter the crucial autumn and Christmas periods and we remain on course to exit the year with a £200m run rate.

In the first half we expanded our coverage, including as some of you will be aware, to North London—thanks to new hubs in Enfield and Ruislip.

In August we opened a further spoke in Sheffield and as planned we will open two additional spokes, in Merseyside and Greater Manchester, later this year.

These spokes will enable us to serve up to 50% of UK households.

Also, in the second half of this year we will begin demand trials for an innovative form of 'click and collect' service.

And we believe our service metrics are best in class:

- Our 'doorstep rejection' rate is around 0.3%;
- Our one hour on-time delivery is over 97%;
- And our substitution rate is just 1%.

Overall, I hope you can see the rapid progress we've made in developing both Online and Convenience from a standing start just a few years ago.

Slide 39
Summary

To summarize, we set out a clear investment plan in March to address the structural changes in the market and improve the performance of our core stores.

It's early days, but we're proceeding at a rapid pace.

We have made a major investment in our prices and our core supermarket proposition, made real progress in addressing our cost base, and significantly improved our cash management.

Our initial progress is good and performance in several key metrics is encouraging.

And we expect our underlying profit for this year to be in line with the guidance we set out for you in March.

But there is still a lot of hard work ahead—we don't expect our initiatives to start to really impact our like-for-like sales until the back-end of this year as customers take time to reappraise our offer.

Finally, let me remind you of the journey we're on:

- We are modernizing our legacy systems;
- We are becoming a multi-channel business;
- And we are focusing on being a value-led fresh food grocer.

Not a discounter.

Not a hypermarket.

We are about fantastic value, supported by unrivalled service and skill in making and selling great quality fresh food.

This remains a bold and decisive plan to deliver this vision, which will make Morrisons truly fit for the future.

Now, let me open it up to your questions.