Wm Morrison Supermarkets Plc
Preliminary Results – 12th March 2009
Script

Slide 1 – Sir Ian Gibson, Chairman
Good morning ladies & gentlemen and welcome to the Morrisons annual results presentation.

Slide 2 - Agenda
We follow the usual format that you are all very familiar, Richard will take us through the results and the Marc will explain the business highlights, the story of the year and our expectations for the future followed by Q&A.

Slide 4 – Overview 2008/09
We're pleased to be reporting another year of good progress

These are challenging times but we have continued to deliver good growth in sales and profits – testament that the Morrisons offer is in tune with the economic backdrop and the demands of its customer base

Underlying Profit is up by 13% to £636m

As a result of which we are pleased to be increasing our dividend by 21% to 5.8p. This is in line with the progressive policy we set out last year and is further confirmation of the Board confidence that our strategy is delivering.

Board Changes

Roger Owen - Property Director, 34 years (21 on Board)

Philip Cox – NED - International Power

In 2007 ago we set out the building blocks of our Optimisation plan. I'm pleased to say that two thirds of the way through this 3 year programme we are very much on track. This is further proof that our strategy is resonating with consumers and that we are well positioned well for the future.

And now I'll hand over to Richard

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Slide 5 – Richard Pennycook, Group Finance Director

Thanks Ian

Good morning ladies and gentlemen. As you will have seen from our release, there are no surprises in our numbers – in 2008 we delivered what we set out to achieve, despite a backdrop which worsened considerably as the year progressed.

Slide 6 – Financial Summary

We continued to grow sales and profits, whilst also investing for the long term, both in our infrastructure and in customer acquisition. Turnover was up 12%, with a large fuel related impact which I will break out in a moment. We were delighted with our operating profit growth of 15%, to £669m, which included an energy cost headwind of c£60m.

Net debt increased, as expected, following a big year of investment, but our working capital management remained tight.

Slide 7 - Underlying Earnings

In setting our dividend policy last year, we introduced a measure of underlying earnings against which to apply it. Underlying profits were up more strongly than the statutory Profit Before Tax figure, because we adjust out the effect of property transactions. It will not surprise you that property gains were low this year, at only £2m. This was mainly because we do not have many surplus properties which we wish to sell – but also of course reflects the fact that this is not a market to sell them in.

The tax charge this year was 30%, in line with guidance, and we would expect a similar level in the coming year.

So underlying, basic earnings per share were up 16% and the dividend up 21% - resulting in dividend cover reducing slightly to 2.9 times, as we took a first step towards bringing our dividend cover in line with the rest of our sector.

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Slide 8 – Operating Profit

Turning now to the components of Operating Profit, our gross profit percentage was flat year on year at 6.3%, although as I illustrated at the half year stage there was a dilutive effect of high fuel sales in the year, which accounted for 20 bps. Another factor was the release of a provision first taken in 2005/6 relating to the rationalisation of our distribution infrastructure. The original provision was £75m, and after taking all final costs associated with this restructuring we were left with a balance to release of £8m, which is included in this line. The details of this can be found in note 21 of the accounts pack. Allowing for these two effects, our clean gross profit increased slightly by approximately 10 bps, despite the headwind effect of energy costs. We were able to mitigate these through continued delivery of our Optimisation Plan.

The split between first half and second half was pretty consistent with the prior year. If anything, the second half year this year was slightly stronger than a year ago, reflecting a very clean period of Christmas trading.

Other operating income includes rents that we receive from third parties for the units where we act as a landlord. Not surprisingly, we have seen some impact from empty units, including two sites that were occupied by Woolworths, but overall income grew due to a number of good new schemes being completed with high occupancy levels. We do not expect income on this line to grow further in the coming year.

Our administrative expenses increased by 5% which is well below our rate of sales growth and reflects our tight management of cost base.

Overall, then, our Operating Profits grew by 15% to £669m and by 10 basis points to 4.6% of sales.

Slide 9 – Turnover Bridge

As usual, we break out here the component parts of the turnover growth in the year. Clearly the key element was the like for like store sales growth of 7.9% - contributing £726m of sales to the business. New space contributed £214m, a relatively low number considering that we opened 2.7% new space – this reflects the weighting of openings towards the back-end of the year and the fact that new store sales densities are lower than those for mature stores.

Fuel had a very significant impact – average pump prices were 14% higher than the previous year, and consumers looked for best value, particularly when prices peaked in August at £1.31 per litre. We were quick to lead the market back down, when oil prices again began to fall, and across the year we generated volume gains of 11% as a result of our reputation for strong value.

Slide 10 – Cash Flow

Turning now to cash flow, 2008 saw a step-up in our investment activities. Our operating cash generation was strong, with good working capital control and growth of 24%.

The second, and final, £100m instalment of our pension scheme funding contribution was made in the year, and we are comfortable that our pension schemes are broadly in balance. Despite the market turmoil, and the impact this has had on investment values, we took the right long term steps with our pensions a year ago, basing all our discussions with the Trustees on very prudent assumptions, and as a result do not perceive any need for further funding measures at this time.

Our capital investment increased to £678m, reflecting our space growth, the acquisition of the freehold of our new distribution centre at Sittingbourne, the purchase of the freehold interests in a further 4 stores and the opening of our new abattoir at Spalding. These figures do not include any cash outflow relating to the acquisition of Coop and Somerfield stores, completion of which will take place in our new financial year.

We spent £146m buying back shares over the course of the year, at an average share price of £2.52, and this will have a positive effect of over 1%, on eps in 2009/10.

Slide 11 - Optimisation Plan

2008/9 was the middle year of Optimisation Plan 2, which is due to complete in January 2010. It was a big year for investment and a positive year in terms of continuing benefits delivery, as this chart shows. We have now invested £250m of the total £450m incremental investment previously announced, and our programmes remain on track.

In terms of benefits, the annual EBITDA delivered last year rose to £145m, up from £105m the previous year. Positive benefits came from our ongoing segmentation and ranging work, the opening of the Spalding abattoir and the start of the roll-out of self scan check outs. We are well on course to delivering the £200m that we committed across the whole programme.

Marc will update you shortly on the Optimisation Plan activities undertaken in the year.

Slide 12 – Capital Deployment

We have a big year ahead in terms of investment for the future. Our capital programme will be approximately £1.1bn, with the key elements being:

- Completion of the remaining Optimisation Plan investments, £200m, the largest of which will be the opening of Sittingbourne by the end of the year.

- A step-up in organic new space expansion, with c.10 new stores this year and an expectation of 500,000 square feet of new space in 2010/11, which will require £350m of investment this year.

- Completion of the acquisition and redevelopment of the Coop and Somerfield stores, for total investment of £320m. This transaction will also involve an operating profit and loss charge of c£40m in the first full year, but is expected to be earnings enhancing in 2010/11.

This capital programme will be comfortably funded from existing facilities and from cash flow. We will also continue to look for new opportunities that the economic downturn might reveal.

In the light of this, it is sensible to preserve our firepower, and so we will not be buying back shares in the year ahead. We will, however, continue our progressive dividend policy of moving dividend cover in line with the long-run sector average of 2.5 times by January 2010 – which should result in a further year of strong dividend growth for Morrisons.

Now let me hand you over to Marc for his review of the business.

Slide 13 – Marc Bolland, CEO
Thank you Richard.

Good morning ladies and gentlemen.

I'd first like to first update you on the progress we've made so far this year, and at a later stage, come back to the opportunities that we see. I'd like to give you some perspective, so let me first bring you up to date on the journey so far.

Slide 14 – The Morrisons Journey
. In 2006, when we did our strategic review, we clearly saw that we needed an evolution not a revolution to build on the good things Morrisons had and that we didn't want to change what didn't need changing.

We said in our 2007 strategy that we wanted to be the Food Specialist for Everyone. All these words have a meaning because it's about food, it's about specialists it's for a broad group of people, so it's good value for everyone. Our Optimisation Plan target is to improve operating margins whilst shaping for growth, and I'll come back to that at a later stage. The strength of our strategy was that we had a very clear focus. The focus was on value, on service and on fresh and, as a result, we delivered very strong growth in 2008.

Slide 15 – Sales Performance

Now, what was driving that sales performance over the last year? The like for like sales performance over the last year was 7.9%. If we break that out over the two halves of the year, the first half of the year saw 7.6% and the second half of the year saw 8.1%. And remember that 8.1% for the second half of the year was against much tougher comparisons. If you look at the 7.9% over the whole year, that was industry leading amongst the big four, so for us, good news. But as you can further see on the slide, we had strong customer growth that was driving those sales, and at the same time, we had basket growth. So it was not just driving for customers, it was also delivering the right extra value in the basket. So we feel it's a balanced growth in these key measures.

Slide 16 – Regional Performance

Now, the challenge we face – that's why I took you back a bit to 2006 – is to take the Morrisons brand outside of its heartland. TNS data now confirms that all regions are growing strongly but the South, especially London, and Scotland in particular all showed double digit growth over the whole year. So we have a broader appeal and we have a stronger brand acceptance. And that was, when we started our journey two years ago, one of the most important things. Will Morrisons work in the South, yes or no?

Slide 17 - Customers

As you know, I never identify individual competitors in the market. I've not done so over the last two and a half years and I'm not going to start now. So I have grouped them for you in terms of segments. The customer switching data that TNS had provided shows that we have three main competitive segments, what we call the big three, the premium segment and the discounter segment. We have gained customers from all different segments including our main three competitors. Our gains from the premium segment reflect trading down and, as a result, our Best range is up 5.3% whilst sales in our organic ranges also grew. When you look at the discounter segment, we're the only big four retailer that is not losing share. So if we look over the 52 weeks, we have a balanced growth and we get it from a very broad customer profile.

Slide 18 - Customers

Let's look a little bit more into our customer growth. Another very convincing story for us is that we've been growing a younger customer base, particularly pre-families and young families with very young children. Getting more customers through the door in all regions, getting more in the South and getting younger families is what we would have liked and now that is what we are achieving. But what was the strongest growth category? Why did these people come to our stores?

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Slide 19 – Category Performance

Our vertical integration and Market Street delivers industry-leading freshness and availability. And we saw double digit growth in our key Market Street departments and fresh categories. So our fresh and value strategy is clearly working for us, but at the same time, we are putting in place building blocks for future growth that Ian was referring to.

Slide 20 – Optimisation Plan Update – Key Building Blocks

Turning now to the building blocks and what we achieved last year. Our manufacturing supply chain is one of the big differentiators for us. In 2008, we opened a new abattoir in Spalding, and that means we are now totally self-sufficient. We're the only supermarket that buys 100% British meat, which we can also process ourselves. We also opened a new vegetable pack house in Flaxby which allows us to sort and grade whole crops. That means that we've now completed our present manufacturing needs but we will always keep looking at new opportunities as they arise.

Now, moving to distribution. During the year, we implemented a drive time planning system to deliver operational efficiencies in our supply chain. At the same time, we acquired the freehold over an RDC at Sittingbourne for £80 million. It will be operational by the end of the year. We also filed a planning application for an RDC at Bridgewater in the South West.

Slide 21 - Optimisation Plan Update – Key Building Blocks

In terms of store growth we opened nine new stores and completed 90,000 square feet of extensions. So when we add another 350,000 square foot in the coming year, we will have achieved our target of adding one million square feet of additional retail space by 2010.

Slide 22 - Optimisation Plan Update – Key Building Blocks

We also made good progress in IT systems renewal and we selected Wipro, one of the world's premier computer services companies, as our implementation partner. At the end of last year, we went live with the pilot phase of our new HR and payroll system and this year, we will start the rollout of new financial systems, distribution systems and EPOS systems.

Slide 23 - Optimisation Plan Update – Key Building Blocks

In-store, the range segmentation, the refresh programme and shelf-ready packaging development were all completed by July 2008. During the year we also started the rollout of our Intelligent Queue Management system which measures how many people are coming in to our stores and adjusts the number of open tills to meet demand. At the same time, the rollout of our self-scan checkouts commenced, which brings convenience to customers and more efficiency to us.

Slide 24 - Optimisation Plan Update – Key Building Blocks

As part of our range development, we re-launched hundreds of new value lines just before the recession started which meant that we were well-positioned to meet customers' needs. As an example, our 'Value' fish and chips is priced at £1.29 which represents strong value.

Morrisons is not only about value; Morrisons is also about innovation, and that's important for you to take away. If we didn't have innovation, these new customers that we get in from our competitors, would walk out of the door, and they're not; they're staying. For example, our 'Fresh Ideas' range is something ready to cook; you pop it in the oven and it's ready in 20 minutes. It's an alternative for dining out - the lamb shank, you can see for two people is £3.29. So again, we want to give great freshness, but for great value.

In non-food we are making the space work harder for us, but we are not suddenly trying to rebuild all of our stores for non-food. Our focus in range development is to design a range that complements our food specialist positioning. So one of the important things, in home and leisure is to make sure that we are good at delivering things that are complementing this positioning. The first part of the new range kicked in in the last quarter of last year and we saw promising growth there, especially in the current environment. But the biggest changes are coming in during Q2 and Q3 this year when we will re-launch more than 500 lines.

Slide 25 - Optimisation Plan Update – Key Building Blocks

We made strong progress in our CSR targets. I just want to remind you that two years ago, we were behind out peers. Now we have turned it around to take leadership in carbon management. In fact, we're the only grocery retailer that has been awarded the Carbon Trust Standard and The Carbon Trust is using Morrisons as one of the examples in the media for achieving good performance on carbon reduction.

Slide 26 - Optimisation Plan Update – Key Building Blocks

To summarise, our Optimisation Plan has three elements. The first element is the operating margin which is now at the level of 4.6%. We made good progress on the shaping of our building blocks as I just referred to, but we did it at the same time as achieving strong like for like sales growth of 7.9%. So the three things are occurring at the same time. It is getting the operating margin at a higher level whilst getting the building the blocks in place and whilst getting new sales, and therefore new customers.

Slide 27 – Current Market Background

Now, let me give you a perspective on the current market because the market is developing all the time. We have received three new pieces of market research on what consumers are saying and which have found that the food market is resilient to recession. We have seen that. Consumer feedback confirms that food is one of the last areas to trade down but consumers are trading down in their wallets and consumers are dining out less. Consumers are also switching stores more than ever before and there is more cooking at home. Our fresh pasta, for instance, is up 15%. But also our cooking ingredients such as garlic and herbs are all up strongly. And what we have also seen coming back is the Sunday lunch and the Sunday roast at home. In particular, our legs of lamb sales are up nearly 20%. So we see these things happening in the market and we respond with our ranges by making sure that the ranges are available. We have also noted that people are buying more convenience foods and we have seen in our Oven Fresh, the hot counter which cooks chickens, that sales are up 15%. We've got the facilities to cater for a lot more demand and we can make sure that we work that department harder. We also see that consumers are treating and pampering themselves more, so chocolate treats as well as bath products are up. I think that it's a positive message for retail because it means that people are going to consume more at home. They are still caring about fresh and healthy food but a bit less on ethics, so things like fair trade and organic, goes down the priority list in the mindset of consumers. However, we still see healthy growth in our organic ranges due to more affluent customers switching to us from the premier segment. The point is we now understand our customer background much better than we ever did before. We still use our own shop-floor feedback from our stores and store managers but now it's also backed up with robust research.

Slide 28 – Morrisons Points of Difference

Now, what are the points of difference that Morrisons has that are important in this environment and even in a changing environment? The first one is vertical integration. As I said, our vertical integration is now completed. What does that mean? It means that our availability was so strong that on Christmas Eve you could still find in our stores, fresh bread and sprouts up to 4 pm. It also delivers flexibility and we have the speed of reaction to bring in new lines in response to changing customers' demands that other retailers don't have because we are in control of the whole of our supply chain. It means that we can take whole crops from farmers and because we will use everything it gives us competitive pricing. It also allows us to do the industry leading fresh food deals, like a barbeque that we did this year for 4 people for £4. Our vertical integration means that we don't run out of stock which is what happens when some of our competitors try similar deals.

Slide 29 – Morrisons Points of Difference

Market Street has been mentioned lots of times before, but I think in times like today, even in times when we see there is an economic downturn, you have to invest in it. We invest in the future and so we have built a new, what we call, Fresh Food Academy, together with the six Food Colleges in the country, and we train 100,000 staff in what we call fresh food retail. At the same time, we certify all of our specialists – butchers, bakers and fishmongers; not only the ones that are existing, but everybody that comes in. This allows us to sell fresh value products because our specialist butchers butcher whole animals to provide cheaper cuts of meat such as a neck of lamb for a very cheap price. So now, when times are a bit more difficult, you can find, from the things that we butcher in-store, all kinds of cuts for a good value price that you can't find in other supermarkets. Why? Because we do the butchering in-store and nobody else does. It's the same with whole crops - we sell the odd sizes, which our competitors don't sell, in a big value bag for a very strong price. So customers who are coming into our stores find products that they don't find in other supermarkets that are fresh but also great value.

In promotions, we are not following the crowd and we try to be innovative. We have done some industry-leading deals with really hard-hitting prices and we were the first to work with the media using vouchers in a clever way. For example, we were also first to use a Collector Card scheme over Christmas which worked very well for us because new customers have stayed with us. Today we're running a totally different promotion again whereby we give away four packs of free fruit for a £40 spend.

What it emphasises is some of the things that we did with our Let's Grow campaign. So it's building in the consistency of what we do. 18,000 schools registered for our Let's Grow campaign and now more than five million children are participating in the programme which helps schools teach children how to grow fruit and vegetables from scratch. Therefore, we even link in the things that we did half a year ago with promotions that we do today. But what is more important is planting the seeds for growth for the future. We are now more popular with younger families and children are already starting to know that Morrisons stands for being close to the farmers, close to growing and therefore close to freshness.

Slide 30 – Opportunities – new customers

There are three clear opportunities for growth. The first opportunity is about customers. Our customer perception has soared and on all of our values of fresh, value and service we have seen a dramatic improvement over the last three years. We have made the Morrisons brand much more acceptable around the whole country and Morrisons is now a real part of the choice for all consumer groups from A to E. We still have some way to go but we will keep on planting the seeds for growth and driving the improvement in the perception of Morrisons amongst A to E consumers. Reliable industry data from TNS also shows that 40% of British households have not yet experienced a refreshed Morrisons and so we still have a huge opportunity to attract new customers.

Slide 31 – Opportunities – New Locations

The second opportunity is new locations. Today we have 382 stores which is a national coverage and research has told us that 16.6 million of the 25 million UK households or about two-thirds live within 15 minutes drive time of our stores. Knowing that drive time to the store is one of the primary factors which determines where a consumer will shop it means that about one third of the UK's households don't have easy access to our stores. So the opportunity is to provide easier access to the 8.4 million households that are not within 15 minutes drive of our stores.

Slide 32 – Opportunities – Smaller Stores

The third opportunity that we see is in store size. As you know, we have 60 smaller stores between 11,000 and 20,000 square foot. These stores have higher sales densities, higher sales density growth and higher fresh food participation than standard stores. So they are doing well for us. In the last half year we have developed four new smaller stores that have Morrisons' own specifications. So what did we do? We closed down the stores for two or three months and totally refurbished them with a complete Market Street. We can have something like 1,300 lines of Market Street and fresh lines available compared to 1,700 lines that we currently have in our bigger stores of 35,000 square feet. 1,300 lines is probably more than any big other supermarket in the UK. So it puts extra emphasis on our ability to operate a much smaller footprint using Morrisons Market Street.

However, we don't do a one size fits all, so none of these stores are going to look alike. We're going to take individual stores and look at their catchment area. We're also going to have a look at the competition around it and whether they're in town or out of town. It gives us the opportunity to really tailor the store for the needs of the catchment area and it also gives us opportunities in locations out of town, on the edge of town and even in town. But let me remind you: these are not convenience shops, but they are our answer to convenience shops because they provide convenient shopping.

Slide 33 – Potential New Representation To Become Nationwide

We now have the flexibility through that to operate stores between ten and 40 plus thousand square feet, and that allows us to reach more places and therefore more households. We have identified more than 100 potential new sites where we want to put down a new store or buy one. Priority will be given to bigger stores but as I have already said, smaller stores also represent opportunities for us.

Slide 34 – Our Focus

Our focus, therefore, in the coming years will be on space growth and a strategic next step for us is again very much focused on moving from national to nationwide. Our first move is the acquisition of the Co-op/Somerfield stores that I'd like to take you through now.

Slide 35 – Integration of Co-op/Somerfield Stores In 2009/10

As announced, we have acquired 500,000 square feet of additional space from the former Co-op/Somerfield stores. These additional stores will give 1.2 million households easier access to Morrisons. We did our research and had first choice and pick of the Co-op/Somerfield stores. A significant number is in the South East, in Greater London, and in the South West where we are currently under represented.

The experiences of the four smaller stores, which I just referred to, are going to be used in the building of the newly acquired stores. We're going to close them down and we're going to invest 2.5 million per store to get them properly fitted out with a small Market Street or even a larger Market Street, depending on the size of the store. The integration is planned for Q2 and Q3 of this year.

Slide 36 – Space Growth

In 2010-11, we want to increase the amount of space growth by 40% from 350,000 square feet to at least 500,000 square feet for that year to keep the momentum going.

In our Optimisation Plan we have achieved 650,000 square feet so far and with the stores and extensions that we have planned to do this year we will reach the target of one million square feet by 2010. However, we will also develop an extra 500,000 square feet through the Co-op/Somerfield acquisition during this year and add another 500,000 square feet in 2010/11. That means we will add a further one million square feet on top of what we set out in our Optimisation Plan and so our space growth over four years to 2011 will be two million square feet, which represents acceleration in space growth.

Slide 37 - Summary

Now let me summarise. Last year we had very strong like-for-like sales growth of 7.9% and strong underlying profit growth. We also had a healthy cash flow and maintained a strong balance sheet. We delivered strong dividend growth and Morrisons has been embraced by a wider audience, so we now have a broader appeal. So we feel that our strategy is working for us and it gives us great confidence. But now adding to that, we've got the flexibility to develop stores in a much wider range of sizes and to reach many more places and households. The next step in our strategy is to move Morrisons from national to nationwide.

Thank you.