Sainsbury's Supermarkets Ltd

CAPITAL MARKETS DAY

Wednesday 25 September 2019 – 13.00

Mike Coupe
Chief Executive
Good afternoon everybody and hopefully you enjoyed your store tour this morning. And it gave us a chance to showcase some of the things that we are going to go into a little bit more depth this afternoon. And also to showcase some of our Management Team, because although you see me reasonably frequently, we have strength and depth and that gives us an opportunity for our teams to talk to you about some of the work that they are doing and hopefully give you some insight into the subject matter experts and their particular area of responsibility and expertise.

If you open the curtains there is actually a cricket ground behind us which is very slightly bizarre and anyway it's raining at the moment so what I am going to do this afternoon is give you a quick overview of what we will be talking about, starting with talking about the market and why we believe fundamentally that the earnings of this business are underpinned by the plans that we have. And secondly, that there are some significant opportunities in the future.

So just to help ground my Presentation in the market and the dynamics of the market, I just wanted to talk briefly about the two big factors that are driving the UK grocery market, indeed UK Retail more generally. And that is firstly the growth of the discounters and whether we like it or not they continue to open space that inevitably has an impact on our business and it increases the imbalance between supply and demand. And secondly, inevitably there is a rise in the digitisation of shopping, the growth of online and that growth continues to fuel customer behaviour and shopping habits. And we need to adapt, and we have set out to adapt our business to that changing market environment.

And then just to make it really exciting, there is low or no underlying growth within the UK Grocery Market. Broadly speaking the growth of the market is related to population growth and therefore as more capacity gets added, that continues to put pressure on the underlying economics of any retail business. And you can see that writ large virtually every day within the press with the failure of lots and lots of retail businesses in the last period of time.

So that's the backdrop and that is the context and we have talked openly about that in the past and we have to adapt our business to that changing environment. We have a very clear purpose as far as our customers are concerned, which is to help them live well for less. That has been the branding of the business for quite a considerable amount of time. Something like 10 years now. And we have a series of priorities which we will go into in more depth during the course of this afternoon.

First of all, we need to be more competitive on price. We know that and we will talk about how we might address that and certainly Graham this morning gave you some insight into some of the things we are doing within the baking category and we will expand on that during the course of the Presentations this afternoon. We know there are opportunities to offer distinctive products and particularly for Sainsbury's customers they do have a propensity to trade up. We do have a more affluent customer base and therefore if we offer them the right products they will buy them and they obviously will enhance our mix. And again hopefully you will have seen in the store, and we will expand on more this afternoon, there are opportunities in new categories, Beauty would be a very good example. Sainsbury's as an organisation has roughly a 3% market share and there is no reason why we shouldn't substantially grow that over time. And it is the kind of category where our customers give us permission to compete.

Thirdly, we want to make shopping more convenient and we want to support that with great service, and again hopefully in the store tour you got some idea of some of the innovations we are making. SmartShop will be one example, but also just the way we layout our shops, the way we think about the interaction between the digital and physical real estate is starting to move forward quite significantly at the moment. And of course all the work that we have done on restructuring our shops and measuring our service enables us to have a much more granular view of what we are doing literally day by day, store by store, department by department, and feed that back to our colleagues so that they can react to our customers and their desires, needs and wants.

We know that we have to drive efficiency in our business and we need to do that in order to be able to invest back in our customer offer. And we will talk this afternoon no only about a pay to play, so basically covering the cost of inflation, but also a series of opportunities that we think are unique to us because we are going to integrate our businesses to hit our goal of helping our customers live well for less. But also to enable us to drive efficiencies above and beyond just the normal pay to play you would expect from any business in our market.

We will talk about growing connected services, and by that we mean financial services and Jim will talk around the Bank. And secondly, some of our plans within Nectar which we think is an untapped opportunity for the future. And we will talk about some of the market opportunities that we have there.

And last, but by no means least we will round off with a view of where we are planning to take what we would describe as a seamless customer experience, but how we join our physical and digital real estate together and how we see that evolving over time so that we can be a truly multi-brand, multi-channel business.

We have put some metrics at the bottom, in the end we are a very strong believer, or I am certainly a very strong believer in our business model starts with our colleague engagement. If our colleagues aren't engaged they won't interact with our customers in the right way. If they are engaged it improves our customer satisfaction. If our customer satisfaction improves we will grow our volume share and that will drive the profitability and the cash flow of the business and the return on equity. So those are the key measures that we will be looking at and reporting on in the future.

In terms of the Presentations this afternoon, the first part is about being confident in our core. Paul will expand much more on the work that we have been doing on how we are readjusting our value proposition, particularly within the food business. Graham has already touched on some of the points, but will be more expansive about that, how our customers are responding and how we have confidence in our ability to be able to sustainably fund the investment that we need to make in improving our pricing and our overall proposition.

Simon will talk about what we have been doing on Service and what we have been doing within our Convenience business, how we have changed our store operating model, why we have done that, how that is improving our service. And how it is also improving and lowering our cost to serve. And also to build on some of the points that were made this morning, how we are thinking about investing in our stores and how we can actually do that in a cost effective way and improve the returns that we are making in those investments.

We don't often talk about our Property Estate, but in the end it is one of the things that underpins the value of this business. So we are going to give you an overview of our Store Portfolio and some of the choices we are now making about how we do a better job of realising value from that Store Portfolio in the future, and Patrick will talk about that in some considerable detail. And then Kevin will talk about the work we are doing on cost transformation. Firstly, the pay to play, how we cover the cost of inflation, but secondly, how through the transformation, bringing our businesses closer together we can release a structurally significantly cost savings, and cost savings which are only available. We would take the view to ask not to necessarily our competitors. So we think there are some opportunities for us to lower costs faster than our competition.

So as confidence in the core, but above and beyond that we think there are opportunities for growth. Jim joined us 90 days ago, he will tell you about our Financial Services strategy. He has got 90 days or had 90 days to think about it. So with a target of getting here and today we have made some quite significant announcements around stopping mortgages and also making sure that we are not putting any more cash into that business in the future. But also we believe there is an opportunity to grow the earnings of our Financial Services Business by focusing on Sainsbury's and Argos customers in the future.

And then to bring it up at the end, we have got Mark talking about Nectar and first of all what we are already doing with Nectar. Secondly what we are doing to digitise Nectar which again is an interesting opportunity in the way that we interact with our customers. And thirdly, something that we haven't talked about before, but we believe that there is a substantial opportunity to further monetise the Nectar data in a way that joins our suppliers to our customers through our ecosystem in a much more thoughtful and targeted way. And again we think because of the number of investments we have made over the last period of time that we are uniquely placed to be able to do that in the UK market.

And last, but by no means least, Clo will be talking about digitising our customer journey and we have invested a lot of money over the last period of time basically unpicking some of our legacy systems, putting a lot of stuff in the Cloud, breaking it into service based architectures, investing in Wi-Fi in our shops, investing in big pipes to allow us to get the data in and out of our shops, which we believe gives us a platform for uniquely connecting our business together. And then showing up to our customers in both our physical and digital real estate in a completely joined up way. And hopefully you got a flavour of that this morning, but we will be more expansive in some of the plans that will hit down and this is not fantasy land, this is stuff that is real which will hit down over the next 12-18 months and will be in the hands of literally millions and millions of customers over the next period of time.

So multi-channel, multi-brand business, we have a unique set of assets and capabilities. By joining up our propositions we can do a better job of serving our customers, in our words, whenever and wherever they want. We can only deliver this by fully integrating our business. We will talk about that more during the course of these Presentations. And it will give us the opportunity of fundamentally restructuring our cost base which should be a source of competitive advantage in the future.

As I say we will help our customers live well for less. We have got confidence in our core business. We believe that will continue to generate earnings, cash flow and ultimately pay down debt and pay you our shareholders a dividend. But we also think there are growth opportunities within some of the things I have already talked about. We believe by creating a multi-channel business we will have sustainable cost reductions, we will be able to cover the cost of inflation and invest in being more competitive. That will allow us to generate cash, pay a dividend, deliver and ultimately in what will be a relatively challenging market for the foreseeable future, give us financial flexibility and resilience.

So that is it from me for now. I am now going to hand over to Paul, wherever Paul is who will take you through a more expansive version of what we will be doing on our Food Business. Paul.

Delivering our Food Proposition
Paul Mills-Hicks

Thank you. Showcasing our Management. So I am Paul, I am the Commercial Director for Sainsbury's. It is nice to be this close to the audience. I am going to talk to you a little bit about our customer proposition through the lens of product.

We have actually been very bullish about our performance on transactions in the market over the last period of time and we think we have led some of the thinking that keeps feeding customers what they want to do, which is shop more frequently. But where our challenge has been has been on basket size. And you have seen that in the commentary in the industry over the last six months in particular.

So typically what we are doing is, versus our traditional grocers winning transactions, which is pleasing, but those transactions are losing one or two items out of the basket, particularly that more value conscious end. And hence why Mike tees up the work that we have been doing on value.

So I would group the actions we have taken into three key headings. The first one is Entry Price Points, a replacement for basics in effect. The second one is using the Nectar data, 18 million customers using that data, to see where can we invest to optimise price for our customers? Where can we drive the best volume response? And then thirdly, being a bit more punchy on promotions, particularly those above the line promotions. So where the market over the last 12-18 months has become more competitive, we have stepped into that now and being more punchy. I will show you the results of those actions that we have taken on behalf of customers.

Importantly the question is, is it sustainable? And I would suggest that we have got four key areas that allow us to say we are confident in it being sustainable. I would be very bullish and say to you that our business runs the best value chain analytics programme in the UK. I believe that when you benchmark our programme of on the stand structural costs from field to fork we are really, really good at this. And I will take you through some of that detail. And that is pretty fundamental to competing in the 'Own Brand' space in particular.

Secondly, something that Sainsbury's, you guys, will all know, we have a large overtrade in some particular areas. So areas such as So Organic, Taste the Difference, Free From. But also in some of those specialist brands we overtrade. So we can optimise our sales mix to make a little bit more money in one area so we can invest in some of the other areas where we are more competitive on price. And that is very much an advantage to us.

And then certainly post Asda, we want to work with our suppliers to grow their business. If they can grow their business with us they will help and invest in Sainsbury's. So we see a synergy of working together, and particularly because of our over-index. If you can put yourself in the shoes of some of these big suppliers, we are the destination to launch NPD because of that large overtrade in those key areas.

And then finally, Simon and his team and all the work they do with Patrick, creating those savings that we can reinvest in the proposition. So I would say we are really pleased with how customers have responded. The customers were already in the shops and what they have been telling us is they couldn't fill the basket with what they wanted. I will show you the data that shows that we think we have addressed or started to address that.

And secondly, I am very confident that we can keep our distinctive and differentiated proposition funded in the long-term.

So before I launch into some of the data, I just want to give you a little feel for what we call the Product Quality Framework which in a way is a fancy way of saying the ranges we sell. So Mike has talked to you a number of times before about this and we try and group these product dimensions in four different areas. The reason we do this is because if you leave buyers to do it off their own volition, they tend to make it all up. So we do it very structured, very disciplined. Every single buyer has Nectar data on their desktop, so it is data driven as well. And to give you a feel for it, on the left-hand side it is about three quarters of our business on volume terms. And we would say it is commoditised. You can play at the fringes, but fundamentally customers are making a price comparison between us and our competition. As a result of it being much more competitive you can see that the profit contribution it generates is actually an under index for only two-thirds.

On the right-hand side you can see where our overtrade and Patrick will talk a little bit about our overtrade from an estates perspective. You can see it is actually a quarter of our business, this is a much more differentiated proposition. And it over performs on profit. Taste the Difference would be one you would be very familiar with, but brands are important in that area as well. So it is important, as I take you through the information, keep this in mind as a broad brush outline of how we talk to the left and the right-hand side.

The one thing I would stress is this is fundamentally a relationship between product and the way we see, not customers. We do not segment customers in this way, because you tend to find that customers shop across all of it and they don't behave just one way through the year. So customers might shop more to the left and then it is someone's birthday in the family and they will switch to the right. And at Christmas everybody wants to switch to the right. And in January everybody wants to switch to the left. So don't think of it as a way of thinking of customers, it is a way of thinking of products and their relationship with customers.

So you have seen this slide before, Mike tee'd it up at the Prelims back in May, this is the heart of the exam question we are trying to answer. So if transactions are so good, why are your sales going backwards? You can see where we are taking the hit. The hit is at that entry price point, there are one or two items in a basket for the more value conscious, more competitive products that are coming out of the mark-up.

So back to those three actions we have taken. The first one is that we have looked to re-launch our entry price point. It was all under one banner on the Basics. We are going to move to 13 brands. We have done a lot of work to define what those brands should have as an identity in terms of look and feel. And also on the quality and value proposition that is there. And we are about 60% of the way through. So in the shop you were in today we had about just over 120 skews live. Graham will have told you more about bacon than you ever wanted to really know. We will get to over 200 by the year end. We will get to about 90% complete by Christmas. And so far the reaction from what we have been doing has been positive. So if I show you some of the data that breaks down J.James in particular.

On the left-hand side of that dash, that is where we launched J.James. You can see that we were not having a good time in this category, we were losing share out of that value led area of the business. We launched J.James, customers are already in the store, they just weren't putting it in their basket and so it starts to convert and you can see we switched into positive switching from the actions we took. Now to hit the price points we are trying to do, it is a percentage margin investment in the offer. These products make less percentage margin than those that they replace. But what we are trying to do is change our business in a way it thinks in the trading teams towards thinking of cash margin rather than percentage margin.

But the reason why I say that it is important, is what I have broken out here on the right of the chart is you can see a purple and an orange bit. The orange bit is where a customer was previously shop and maybe buy Sainsbury's, a brand Taste the Difference. They have seen the J.James and they have traded down into this tier. The purple or the blue is the great news which is this was a customer who might have shopped through the rest of the store, but had decided not to opt into meat, fish and poultry or may have just not shopped in Sainsbury's. The blue is accretive in cash terms. So as long as we can get marginal costs equal marginal revenue and we win. And what we have to do is make sure that the discipline in what we do is that that orange bar does not become bigger than the blue bar and we in effect deflate.

And the reason why that is important is because at the moment J.James is actually cash accretive for Sainsbury's, it is not profit dilutive. So as long as we do a good enough job in the tiering and we keep really focused on what those customers do, this does not require a substantial investment in our P&L. So that is the task we have got to keep doing as we roll through all of those products through the rest of the year.

But it is not only about the entry price points, it is actually a relatively small part of the business in its totality. The other high velocity skews that would be in the second box along, those high value commodity lines where it is buy Sainsbury's. We have also made some investments using that data from 18 million baskets to optimise where we can put our price. And we have been really pleased with the volume response in those areas.

Now the other bit that we try and do is get some credit for the value that we put. Very often whenever we do any of the quality service interviews, people perceive Sainsbury's to be more expensive than it is. So we have been experimenting with a number of different mechanics. You will have seen WiGigs in the store. But lockdown is one that has worked really well for us, and what it does is it allows customers to know that that product will be locked down for 8 weeks. It drives frequency because they can shop with confidence and we hope that they then get to see our overall proposition. As I say their perception of price tends to be higher than the pricing reality. And we will keep going with lockdown given that the feedback we have from customers is so positive so far.

Now this question came up quite a lot in lunchtime, so luckily I had a slide prepared for it which is, have you just been promoting a lot more? So some of you will know, certainly I would suggest that we have led the market in the thinking to provide more clear and transparent pricing for customers. Promotional penetrations of over 80-90% in product groups I don't believe is good for those brands. And I don't believe it is good for the retailer.

So what you can see on the left-hand side is that we have traditionally been lower over the last 3-4 years than our competitors, up 34%. You can see that Asda has made a move year-on-year to come down which I think is good for the whole industry and good for customers and consumers. And we are less promotionally dependent than Tesco or Morrison's. If you ran this data for 12 weeks it would show the same pattern. So we have promoted more in the last 12 weeks. In a post Asda world it was the right thing to do for our customers and for our business. Suppliers wanted to invest in Sainsbury's, we are a prime destination for them. That was the quickest and easiest way for us to drive an outcome in growing their business.

So as I say if you look to the 12 week data it will show the same broad pattern. The margin narrows, but I would make the point, we are still less dependent than our competitors and we remain completely committed to transparent and clear pricing for consumers. It particularly works for Sainsbury's because of the tendency of our customers to want to trade into better value, not just cheaper. So the trade-ups that we can do with our suppliers are very different to those that they would get in some of our other competitors.

On the right-hand side we have been more punchy in the last 6 months, the last 12 weeks on something like petrol. The market did heat up above the line, big deals. And we have responded. So you can see we are playing a bit of catch-up, we will keep an eye on that market and how it reacts. But on behalf of customers we need to be punching in that space. You will see that Asda does nil, it actually tends to lead the market down on base price moves. So it doesn't count as a promotion but they tend to lead the market down. So as I say really important to register, we have promoted more. Suppliers as a step towards us post Asda was the right thing to do, but it is not a change of direction for us.

And so where does that leave us in the value index? I am convinced that customers are very focused on the value index and the correct promotional highs and lows in their overall basket. And so the overall metric I look at is the total basket. What you can see on the left, and we are really proud of this, is as we stand today Sainsbury's has not been more competitive versus Tesco across 15,000 skews in 15 plus years. So I will just say that again, Sainsbury's has not been more competitive on a broad basket of 15,000 goods than it is today.

Now if you look at the left-hand side it goes up and down, it moves in cycles, sometimes those cycles are four monthly, three monthly, six monthly. But I would suggest that if you look at the trend, even with my poor excel skills I could have put a trend line on there. You can see that we have been closing that gap materially over the last 15 years. So we are really, really proud of that. And as I say the dilemma we have is how do we get credit from customers for all of that work.

And the other bit is we have closed without work on entry price points brought to those high velocity lines, we have closed just under 800 basis points, the gap with Aldi in those high velocity lines. We are not complacent, that is not good enough for us, we have to keep going in closing that gap down. But it is progress.

So how have customers responded? You guys see some of this data. So on the left-hand side you can see our value growth. The four weeks is very spiky, you can correct it for petrol deals, you can do six for 25s in the market, so tend to counsel to look at the 12 weeks just as a direction of travel. Even better is when you look at the 52 week to understand the changes in the marketplace. So on the 12 week as we have taken these actions, you can see that consumers have responded. And so you can see we are doing relatively well, this is this is the traditional grocers and we are broadly in line with the marketplace with the growth in the discounters. So it is a positive reaction from the customer.

Importantly on the right-hand side and Mike has mentioned this in terms of volume, it is not coming from price. It is coming from volume and sales mix advantage, the two things together. So if you go back to that PQF balance in the left and the right. So we are really pleased with where we are.

And if I try to give some colour of what is underneath it on this chart, you can see as is often written, the big issue is the traditional grocers losing share to the discounters from all that additional footage. And we have been in the pack nip and tuck, cut and thrust. But from May onwards when we start to pull our levers and launch our entry price points, correct some of the price and optimise cash, you can actually see we had a really good run reducing those losses substantially to the discounters. And actually at the moment we are doing better than the competition in stemming those losses. But as I say, we are not complacent because they are still losses.

And we have talked a lot about value, it is the key answer to the question of why we were losing one or two items out of the basket. However I will come back to what makes us special is universal appeal. We will not win by just being another Aldi, we have to be a better Sainsbury's. And so as we have been rolling on, on entry price points, we have also been re-launching Taste the Difference. Taste the Difference is a £1 billion brand, it does really well for us and what you can see on the line chart on the right is that whether it is Taste the Difference, So Organic, my particular favourite, Fresh Pasta. All of these product areas where we have 28,30,32% market shares, then play a role in switching premium customers away from M&S and Waitrose. So we have done a better job, still not good enough, but a better job against the discounters, but we do have an iron balance in the distinctiveness of our proposition in winning those customers from Waitrose and M&S and that is two years worth of data that you can see with consistent wins.

And if Own Brand is important, just under half of our cash sales, about half of our total volume, actually one of my frustrations is that when you visit supermarkets the offer has historically been very similar. So we set out 18 months ago to change that. And we launched our distinctive brands, future brands, team targeting entrepreneurial brands to get them into distribution with us either exclusive to Sainsbury's or exclusively in the grocery channel. And actually we have been really, really pleased with the results. We have got over £200 million of sales now from what we call these brands. And they are doing something very different in the store in terms of the choice and the interests they give our customers.

Most importantly with a commercial hat on is they are accretive. So back to this creating cash, incremental cash, these brands are not cannibalising other brands in the fixture. So you can create a win/win culture with our big branded suppliers as well as the entrepreneurs, as well as Own Brand manufacturers. And that is what we are trying to do in creating that balance.

So what I have done here, on the left-hand side is you can see the original chart that Mike showed at the Prelims and in the middle, I will just roll that data set forward so you can see the most up-to-date. We talked a lot about the economy Own Brand. So we have reduced those losses, we have halved the run-rate from where we were. We are holding onto that Premium Own Label and post Asda our branded share is growing as suppliers step towards us as a prime destination for investment. So we are really pleased with that because it is the balance.

I have put Tesco up there just to compare and contrast. They have done a really good job on the economy Own Brand but you can see the balance is not in the right direction in my humble opinion compared to our own. So I would just like to make that point again. It is all about the balance on the left and the right, we have to be a better Sainsbury's and not try and mimic some of the competition.

And so I have talked a lot about what we have been doing in the last six months and a lot about the past which gives me confidence, hopefully gives you confidence. Just talk a little bit about the future as well. So where are we on this journey? So the good news, well Mike doesn't describe it as good news, he says I am going too slow, but I think it is good news, is we have done about half of our food volume through that product quality framework. So still another half of the business we can run at in terms of resetting the ranges, prices, range hierarchy, supplier relationships. Half of the opportunity to go, what are we saying to the supply base? We are saying we want to put the same amount of volume through fewer skews. That is great news because that is a very efficient way to run a business. And those branded manufacturers and Own Brand manufacturers that want to run a more efficient business, where they recognise that the business model of the past does not quite work, are stepping towards us. If they step towards us we can share that benefit, put it into price for the consumer. That opens up more space then that can be used for the distinctive brands. And because they see an overall halo to the category, it works for all of us. The great news of where we have done these, we are creating cash profitability. So in a very tough environment we are creating cash profit, 3½%.

And you see some of these ranges live today. I have picked out cereals and some of you will know that is very dominated by a small company called Kellogg's. CP Partners which is General Mills, the third largest food company in the world. But actually look we can work with these guys to create win-wins. We actually took out 20% of the skews, taken out a load of the promotions. All of the savings have gone back into either proposition or price. So we actually improved our price position compared to the competition. We've got six new brands, targeting new areas such as gut health. And as a result we are delivering that higher cash gross profit.

And so if that area, the last bit I just want to touch on for the future is VCA. So I am quite bullish from all of the work we do with the likes of Mckinsey, Boston Consulting etc. We think we benchmark as leaders in this space. So we have looked at about £4 billion of our Own Brand COGS, 7% is a very good run-rate on that scale, it is a pretty big number. And what we are trying to do is change the structure of the value chain, what we describe from field to fork. Trying to look where we can eliminate waste. It takes time, this is not a negotiation, invariably it ends up in a negotiation, but it is not a negotiation in its nature. It can take six months, nine months to do the work to really understand these value chains. The good news is that we have still got another £2 billion to run at. So I suspect we will then decide to go back to the start again later.

And then to bring it to life, let's look at Spanish fruit. The traditional value chain has four steps in it. Actually all of the work was about taking out an entire step. So you get to three, take out a substantial amount of cost saving by removing that depot operation. You handle the fruit one less time, so you get less damages, less wastage, better temperature control. Actually it is the better freshness and quality for our customers. And actually they get another day's life as well. So that is where we want to go and we have still got a third of our Own Brand Business that hasn't been through that process.

So in summary, the exam question we have been trying to get right from customers from their feedback is address value, to address the items that they were taking out of the basket. We have gone harder entry price points and we will complete that work by the financial year end. We have invested in key high velocity lines using our Nectar database and we have punched harder in the area of the above the line with the support of our supply base. We believe that is absolutely sustainable in the longer term, (a) because we are not just going for short-term negotiations, we are trying to do the VCA, the value chain work sustainably in the long-term. We do believe and suppliers will feed that back, that we have the ability unlike others, to optimise our sales mix. This is an advantage with that very large affluent customer group. And we are a prime destination for investment. And that is all supported by the hard work from Simon's team where we can create those operational efficiencies not just cost savings, but efficiencies to reinvest in the offer.

So hopefully that gives you a feel for what we have been up to and I am going to pass you onto Simon who is going to take us through stores and customer proposition.

Delivering Service and Convenience
Simon Roberts

Thank you Paul. Good afternoon everybody. So I'm Simon, I look after the Operations and Stores in Sainsbury's. And building on what Paul has just shared in terms of the Product Proposition, we are going to really talk now about what we have been doing in our stores over the last 12-18 months to really think about how we can give our customers even better service and availability whilst at the same time facing into how we operate at a lower cost.

So the real core of the question we have been focused on is improving and creating a more distinctive offer and doing it more efficiently.

I also want to talk about and just recap on some of what you have seen in the store this morning. I hope you enjoyed seeing Hedge End this morning and much of the changes that we have made. So just to give you a real sense of what we are doing in terms of our proposition in store. And as it all then ladders up, why we now feel really confident we can give our customers an unmatchable service and availability experience in our stores.

So reflecting first on what we are doing in terms of our channels, Mike opened the session talking about being a leading multi-channel, multi-brand retailer. And at its heart, as we know our supermarkets and convenience stores are absolutely critical in delivering that. Over 90% of the food we sell today in the UK is sold through one of our stores. So in our supermarkets as you have seen in Hedge End, we are very focused on responding to the new missions that customers want to shop with us on. And particularly in areas like beauty and wellness, in value added food as you have seen in Hedge End today.

We are also of course rolling out and continuing to roll out the Argos store in stores, integrating that offer more within the overall supermarket footprint. And we believe there is a lot of opportunity three years on from the acquisition of Argos, still lots of Sainsbury's customers, somewhere near nine million of the Sainsbury's customers aren't shopping Argos today. So a real ability for us to drive cross-shopping in the supermarket, broaden the sales reach and fulfil more of the basket.

Of course we are rolling out concessions too, and you saw some of that in Hedge End and again that adds to the mix of the supermarket offer, creates more reasons for customers to visit our stores. And if we think about strategically where Mike started, which is against the acceleration of the German discounters putting more choice, offer and convenience in the supermarket is absolutely at the heart of why we believe we can answer more of those customer issues .

We have repurposed somewhere near 20% of the space over the last period of time and we have lots of plans to continue to invest in our stores and our supermarkets, both driving the trading intensity, but as I say, very importantly, delivering what our customers expect.

Now one of the key facets of our ability to drive the productivity in supermarkets is of course our online operations and you saw that in Hedge this morning. 244 of our supermarkets today out of the 608 that we operate run online operations. And there are two key elements to this. The online fulfilment in store of our orders is a very efficient way of running that operation. It also optimises customer choice. So we are now able to deliver to 98% of UK postcodes. We are now somewhere near 60% within the same day. We are seeing strong market leading growth in terms of our online operations and importantly we are making a profitable growth as well.

Now at the heart of that, as you heard from Nigel this morning, we have been absolutely focused on how the operations in terms of picking in store are working. And the advent of new technology has given us a real ability to take work and labour out of the operation, to repurpose that into the rest of the store and drive a 40% improvement over the last five years. To put some more specific on that, that is a 23% improvement in the last two years. And what that means is in the items we pick per hour, we have gone from somewhere around 116 to 160. So a real shift in the rate of productivity, but we have been able to do that at the same time as continuing to improve the service experience and also delivering to customers very importantly on time. And we measure picked in full, we measure on-time departures and we measure our productivity day in-day out in every single one of our stores.

So the combination here of giving a very strong customer experience as well as driving of course the efficiency.

And then the third of our channels in Convenience, now we do believe that we do lead and provide for us customers a market leading experience in Convenience stores with 825 Convenience stores today. And what you can see on this slide is really three key components. First of all a continued strong growth story. As customers shop differently, they shop more frequently, the locations of our Convenience estate are really working to our advantage. And you can see here both in terms of the growth we are achieving in market share gain, but also very importantly as we continue to optimise the offer, continue to look at the space and range in those stores, so too we can drive market leading trade intensity from our Convenience estate.

We will open about 13 stores this year, 13 stores we will open in terms of new locations. And we have seen many opportunities to leverage an advantage this Estate going forward. And Patrick in the next session will talk more about some new format thinking we are doing in Convenience.

Now at the heart of the Convenience mission clearly is giving customers brilliant service, great availability and the ability to get into the store, get what they need and get out quickly. And we are really pleased with the level of service improvement we have seen in Convenience stores. You can see on this chart that against all of the operational measures in our Convenience stores we have seen a real step on year on year. Over 12% improvement in our service measures since this time last year. And the particular areas that have moved on are speed and ease of checkout. And I will talk in a minute about some of the big changes we have been making in how we help customers checkout far more quickly in Convenience. So lots of growth, lots of reasons to believe we can go further in Convenience and a very profitable model for us.

So having reflected on our channels, I want to come back and just reflect on what we did at this time last year. Because it seems a long time ago now, but in fact it was this week last year that we launched in our Supermarkets and Convenience stores a completely new operating model for all of our 130,000 colleagues that work in our stores. And fundamentally we had to go back and look at how we could drive a better service at the same time as reducing our costs. And so at its heart we did a number of things.

The first thing is that we substantially reduced the number of leadership roles in our stores. So if you take a supermarket today, somewhere between 14 and 18 leadership roles in a store. Before we made these changes we were over 30. We used to have 20 plus separate roles within the store and we have now moved that as you can see on this chart to effectively five families within the store, which means that all of our colleagues are multi-tasking, are multi-skilled and that means we can be there for our customers when we need to be. So for example, I might start the day helping on grocery online, I might then work in the cafe. I might then work on the checkout before I finish my shift. So by moving the skills through the team it means we can serve customers more efficiently, but importantly we are not putting extra costs into the operation when we don't need it.

The other big change that we have made is to put the customer right at the heart of our operations and I will talk in a minute about the way we are listening to customers. So in stores by time of day and week, we can see exactly what our customers think. And a year on, you know it has been a really big change. You know I wouldn't want to underplay how significant this has been. We were the first in the industry to make this change and it has taken us some time to embed it. But we are now seeing really concrete movement in terms of our availability and service. And very importantly in terms of our colleague engagements, we are very proud of the engagement we have with our colleagues. Our colleagues do a brilliant job in our stores. But at the heart of being a great retailer is giving a great service to our customers. And so we have been really focused on how we make sure our colleagues feel really part of this change. We have got over 2,000 new leaders in the Business since 15 months ago and we really want to make sure that through great leadership our colleagues do a great job for customers.

And a couple of the key indications of the change, we are seeing attendance levels really step up. So we now have the best attendance in the industry. We are seeing multi-skilling really move forward and we are seeing our service improve too. And I will come back to that.

So I think that has really given us a platform now with that change in how we run our stores to really drive forward. And you heard a lot from David this morning about how we are simplifying the way we work in our stores, taking lots of task out of the store. Because of course the challenge is, how do we become more available for customers and not tie ourselves up in admin and activity that takes us away from the customer.

So we are simplifying the operations in the shop. We are using technology in a very different way to take task away from things that get in the way of what we would do for our customers. We are improving our service and availability, so that is a big change. And to give you a dimension of that, we have already taken about 10% of the tasks in a supermarket on a weekly basis out of what we do compared to a year ago. Massive change in the role of technology. That is both front of house and back of house. So as you have seen in Hedge End today, big change in the way our checkout platform is working with the rollout of SmartShop and the new Self Checkout hardware in our stores. But very importantly we are changing the hardware in the shop as well for our colleagues. So to make our new way of working really come alive we have rolled out at scale a digitised way of running the supermarket. And we'd all reflect on supermarkets in many ways as being a very manually operated process for a long period of time and we think we are really at the heart of changing the way that works so we can free up a lot of available colleagues to customers.

Which comes to the third big point, and Mike started this session talking about how we listen to customers. Since we launched Let us Know a year ago we have heard from 1.65 million customers. We are hearing from over 100,000 customers every period and we are hearing by store, by hour, by time of day, by part of the shop and often by colleague. And that means that our store managers now are absolutely focused on what our customers are thinking, seeing and feeling. And that is enabling us to really task ourselves. Where we are doing a good job, great. Where we need to do a better job, we are knowing that much quicker and much faster. And I would just make the point, I am not standing here today thinking we have done all of the work we need to do. We have made some big progress, but we see a lot of opportunity with this insight to go a lot further.

And then very importantly, to be able to do all of that whilst offsetting inflation. Of course within the store operating costs, with labour pressures, with pressures on the store operating cost lines and in this financial year we will arrest the impact of inflation in our store operating costs as a result of the changes we have made.

Now David talked at length I know this morning about Smart Store in store and I hope you enjoyed the session that you saw in the shop. I don't want to repeat too much of that other than to say a couple of things. The first thing is of course the relationship between driving productivity and giving better service. And over the last two years we have seen a 14% improvement in the productivity in our supermarket operations. And we have done that at the same time as improving the service we are giving to our customers on the key measures of friendliness, availability, knowledge and product. And we have done that through focusing on these four key areas. And I will touch on just a couple of them now.

So we talked about the importance of checkouts, serving over 27 million customers a week in our supermarkets and convenience stores, 9 million customers a week in our Convenience stores specifically and Clo I know has given you a real insight into how Smart Shop works in our store. We are very confident about this platform, because it is democratising the choice for customers where, when and how they want to shop in-store. They love the technology, they love the flexibility it is giving them. And it is giving us a real choice to drive SmartShop hard, but importantly also free up some of the labour and some of the cost that is tied up in traditional checkout operations.

So SmartShop will move out at pace, we are in 300 stores today, we are really pleased with the level of step-up from customers. Customers are very quickly wanting to move into that technology because it is giving them more time back too. It is giving us lots of advantage on increased transaction, value and speed. And customers are rating the level of service in the SmartShop experience well ahead of what we expected. As I say we have rolled out new self checkouts too, of course more customers want a self checkout now, not just on Smart Shop, but in the self checkout lane too. And you can see there as a result of the technology platform we have put in place, in terms of improvement and speed, a real shift in terms of both the speed and ease of checkout.

And I just want to pick up from this point at the end here about the efficiency. Just to be really clear, customers we think want to move to self checkout whether it be through a self checkout till or SmartShop. And for every 1% of our volume we can move to a self checkout method of operation, we can look at a 4.6 million level of efficiency. Now in some cases we will redeploy that into service, in other cases we will take that as an efficiency within our P&L.

Connected Colleagues, this is really exciting I think because in the past every piece of task in a store was driven by a piece of paper or a folder or a piece of administration. And what we are doing now is using technology in the palm of the hands of our colleagues to re-liberate the way the store works. And you saw this in store this morning, it is giving us lots of benefit in terms of task. It is taking real labour out of the store. But it is also driving consistency. And one of the big challenges for any scale retailer is can we land the things we want to do in 1,400 plus stores at a point in time really consistently? And this is enabling us to do it because we can talk directly to our colleagues in the moment and make sure we are delivering what our customers expect when and where we want to make it happen. And you can see the big change in management time and in colleague reduction as we talked about earlier on. This is just the start of what we think we can do, really reducing task, freeing up our colleagues to customers.

Now a year ago when we put the changes in place it was disruptive for a period of time. We took a very conscious decision to look at our leadership structures and our colleague contracts at a point in time. And we did that because we didn't want a long protracted period of change. And I think it has definitely stood us in very good stead, because a year on we have now completed those changes, we are seeing a shift in our availability and in our service at a point in which our other key competitors are just starting out on this journey. And just having been through this period of change, this is highly complex change to land. Of course we are changing contracts, we are asking colleagues to work differently, it is very, very demanding to lead the change. We have done that and we are now getting the benefits from the other side.

So product availability, still more we can do, still stores where we can do a better job, but overall our availability has stepped up significantly year-on-year and we are now ahead of where we were before we started the changes last year. By the measure of the gross of the Grocer 33 which industry wide would be seen as a good assessment of our relative availability, we are now leading the industry again and we are ahead of all of our key competitors.

Connected Buildings I think is really exciting and David I know showed you this in store this morning. This is a real ability to take costs out of the operation and do things more efficiently, linking all of our assets and energy management together and over the next two years we see £40 million of savings. This isn't about taking labour out of stores, this is about just doing things much more efficiently and using technology in a different way.

So having thought about what we have done on our operation, we have taken real cost out of how we run. We are leading our stores must more efficiently and we are really focused on how we do a better job for customers.

So coming to the investment in our shops. So we are making really significant headway in a programme that we have launched this year to focus on the key parts of the shopping trip, whether that be cafe, produce, bakery, some of the key parts of our store that customers really expect us to be leading the way. And this year over 250 stores will see investment in these areas and already we are seeing a satisfaction level of over 1.4%. This week somewhere near 55 supermarkets are having this kind of work happening right now. So we have really stepped up the programme. And when you link it to the new growth initiatives that Graham read out this morning, we currently have the biggest programme of investment in our stores that we have had in a long period of time, in fact well ahead of where we were at the height of the Argos store in store programme.

So Beauty transformation you have seen in store today, I hope you like it. We are really pleased with the progress it is giving us. Strong growth, customers traditionally going elsewhere to buy those products now buy them in the Sainsbury's supermarket. Of course the new food service areas that we are rolling out at pace as we re-purpose the value added part of the store. Big shift in terms of Clothing and General Merchandise and of course as we have talked, the further rollout of the Argos store in stores. So 289 Argos store in stores today, a further 17 in the second half of this year. And as I mentioned before, a big opportunity to convert more Sainsbury's shoppers particularly to shop in the Argos channel.

One of the particular points Graham made this morning is we are able to put these interventions into store now without causing customer disruption which is very important. And we can pinpoint specifically what are the right composition and elements to put into each store, thereby driving significantly higher returns and faster payback.

So if we link all that together we are, as I said a few minutes ago, listening to customers in a very different way. And that is because we really want to understand where we are doing a good job and where we can improve. And as I said before 1.6 million customers talking to us across the 16 drivers of our Let us Know measure. And you can see that we have improved particularly in our checkout areas, as highlighted here, and also in some of the key colleague measures, for example friendliness and knowledge of colleagues. And we are also starting to see a real step-up in the perception of our store environment. We have still got a long way to go and as that programme continues this year I would expect this performance to continue to build. This year the service in our supermarkets at this point in time is 10% higher than it was at this point last year. So the level of highly satisfied customers has increased 10% year-on-year.

The other way we look at services, we also look at how our customers would rate our service position, our experience in relative terms compared to our key competitors. So on the next two charts you can see the relative progress we have made since the earlier part of this year into the summer in the areas of the store fabric and infrastructure. And as I say we are in the relative early stages of the interventions we are making, but we are pleased with the progress that we are seeing in how customers now rate us and we think this will continue to build as that programme rolls out.

And then similarly in terms of the colleague measures, a year on from the big changes we made last year, customers in Sainsbury's expect us to have the friendliest colleagues. They expect us to be most available when they shop with us. They expect us to have the best checkout operations. And as I say, a year on from the changes we have made, we are absolutely determined to build on the new platform we have put in place. Our colleagues have done a fantastic job in helping lead through a big period of change and we expect to see this position continue to improve.

So it is interesting, this is the time of year where we do our set up for Christmas and I have spend the last week to ten days in store manager road shows up and down the country with all of our store managers, thinking about our plans for Christmas and how they are feeling about where we are up to. And one of the things we talk about is the progress we have made, but also the opportunity we still have. And in the business of 1,400 supermarket and convenience stores there is a huge opportunity to build further on our consistency. So with that data of day and time of week, we are now looking particularly in each store, where exactly can we go further to improve the service that we are delivering. And particularly we are focused on late nights in this example. But the point I would just want to draw out is having put in place a single contract with all of our colleagues, having now put in place multi-skilling, having really skilled up our management teams, so now we can really drive on the way in which we focus and deal with the parts of the week when we are not as strong as we need to be.

So in summary, I think a year on we really have made a fundamental change in the way we work that gives me a lot of confidence we can build on our store operation to give great service for our customers at lower cost. The challenge in this industry isn't it, to distinguish what we do on service and offer, but make sure we arrest the cost of inflation and I think we have already proven that we can do that. We see loads more opportunity to keep driving service and availability and our teams in our stores are really focused on what they are hearing from our customers every day.

So with that, thank you for listening, I am going to hand over to Patrick now who is going to talk about our Property Estate. Patrick.

Driving value from our estate
Patrick Dunne

Thank you Simon. Hello everyone. My name is Patrick, I look after the Group's property procurement and help develop the plan for cost transformation. I joined just under two years ago, having spent previously ten years working with Stefano Pessina across the world for ten years as I say running his property and cost agenda there. So quite excited to have joined. I took over property about a year ago.

Today I want to talk to you about why we believe we have an advantaged estate. Mike said many companies don't talk enough about the physical assets which are probably our second largest cost base, if not our largest cost base in the business. So I am going to talk to you a little bit about the Portfolio, give you a little bit of background. Why we are getting the basics right and I will then take you onto why I believe we have very strong plans for growth and I will take you in detail into that. Why we believe we can generate even further value mainly through our mixed use development or freehold estate. And then I will talk about why we need to become more efficient as well and what that means for the estate.

Starting with our locations. On the left you will see where our current estate over indexes above average for grocery spend across the UK. On the right you will see where the UK population over indexes over the average spend TDP in the UK.

So we are already in the right places, the affluent part of the country. For supermarkets, 72% of the population can reach a Sainsbury's supermarket in under a 15 minute drive. 21% can reach us within a five minute drive for a Convenience location.

We have over 2,030 stores, 53 million square feet, on average roughly 28 million square feet of sales space, changes day by day as you can imagine. But really pleased with the way we have historically managed the estate. I will talk about our legacy pipeline in a moment but for our existing estate, 38% of our space is owned, 50% of that owned is supermarkets, the rest, as you can imagine across our Convenience and Argos as leased.

And then if you look at our leased estate, what do we try and set out to do? We try and do two things fundamentally. Give security of tenure where it is needed, but flexibility where we think we will need it also. So our supermarkets we have an average of 14 years lease term. That is a good secure term, but in the life of a supermarket it also gives us good flexibility should we need it. Convenience 8 years, predominantly a leasehold estate. Again the dynamics of a Convenience estate if you look at a Convenience store, the 10 year lifecycle of the store, you can have a very successful store in 10 years, it can actually become less successful. So that helps play into that strategy and of course with Argos, predominantly playing into, and I will talk a little bit more detail on Argos, but playing into our store in store strategy, 4 years gives us suitable flexibility for the store in store strategy, but also any change in market dynamics allows us to act pretty quickly should we need it.

So all in all historically and today, a very well managed estate. Closer to home with Argos, you know we are very proud we have over 1,200 points of presence for Argos, but more importantly since the acquisition we have reduced our freestanding estate by over 25% since acquisition. So we have grown our points of presence substantially, but reduced our expensive freestanding estate. So much so that we have increased our UK population within a 15 minute drive of an Argos from 82% to 86%. Again, and I will talk in more detail in a little while, that is core to our strategy, increase access to the UK population, lower our operating costs by so doing and bringing more of our business inside a Sainsbury's supermarket so our customers have more missions. So again another very advantaged estate. Remember, very flexible leases that allows us to continue our strategy and act quickly should we need to.

So closer to home, I was tasked just under a year ago by Mike and the Board to look at our estate and find what is our future five year plan and beyond. But in any estate you need to know you are getting the basics right. We have a very strong culture on our corporate responsibility. I will talk a little bit about that, but making sure we continue on that where it makes sense and making sure that the capital that we are spending every year particularly being the Procurement Director as well, that I am driving maximum value for money for that spend. So Graham and I, Graham will have talked to you this morning, you know, I will talk a little bit more about the scale of our interventions in stores this year and how we are spending that money.

I will then go onto growth in more detail about new space, quite topical, but I will give you confidence as to why I believe we will have very successful new space openings and how we are making the existing space more productive. Value creation, we have a very strong freehold estate predominantly in great locations in London and a proven heritage of how we have taken a number of those schemes to market. I will give you more detail on how we are going to do that over the coming 5-10 years.

And efficiency, you can't talk about growth and value creation and not actually address your existing estate and the performance of that and making sure you are pruning the bottom so that we can continue to invest in the top of the estate.

This year alone we will do 10,000, just over 10,000 this week, 10,000 store touches that are projects, you know historically, as Graham may have said this morning, we were always doing large stores and we were now on a 10-15 year cycle. Now we are doing a lot in every store. 10,000, we are spending over £200 million. Of the discretionary spend of the £150 million with a very strong supply chain reinvention and a very strong procurement approach we are seeing upwards of 10% improvement on our capital investment across the estate. As I say we have touched 450 supermarkets, 200 locals and 250 Argos. So that in itself, you will have seen, yes today we will continue to do single large stores where it is needed, no more than probably two or three a year. Historically we will have done a lot more in any given year, maybe 10 or 15. But more and more this is the future so that we can be really relevant to customers and bring them in real time the offer but again doing it in a cost effective way that gives great returns.

One of the things I am really proud that I have inherited, and the business you know is very strong in this, is our CR&S Agenda and I will talk to you a little bit about active management. Since 2011 we have spend £260 million in energy and carbon reduction which goes on talked about sometimes in many businesses. The carbon disclosure project, and if there was one thing I would ask you to do today, look up what that is. It is a global programme where companies have to or do go and record what their performance is and then they are assessed. For energy, Sainsbury's for five years in a row has been A graded. Only 137 companies around the world are A graded, only seven in the UK, none of them in the space that we operate, no retailers. Sainsbury's is the only retailer that has a Grade A. The same for water. Only 31 companies around the world have got a Grade A, we were A minus, but by far the highest scoring company in the UK. Again it plays, but these are investments that have also saved resources, saved energy and saved cost. And we have only got started, we have a lot more to do in that space. And over the coming years those investments will continue to accelerate and help reduce our carbon footprint but also give us greater returns on our investment.

Now coming into the growth segment, it would be foolish of me not to address what many people sometimes fail to address is what we call the legacy pipeline, and I am pleased to say we don't have one. Since 2014, 72 pipeline locations that were mothballed have been tidied up. 16 of those stores we opened, 10 we want to progress, we believe now we have got to a level that the next 10, the final 10 sorry, will be ones that we will open over the next 5 years. Two of them will open this year, one will open next year. So we are not rushing at 10 openings, we are doing it in a very considered way. For the 46 that we have commercially resolved mainly in the last few years, we have generated £82 million of cash and we have the final 6 schemes in the market for sale to generate an additional £20 million hopefully this year. We won't sell them at low cost, but we are hoping to sell them in this financial year.

So no legacy pipeline. The 10 schemes we have we will now build out and I will talk to you a little bit about where that comes. We have identified through our Estates Review, our Portfolio planning that there is an opportunity across the UK upwards of 300 locations in the UK for what we call large Convenience stores or internally it is a community hub. We don't believe there are 300 suitable for Sainsbury's, we believe there is 80 of them that would be right for Sainsbury's customers and we are planning to open somewhere between 16 and 20 in the next 5 years. Again we are not rushing out there to open lots of space. They will be very considered units, quality units. And what are they? They are 3,500 upwards to 12,500 square feet, well ranged Convenience but also bringing into it our concession partners where it makes sense, tailored to that community. And I will talk a little bit more about something we don't always talk about is how successful our concessions business is within our

Sainsbury's estate. On top of that we have new formats, Food on the Move and things like major city infill's, we are looking at our conurbations where we have very successful Convenience estates and we are also identifying opportunities where we can drop in even smaller Convenience stores. And Mansion House in London, which will open in February is an example of that.

So a very active pipeline, but our core Convenience is what we are very successful at, will continue as well. This year alone we will do 13 Convenience stores with two extensions, two major extensions, so let's say 15. And for the foreseeable two years I have a very active pipeline ready to go. Whether we do 15, 17 or 20, we will decide as we go forward, onwards, but you could look at, we believe there is 95 opportunities in the next five years for us in standard Convenience.

Remember I told you we had 21% of the UK population within a five minute drive, and it is a very successful business, well we will now work up through that 21% and get it further up where it makes sense. There won't be mass openings just for openings sake, there will be quality that gives great returns and we are not opening at low end sales values per week. We are opening at very considered levels that we know will be successful, keeping to the format that we have today. So that is Convenience, or large community hubs. I will talk to you about the supermarkets the 10, the 90, 95 larger Convenience.

Concessions, another area of growth, again we have over 650 major concessions in our stores, 4,000 are minor concessions, but they are generating just under £25 million a year. We are in very active dialogue with a number of our existing partners, Spec Savers, Timpson's, very quality brands and we have an active list of over 50 other target retailers, some of which we are bringing to market as we speak, that want to grow with us. Again in a considered way, missions that will increase the missions within a supermarket. Yes they will also bring a halo effect, but what they also do is bring over forecasting £20 million of additional income over the next 5 years.

My challenge to the team is can we grow faster, but will do it in a considered way so that we are not just rushing in there and putting in any concession partners. They have to be partners that actually complement that locality and that supermarket. Just for evidence, we have over 46 Spec Savers as we speak. We have quite substantial Timpson's footprint already and these are services and products that our customers are asking us more and more for.

So in summary, for growth new Convenience stores, large and small, we see £70 million plus of profitable growth there. We will build out the rest of our supermarket pipeline. They maybe smaller supermarkets, they may not be what is traditionally larger footprints, but they will be tailored to that local market and we will have further concession income with our existing partners and a number of new partners that want to join and see the success already of a number of pilots that we have taken on the way.

So that is growth. Looking closer to what we call value creation as part of this strategy, we have a successful track record of developing our freehold estate. We have developed three to date. Most recently we have not quite finished, but in Selly Oak, some of you may have gone up to Selly Oak, but that was a mixed use development created by us. Closer to home in London for most people they will know Nine Elms. As an example we had the freehold site. We went and got planning permission to redevelop the site into a new supermarket and 737 new homes. We then sold it into the market on a competitive basis among a selected number of developers that we wanted to work with, because not any old developer, we wanted to make sure that they could deliver a store that would be in keeping with the way we wanted to trade. And we got a new store on a 999 year peppercorn rent, and proceeds of £66 million. That is one example of what is a pipeline that has 12 future opportunities over the next 10 years. As you say, we have a very strong advantaged estate in London and five of those in the near term 0-5 years are in the London M25 area. They we are confident will bring £150-200 million. In total over the next 10 years we see £270-350 million, and yes I am being a little conservative with those numbers. They are subject to planning, but the first 5 schemes are well advanced and we understand, we know we have good confidence to bring these in some form or fashion to fruition. So that is value creation.

If you are going to talk about growth and you are going to talk about value creation, it stands to be sensible to be remiss of us as a business not to look at the existing performance of our existing estate. We have always looked at cash contribution in a number of service related elements. But we have overlaid it now with stricter, more stringent performance metrics. So we have undertaken a review of the entire estate including Argos, we are looking at new measures of profitability, minimum expectations now and for the foreseeable future. Rent cover and the stores ability to pay its rent. Anything less than two times cover gives us a worry. Cash generation, its ability to generate cash and of course as Mike said earlier, the return on equity. The return of capital employed. What does that do? It allows us then to put a programme of improvement in place. And the improvement is a cross functional, mainly led by Simon's teams, Store Operations, myself, Property, Graham's team in Arranging. And we have decisions to make whether we invest more capital in that store or whether we change the format of that store or the range, look at how our people need further training.

But in the end if we don't have a suitable path to improve those measures we will take the decision to close. So today we have announced for supermarkets, we are proposing to close between 10 and 15, and convenience between 30 and 40. People say, have you a definitive list of stores? No we have a list of stores that we are still working through and we are not concluded yet with the finite number at the end, but that is the range.

Looking to Argos, Argos is a much easier story. As I say we have over 1,200 stores, I talked earlier about how we are trying to improve our cover to the UK population. 602 of those stores at the end of FY18 Financial Year, were freestanding. But we are going to open a further 80 store in stores and that is 80 beyond the initial acquisition target. So we had a very success synergy programme with a very successful programme of store in stores. But as we look closer into our store network we can see further opportunities over the next few years in return. Not 100% linked to the store openings, but generally linked. We will then have the ability to close 60-70 freestanding stores over the same time period. So if you are asking yourself what does that mean? A one-off cost for closure and implementation of a range between £230 and 270 million. The cash element of that, £30-40 million, and that will generate an ongoing EBIT benefit of £17-23 million for those closures. All to be executed in a two year period starting this financial year.

Now as you travel down a road in the property world whether we get to 78 or 80, of these things to be executed, but that is our intent as we set forth over the previous few months and by the end of the next financial year.

So in summary, we already have a very advantaged estate. We have lots of room to grow. We are quite proud of our corporate responsibility investments. We will continue to invest in the way £200 million a year bringing new missions. We have a very successful concession business and we will continue to grow on that because that is what customers want from us, which helps us with our space, productivity as well in store. It also generates a great halo effect for the rest of the store. We have value creation, which will generate cash and proceeds, it will help us fund our growth if that is where Kevin dictates we want to go. And in the end we are willing to close stores after we have looked at improving them in a way that as the market dynamics change we are going to face into those low end estates and we will close them if necessary.

Hopefully that has brought a little life with a bit of colour and we will be taking questions later. So I am going to hand you over to Kevin now who is going to talk about our cost transformation agenda.

Cost Transformation
Kevin O'Byrne

Thank you very much Patrick and I was pleased to see Patrick raising the target for mixed use development funds there, so that is a good start to the afternoon. You heard Mike kicked off the afternoon talking about the challenging environment we are operating in. We all know that. And Paul was talking about the need to invest in our offer. So in that context it is really important that we have very tight projects to reduce the cost base of the business. So I would like to touch on just two areas. One to talk about our proven track record of removing about £120 million a year out of the business which is our annual cost inflation. And then secondly talk about our significant opportunity to take further costs structurally out of the business as we combine the Argos and Sainsbury's businesses together and this is unique to us.

So onto the first what we call sort of business as usual savings. This is something that the business is very adept at. We spend a lot of time looking not just at the year we are in, but the year ahead. And I thought I would just bring that to life for you by just talking about some of the savings that you have seen us taking out of the business in the year to March 2019.

Now there are always lots and lots of projects going on in this space, some of them saving maybe as little as £50,000, but they all add up, they are all important. But we also have every year some large projects that take out substantial costs in significant numbers. Simon talked about the work we have done in the store structures, changing the store structures. Hopefully you saw a lot of examples with David in the store this morning where we are using technology to take out task, take out cost without impacting service, in fact improving service because we get our colleagues on the stores and out of their offices in front of customers. That saved us £31 million last year and that was just the in-year saving. The annual run-rate of that is larger.

We have an award winning procurement team who work closely with each function in the business, so look at all our supplier contracts for what we call GNFR. So these are the products that we don't sell to customers so it is uniforms, it's vehicles, it's IT services, it is energy etc. And that team generated £50 million of savings working hand in glove with the business.

Nigel talked you through the work we have been doing on grocery online in store today. We are really, really pleased with that, giving great customer service, much more efficient and saving £17 million last year.

Patrick just touched on our energy initiatives which we push very hard, that saved £5 million in the year. And in the year we also materially changed the way we support our stores with HR human resource support, taking out substantial savings.

So that just shows you the kind of things we are doing and these are sustainable savings that are bedded into the business and then we have got line of sight of savings probably 18 months ahead we are working on savings to generate that £120 million a year to hold our cost base and cover inflation.

But on top of that for the reasons Mike talked about earlier, as we integrate the business and put the Group together, we have line of sight of further material cost savings, structural cost reduction of an additional £500 million over and above the annual £120 million.

We have analysed our cost base, we have looked through it in detail and we can see about £5 billion of costs in what we call an addressable cost space. And we can see line of sight of a 10% reduction across those various cost buckets.

And this isn't a completely new thinking, we are well advanced in many areas in our plans for this, and in some areas we are just starting with new plans. But you can see, to give you a sense of the work that is going on to deliver these costs and this is over a 5 year period.

Now on some areas as I say, very well advanced technology, digital is a good example. We have put the teams together with Argos and Sainsbury's. One example, data centres, we have 12 data centres. In many areas we are overly complex. We don't need 12 data centres, so that is an area we will go after.

Clodagh will talk later about the great work we are doing on digital. We can do it once, we can do it for financial services for Argos and for the Food Business. So a lot of areas we can get savings from. Another area is Property, Patrick talked about. Now as well as going after Retail property that we don't think we need, there is other properties across the business, the data centres is a good example. Whereas we put the businesses together we need less real estate and we can take out structurally take out fixed costs.

Another material area will be logistics and supply chain as you can imagine, having two independent supply chains and logistics operations across the island you can see lots of opportunity to do that. So very clearly a significant opportunity. Detailed plans in place in some areas and being worked through in other areas and clear line of sight of opportunities to remove those costs.

Now I know many of you in the room would like us to get into more detail on those, clearly these are very sensitive programmes so you will understand there is a limit as to how much we can say about them at the moment. But we have raised our ambition, we want to structurally reduce the costs in the Group and we can see how we can do that and take between 150 and 200 basis points of cost out of the business over the coming years.

So just to wrap up, we have a track record of taking out £120 million a year to cover our cost inflation and we will continue to do that. We have a significant opportunity on top of that to take out structural costs out of the business and that will allow us to support the investments that Paul talked about earlier in our offer to support our customer offer and protect our profit in the business.

That was everything I was going to cover on costs right now. We are now going to have our first session of Q&A. So we are going to have a break. You will be also glad to hear that we will have a cup of coffee and a break for toilets etc in about 15 minutes. But Mike is going to take the first set of questions. We will cover financial services, Nectar and digital and wrap up after and have a second Q&A session after that.

Mike Coupe
So the less questions you ask the faster you get a comfort break and the faster you get your coffee. So the floor is yours. As James said, maybe if you just have a hand up and who you are and then we will pass the microphone to you. So at the front, Andrew.

Question and Answer Session

Question 1

Andrew Gwynn, Exane
So it's Andrew Gwynn from Exane. I will go for one question for the moment, maybe more a bit later. You talk quite a lot in the results about going after a cost opportunity which was in effectively cost of goods sold. I think in the slides presented before it was a little bit more collaborative, but is that still quite a substantial opportunity do you think?

Answer: Mike Coupe
Yeah maybe Paul would like to reflect on it, but we have talked previously about the programmes that we run, not least things like VCA which will allow us to structurally change the way that our supply chains work. So looking for where value losses happen and how we might restructure and rebalance our supply chains to allow us to get the benefit from that. You know there are straightforward negotiations, there are negotiations with a large branded suppliers. And we think that there is a substantial opportunity. Now Paul maybe if you reflect a little bit more on the question.

Answer: Paul Mills-Hicks
Yes, so to build on what Mike said, I would characterise it as anyone can save some costs in the short-term and conflict doesn't really work. So when I was younger and more dynamic I thought conflict was the way to negotiate. Everything I have learnt in this industry is if you want to take out cost, you have to do it through efficiency. And efficiency is fundamentally about collaboration with suppliers and you have to look at the end to end cost. So the way I characterise it is where you end up with a conflict, we win, they those, they win we lose. Or you just see it move around the industry so you get competitor winning for one period, we win another period. That is really tactical, it does not create long-term value.

So where we are trying get to with the way we are working is can we take out inefficiency waste with our suppliers. And invariably you are much better off doing that in a collaborative mode. In some instances you just can't do it. There is too much capacity in the industry, they are maybe a third already in the discounters. The discounters pay a good price so it is not that our COGS are bad. And therefore you are much better off having a direct conversation, which is, this isn't going to work, let's not spend any time on it. So all my learnings would be is we have evolved into a world where there isn't that much profit to go round for us and the supply base, collaboration is the only way to get structural advantage rather than just tactical here and now.

Further question
Am I right to think that tone has changed? I think the tone of the full year results was always quite aggressive, but the tone now is much more relaxed, but is that maybe my misunderstanding?

Answer:
I wasn't aggressive, I am a really nice guy I am not aggressive! I do think the one thing I would say that has changed in our industry in its totality is I think is the dawning realisation from the big brands that they are under siege from both Own Brand and smaller and more nimble brands. I think that has definitely changed in the last 3-4 years. I think there is a realisation that sometimes just sending our two teams into battle is a zero sum game. So I do think, I am not sure just between the yearend results and now, but I would detect that in the last 3-4 years there are different conversations and there are more professional conversations that are being had. Because ultimately for our industry the only money, the only profit we make is what customers are prepared to part with. And then the only question is how you split it between yourselves.

Question 2

Rob Joyce, Goldman Sachs
Rob Joyce, Goldman Sachs. A couple from me. So firstly, just to put some context maybe around the cost savings and the structural cost savings. So first thing, am I right in understanding it is sort of £170 million a year is recurring, £120 million a year, sorry, so that is £600 million and then you have got the £500 million structural on top? So just 1.1 over five years. Just to understand how that might drop through, could you put that in context of the sort of previous five years in terms of the levels of cost saving synergies, structural costs you have taken out of the business maybe over the last few years?

Answer: Kevin O'Byrne
Well the £120 million will happen every year as you would expect. And the £500 million we would be looking to do that largely, a fifth, a fifth, a fifth, because clearly if we weren't we would be getting concerned that we are not getting there now. Clearly on some of those things there is a bit of a slower burn. I probably shouldn't get into the details, but there are some things where we need to take some actions and you would take the cost out in year two and year three.

Further question
Would I be right in thinking if I add the sort of last five years disclosed cost savings plus the Argos synergies, it is roughly the same number next five versus the last five, if you have done some £200 million a year for the last five years, Argos synergies?

Further answer: Kevin O'Byrne
Yes I think the difference with this additional £500 million we are talking about is the structural nature of it, because as we bring the business together we can see line of sight of taking fixed cost out of the business. So that would be, and taking our cost as a percent of sales down, we wouldn't have had that ambition.

Further question
Thanks very much. And just on the recent, the slide you discussed on promotions, it does look in the recent weeks we have seen some uptick in promotions and some more marketing going in as you guided to. Is that something we are going to see drop back in the second half of the year given the guidance for a step-up in profitability or how should we think about that?

Answer:
We wouldn't possibly disclose that would we, it would be giving too much away. I mean in the end, to the point that Paul made, the realities our competitors have stepped up quite significantly their level of promotional activity and that has happened over the last 2-3 years. We believe that we should be running a sustainable underlying value platform for our customers. And so we have gone down the road of trying to reduce the amount of promotional dependency, but we also accept that we have to be more competitive in the marketplace in which we operate.

So hopefully that gives you some sense but you know in the round we can manage it and the point we are trying to make is we can manage it within the mix whether that is directly through cost of goods savings, our relationship with our suppliers and the fact that broadly speaking, during the Asda transaction the large branded suppliers were less likely to come to the table for obvious reasons. And last by no means least, a combination of underlying cost savings and structural cost savings in the organisation overall.

And in the round, the point we would make today is that should give you confidence that we can protect the underlying earnings of the organisation because it is still a very competitive market, it is still pretty brutal out there. The discounters are prepared to make less money in the medium term and continue to open lots of shops. That will continue to put pressure on us. But we believe we can protect the underlying earnings, cash flow and ultimately the dividends and debt reduction that we talked about.

Further question
Specifically on the marketing?

Further answer: Kevin O'Byrne
We did say we would put a bit more marketing for the first half because as we did the changes on the offer with the new products etc, we needed to tell customers about, we don't see ourselves having to replicate that in the second half.

Rob Joyce
Thank you.

<u>Question 3</u>

Nick Coulter, Citi
Nick Coulter from Citi. Just to follow-up on Rob's question actually. On the 120, is that enough to offset, as you know inflation, I had a higher figure in my mind from previous presentations?

Answer: Kevin O'Byrne
Yeah we talked about a higher figure before because in one year, as we did the wage increase, the 15% wage increase we did in September 2018. So we talked in that year I think in one of the presentations about £200 million, that was a one-off if you like. But the underlying run-rate of inflation is £120 million.

Further question:
Okay, so that covers it effectively?

Answer: Kevin O'Byrne
Yeah.

Further answer:
Well one thing it is worth just reflecting, over the last four years we will have effectively given our colleagues not far off a 30% pay rise in 4 years and after our cost of goods it is effectively our second largest cost. We are now well ahead of the market rate, so in effect we go back to a much more normal scenario of effectively wage rises in line with inflation without predicting exactly what that looks like in the future. Our competitor will have to catch up, so one way or another, whatever the change of Government is, I am pretty sure we will end up with a headline £10 an hour wage rate. We are at £9.20. Many of our competitors are significantly behind that. And you know there's a lot of costs associated with that which is now embedded in our cost base. We have done it, we are now in a position where that effectively acts as a source of competitive advantage as others have to catch up with us. I mean Waitrose are paying effectively the minimum wage at the moment. That is the kind of delta which would have been unthinkable even 3-4 years ago.

Further question:
And lapping that inflation, is that the key factor that gives you line of sight on being confident in consensus for the year?

Answer:
It is one of the factors, I mean in effect we don't have to face into the next wage round until March 2020 which means effectively for the rest of this year, as of literally this week, we are at zero wage inflation for six months.

Further question:
Just one tactical one if I can. The thing to Paul, on the price index, is that volume weighted that price index that you are moving against one of your competitors?

Answer: Paul
Yes so we volume weight for our volume. So as you know someone else could weight it for their volume and particularly where brands switch between places, you could actually have 4 retailers all saying that they are the most competitive. That is genuine data, 15,000 skews volume weighted rolling basis for us.

Nick Coulter
Thank you.
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<u>Question 4</u>

Andrew Campbell HSBC
Andrew Campbell from HSBC. Just a quick follow-up on that one Paul, has there been any change in the 15,000 skews over the past few years or is it always 15,000?

Answer: Paul
It's around 15,000. Mike set it up actually, so this is all Mike's creation, it's brilliant, really love it. So it is around 15,000, it rotates. We are actually really excited, we are trying to use a matching tool. So we are going to digitise the business, when effect we can web-scrap all of that and automate it. So it is 15,000. We manually match it every single week to where the matches are. You get errors, a number of you will use brand view. We think that is only about 60-80% accurate to what we do, so we scrub that and Graham Bigot, who you met earlier today, his team scrub that. Ultimately where we want to get to is to automate that and then ultimately what I want to do is give that to all the suppliers so they can see their own match and so you can see the direction of travel, when I talk about professionalising what we do as an industry, that would be the directional travel.

Further question:
Then on the cost savings, this sort of £500 million structural, should I be thinking about that? I suppose it is sort of building on Rob's question around drop-through, as effectively it sort of underpins your ability to compete for five years and invest a bit in your offer, and anything that is left sort of?

Answer: Kevin O'Byrne
I think that is, we will wrap up at the end and just talk about what this all means financially, but I would be thinking about it as something to underpin our offer.

Further answer: Mike Coupe
The fundamental thesis is, within the core business, and by that I mean the general merchandise, clothing and food business, we believe we can protect, grow our earnings over time, maintain cash flow dividend, pay down debt etc and will wrap that together. From a share point of view, you know if you bought the shares today you would yield 5% and we would start with the premise that that would make it look remarkably like a bond. If you believe some of the other things we will start talking about and some of the things we would have demonstrated to you in the shops around how we might utilise data differently, the earnings potential in the Bank, some of the other opportunities that we have to grow our real

estate is another example, then you might start to believe there is some future earnings growth above and beyond protecting the core. And that is the way I would think about what we are describing to you today. What we want to do is give you reassurance that we can afford to pay to play in the core competitive part of the market, because whether we like it or not, as I said at the very beginning, the discounters will continue to add capacity. The digital players will continue to add capacity and we have to be in a position to do everything we can to maintain our competitiveness in that environment.

Andrew
Thank you.

Mike Coupe
Right, we will do three more questions before coffee and then there is an opportunity at the end where any residual questions we can hopefully address.

<u>Question 5</u>

Serhat Birbilen, Fidelity
Thank you for the Presentation. I have a question on availability. I mean there was a charge showing the online availability, but I am curious about the in-store availability, has there been any improvement there? I am a Sainsbury's shopper and the shelves, in Pimlico, it is always empty. So I was just curious if there was any improvement, any changes there?

Answer: Mike Coupe
Well Simon maybe, I will let Simon answer the question, I think he did in the shop, but hopefully we can give you some reassurance. And you can tell us which store it is and we will let you fill in and let us know as well.

Further answer: Simon
Definitely, absolutely. There are always stores where we can improve and definitely we will take a look at Pimlico. The data that I shared shows our overall availability in terms of the way we measure it. The other key metric I would draw upon, is what our customers say. So 1.6 million customers have given us feedback on our availability over the last period of time. And if you look at the level of highly satisfied customers, it has stepped up significantly year-on-year.

At store level, just to your point, and I think, without going into the specific detail of Pimlico, that would be one of the stores where our trading profile would be a bit different to the normal, so there is definite opportunity to improve there. But overall in terms of when I look at availability year-on-year, at the corporate level it is moving along. When I mention the Grocer 33 measure earlier on today, and I think industry-wide that would be seen as an established measure of availability. Last week we were at 95.9% and that was 0.6% ahead of our next nearest competitor.

So lots of opportunity to keep improving it. You know and I think the balance between availability and waste is of course important. We want to make sure we optimise fresh food availability, optimise freshness, but at the same time make sure also that we are managing our waste.

So we will pick up on the Pimlico point, but absolutely be assured we are on getting the best availability in the market, thank you.

Comment
After Ladbroke Grove which is my local store!

Question 6

Clive Black, Shore Capital
Clive Black from Shore Capital. Thank you for the day and all the work the team put into it. And there are a lot of moving parts to think about. But I just wonder, looking at this morning's statement, the key messages you are saying today is we should be expecting a relatively flat outcome at an earnings and dividend level for the next 2-3 years. What struck me was you were talking about net debt doing down by £50 or £150 million over the next three years, and the pension contributions go down by £50 million per year now. Does that mean that you know literally the rest of the business, all this work is basically going to be flat-lining? Is that the core message?

Answer: Mike Coupe
I think I would frame it slightly different to that. The first thing is we want to give you confidence that we can maintain, if not slightly grow the earnings of the organisation through the core channels that we run today. And there is a lot of examples we can give. And like all of these things, you know if somebody starts the mother of all price wars tomorrow, if the economic environment changes, there are a whole series of moving parts that none of us can predict. But we think we are as well placed as we have ever been and indeed our competitive set are, to be able to deal with those competitive pressures. And I keep coming back, I can't stop Aldi opening 50 or 60 shops a year and that inevitably has an impact on our business, it adds capacity to the industry and that puts pressure on the industry. I have said that many, many times over.

Above and beyond that, and that is all you have to believe, in terms of the core investment thesis, if you are want a dividend stream, if you want the debt to come down by £750 million, which is roughly 15% of our equity value as of today. And that would, let's say for the sake of this conversation, a relatively conservative view because we would not want to commit to something that we didn't think we could deliver.

There are a series of things we will talk to you about after the break and you might have seen in the shops where if you might believe, you know some of the numbers we have put into the Bank Presentation or some of the opportunities in the digitisation of the ability to sell Sainsbury's products to the nine million customers in Argos that don't shop with Sainsbury's or vice versa, you can start beginning to believe that there are some quite significant opportunities for growth. The bits that Patrick has talked about is another example.

But the base thesis is, I don't think the market believes, rightly or wrongly, that the underlying earnings of the company are robust. And we want to give you the reassurance that that is the case and that we think there is opportunity above and beyond that.

Further question
Just quickly, maybe because I live in Merseyside, I am just naturally more aggressive than other people! But I was interested in the shop today and the Presentation by Paul, you were talking about being 1% below Aldi on entry price lines. Why don't you just have, and you are talking about frustration that people don't understand how good your value credentials are, why don't you just have a big shelf message that says, this is cheaper than Aldi?

Answer: Mike Coupe
You can talk to Mark about our marketing. He is sitting here right now, he will talk to you later. But you are right, I mean in the end we have a lot of marketing messages. We have a limited resource to talk to our customers. And you'd have seen on Simon's chart that value for money is one of the key metrics that hasn't moved significantly or in fact hasn't moved at all in the last period of time. And it is very, very difficult to change. And it is ultimately going to be driven by the experience you get in shops. And over time, certainly my experience, if

you see volume growth and customers start to appreciate your prices, then that will then reflect in value perception. But I suspect even if we spend every, above the line marketing dollar that we have today, it would be quite difficult to move that value perception dramatically. And we have tried lots of different ways over the years. I don't know Mark, maybe. This is Mark by the way.

Further Answer: Mark
I think you have probably seen over the last 6-9 months a number of tit for tat, ASA wins back and forward, and I have been in the industry for a number of years and we've certainly had the competitive goes back and forward. And when you talk to customers you know, it pretty much passes over them. You say, tell me about your prices, tell me about your business and focus on your offer. We absolutely have stepped up our value communication in the last 6-9 months both in store and how we frame that value and in the plinths now, segment as well as our broadcast communication on the convince of knocking down our prices.

And then, obviously what you don't necessarily always see is a lot of the direct marketing communication and price reassurance we have given to our competitors. So I think that is what I have learned in this job, the best way to necessarily focus and to Mike's point earlier, stable prices over time is what drives price perception regardless of what you see, giving people shop around the number of stores.

Mike Coupe
We will take one more question before the break.

<u>Question 7</u>

James Anstead, Barclays
Thanks. James Anstead from Barclays. Two questions if that is okay. Firstly on the stores you are thinking about shutting, I know you don't have a specific list, but is there anything that those stores have got in common, whether it is the size of the supermarkets, the geography or the proximity to discounters, is there anything in common?

Answer: Mike Coupe
No I mean there is nothing I would pick out particularly. I guess in the end you could take your own view of our real estate. Typically they are going to be at the tail of age, you know lots of reinforced concrete, so they are of a particular era and in the end they are coming to the end of their life. The Convenience store Portfolio is much more straightforward. In the end it is pretty much a renewal programme. We built into our models the fact that we will close a certain proportion of stores every year. So it is just a reflection of that and wrapping it together makes it easier in terms of communication and doing it piecemeal. So I have a few in mind, but you know as I say, if you imagine 1970's Bridget Junoesque reinforced concrete stores then that is the kind of territory that you might be thinking about.

Further question
Okay. And the second one is the comparison again in base price index against Tesco, which looks like clearly consistent progress over the last 5,6,7 years. I mean do you think that is holistic way of kind of measuring overall price when over that period you have obviously made quite a big thing of reducing promotions? And again the industry data suggests you are now promoting a bit more than you were six months ago but a lot less than you were doing 5-10 years ago?

Answer: Mike Coupe
Yes, well the commercial mix is reflected in the price index. So it effectively takes into account that pricing dynamic. But to Paul's point, we are very pleased with where we are

today. We have seen significant progress over a long period and significant progress particularly over the last 3-4 months.

You know, the other point I would make is over the last five years, all of our main listed competitors have all dramatically reset their profits. They have written off swathes of their assets. Their return on equity therefore looks better. And they have given themselves a runway into investing in their core proposition. I would argue, as we look forward, a lot of that "self-help" if that is the right way of describing it, is disappearing and therefore the platform of stability or otherwise that we might think about as we look forward, should give us the ability to do the things we talked about and to maintain a level of competitiveness. But when you are mainstream with a competitor, who is effectively taking the mother of all profit warnings and allowed themselves at least 2-3 years worth of investment in the offer, that is quite a difficult competitive dynamic to manage. But I would argue very strongly that we are pretty much through that in terms of the legacy they had. And that gives us I think a more stable platform from which to work.

The other challenge is, you just think about the discounts. I mean Aldi are making half the money they were making or at least as a net margin compared with 4-5 years ago. If we were a publically listed company and we spend half a billion pounds a year on opening shops and we were making half the profit, I suspect that would be a very different conversation. But we are competing with somebody who thinks about these things in a much longer-term timescale than we are in the public markets.

Mike Coupe
I am going to call it a day there in terms of the questions. We going to have a comfort break, a coffee break. We are back in 15 minutes. 15 minutes for a coffee break, that is a lot of people. There are several floors of toilets! And then we will wrap up. We have got four more Presentations to go. So thank you very much for begging our indulgence.

Coffee break

Financial Services Strategy
Jim Brown

Alright everyone. Are we ready? So we get started. My name is Jim Brown and I am going to talk with you for the next 20-30 minutes about financial services. But before we kick off I thought I'd just make a couple of introductions, one about myself, but also Mike Larkins. So Mike over the back here, Mike has joined us this afternoon. He is the CFO for the Bank. He has been onboard a year, so a little bit longer than I have. But brings with him a wealth of experience in financial services. He was most recently the CFO for RBS in the personal and business banking space, but does have a very wide range of experience in financial services over the years.

In terms of myself, well I have been here 90 days as Mike said. My earlier career going back a little bit was out in Asia and the Middle East where I was Head of Retail and Commercial Banking for ABN Amro and then RBS Bank after the takeover. Following that RBS then asked me to become CEO of Ulster Bank and that is one of the big three banks that operates across the island of violence. So I joined there right in the middle of the financial crisis. Over time, the five years that I was there I basically restructured that business and returned it to profitability and then was asked to go to become CEO of Williams and Glyn where I spent the last couple of years doing that. So that is just a bit about the team.

So in the 90 days that I have been onboard, most of the time has been spent around looking at the strategy, what are we going to do with the business. So really looking into the business and seeing what the opportunities are there to transform it. This afternoon what we are going to talk about is how we reshape the business to deliver a great proposition for our customers first of all. But equally importantly how do we deliver value for the Group as a whole. Some of the things that are outlined up here have already been announced today, but through the Presentation I will delve into these a little deeper.

So let's have a look at Financial Service as a whole within the Sainsbury's Group. So what I have done here is as we are going through the sort of the strategy, taking a step back and looked at the business over the last five years. And what you can see here is that a significant amount of capital has been invested by the organisation over that period. A total of £650 million. And that has gone into support really four key areas. One is clearly what we call the new bank programme which was basically replatforming the IT out of Lloyds. The second was to finance the purchase of Argos Financial Services as part of the Argos transaction. The third is to fund the growth and the balance sheet. And then lastly, there has been an increase in capital because of regulatory requirements across all financial institutions as well.

Now as a consequence of all of that, the Business has grown. And you can see here that in terms of customer loans we have significantly grown the balance sheet over that period. It has grown nearly threefold. However the challenge is that, in terms of returns, or the underlying profit before tax, that hasn't kept pace.

You can see here that the Bank profits back in 2013/14 were a total of £56 million. And then most recently it totalled across all the financial services, £68 million. Now this number includes both profits within the Bank legal entity as well as profits that are within the Argos Business as well. So an uptick for sure from £56 to 68 million. But when you look at the return on equity, certainly not where it needs to be.

There are a number of big questions that we looked at when we were looking at the strategy. So the six key questions. The first one was well having looked at the last slide, £650 million has been invested in the last five years. When are we going to stop putting cash into the Bank? That is the first question. The second was, we have got a 6% return on the capital employed across all the financial services, so how can we improve returns? We haven't paid any cash dividends to the organisation doing that, we have a relatively high cost:income ratio at 63% how can we get our costs down? We have a customer loan book of just over £7 billion. How can we mitigate the risk across the rest of the organisation? And then there is a huge opportunity that in terms of the Business going forward where, whilst there is high connectivity between the Bank and the rest of the organisation today, 85% of our Nectar card customers today still don't have financial services. So what can we do in that space?

So we took a step back and we did look at everything when we reviewed the Business. But we started with the market first of all. So many retailers across the UK offer financial services and offer them very successfully. I have just outlined a few here, but you can see Tesco, Shop Direct, Next as examples. They have very good financial services offering for their retail customers. And the returns that they are generating from the Financial Services Business range from £120 to just under £200 million. So there is a real opportunity if we do this right to really create value across the Group as a whole.

So let's talk about Sainsbury's for a second, for a few minutes. The Business today operates a lot of products. We have a wide range of retail products and services that we offer. Everything from store cards to loans to credit cards, mortgages, savings accounts. And then we have a range of commission based products as well. However when you look at this, you can see that in terms of revenues, most of the revenues are actually concentrated across the consumer finance products. So Argos store card, loans and credit cards. And the other 30% actually comes from commission based products. And that is a range of products here, we have got the ATM network, insurances as well as travel money. But can see a lot of products. However there are some that don't make any significant contribution in terms of revenue at all.

Having said that, the connectivity as I mentioned earlier with the rest of the Group with financial services, is very strong. And by providing financial services products we have a material uplift in terms of the overall business.

So I just wanted to show you here a couple of things. First of all just on Argos, and this chart on the left here just shows that a comparison between somebody who comes into an Argos store for the first time and just buys an item versus someone who comes in and takes an Argos card with that purchase. And what you can see is that in terms of new customers, if they take the Argos card product, they actually spend twice as much with Argos if they didn't take a card. But importantly, if you go without 12 months, the same customers, you can see that those customers go and spend another £434 in Argos versus the just over £200 that they did at the first transaction which is £245 more than someone who doesn't have an Argos card. So there is a significant uplift in terms of retail sales into the overall business.

A similar trend for Banking. What we know is that customers who have a bank product spend a lot more than like-for-like customers who don't. And in fact that gives us another £100 million uplift in retail sales across the whole organisation.

Now just to put it into perspective, when you add all the retail sales that we finance just through Argos as well as through credit cards in the Bank, those customers spend a total of £1.75 billion in retail spending every year.

We also have some fabulous assets across the organisation that financial services can leverage as well. So first of all brands, we have some great brands. We have got Sainsbury's brand, Argos and Nectar which we will come to in a moment. But some great brands. Lots of retail outlets as well. A huge customer base, and importantly with Nectar a lot of data that is very interesting from a financial services perspective as well. Importantly, the Bank, having the Bank entity and the Bank licence, that provides another £6 billion of retail funding to fund the purchases that our customers make. So having that licence actually gives us access to cheap funding as well.

So having said all that, what are the challenges that we have got? What are the key issues that we have got to address going forward? This slide tries to articulate that all on one slide. So very simply what this looks at is on the left to right-hand side, complexity of the financial services organisation. So on the right-hand side you have large financial institutions that offer all products. So it could be asset management, investment banking, retail, commercial and so on. On the left-hand side you have relatively simple organisations that might be one or two products. So here you have got the likes of New Day, One Savings Bank, Paragon Bank and so on.

On the vertical you have the cost:income ratio. So low cost:income ratio at the bottom, high cost:income ratio at the top. Now what this shows is that if you look at the size of the circles, the circle represents the overall size of the organisation. If you want to have a full proposition, you need to have a scale to compete to have an acceptable cost:income ratio and deliver an acceptable financial return.

On the left-hand side, these competitors can compete because they have a very simple model, single, one or two products, very low cost to operate to deliver those. In the middle we have the challenger or challenge banks I guess. And they are organisations that have relatively high cost:income ratio. They don't have the scale of the big competitors and therefore have profitability issues. Now they don't offer all the products that the larger banks have, but certainly offer a wide range.

Sainsbury's Bank as you can see here sits up with that Group. We don't have scale in all products, we do in some like deposits and consumer finance for example, but we don't across the rest. And we have a relatively high cost:income ratio. Now if you look at the total organisation it is at 63% in terms of financial services. But you also have to remember we don't have a branch network either which some of these have. So that is the challenge that we have got.

So the key for the strategy going forward is how do we move from, because we are not going to be on the right-hand side. So how do we move more from where we are at the top here to the left and down to be able to compete. So how do we become a more simple organisation and compete in the areas where we have scale?

So going forward, the first thing we did in terms of strategy was think about why should Sainsbury's as a whole have a bank and what should we do or should have financial services and what should we do? So we said, well the real reason for Sainsbury's to have financial services is that we should be the provider of financial services for both loyal Sainsbury's as well as Argos customers. That is the real reason that we are in business. And if we get that proposition right, we know we can add value to customers and to the Group overall.

How do we go about that? What is our objective? How are we going to deliver that? This is really important. We are going to do that by being an agile, capital and cost efficient provider of simple, mobile led financial services. Now that is quite a long phrase, but it is very important to articulate what we are going to do but also it articulates what we are not going to do because if it is not in that then we are not going to do it. And there are three things, three areas that we need to focus on to deliver that strategy, three key priorities. First of all we are going to reshape the balance sheet, the second is we are going to simplify the organisation. And the third is we are going to strengthen the business as well.

So I just want to take you through those in a little more detail. So in terms of reshaping the balance sheet. The first thing as we announced this morning, we are stopping mortgage origination now. So no more mortgages being originated on the balance sheet for the Bank. The second, by doing that, not only does it mean that we don't have to put capital into fund that growth, the other important thing is that it improves our liquidity position so we don't have to keep on raising retail funding to support that. So by doing that we can actually improve the margins in our business pretty quickly as well.

The third thing that we are going to do is further build out the AFS proposition or Argos Financial Services. We have a very limited product range today, but if we broaden that product range and we look more closely in terms of pricing and pricing for risk and those sorts of things, broaden our proposition, we think there is an opportunity for us to do more in that space than what we are.

The next point is around our cards and insurance business, both of those are very connected to our customers, to overall customers of the organisation so we want to improve the momentum in that. And lastly, we think there is a real opportunity for us to really develop a new financial services model with Nectar at the core. I don't want to say too much about that yet, but we have got a great bank infrastructure there today and we also have a great Nectar proposition which Mark is going to talk about shortly and we think that there is an opportunity to do something really good in that space.

The second point around simplifying the organisation, we need to right-size the cost base. So we are having a look at the whole target operating model of how we deliver the business today. There is a huge piece around simplifying the business and we have identified quite a number of areas which I won't go into today, that we are looking to really address to take out costs. So over the coming months as well. But that is really important that we right-size for the simplified organisation that we are going to have.

We also need to rationalise the products, so reduce the number of different types of products and reduce the variances on those products as well. We are a heavily outsourced model, so we need to revisit our vendor, our third party supplier arrangements there as well. We think there is opportunities in terms of value there as well. But one of the big opportunities that we have got is, by being part of a large organisation at Sainsbury's is we have a real opportunity to actually do more in terms of leveraging the synergies that that can provide for us as well.

On strengthening the business, really important point this, we want to make sure we continue our focus on strong operational resilience, on doing the right thing by customers, so conduct is really important as well. And also have absolute discipline on how we deploy capital, what we invest our money into in terms of financial services, make sure that we get the adequate returns that we are looking for as well.

Lastly, but not least, the other key thing that we need to do is make sure that we have got core competencies, in some of these we already do, but further build out those where we need to do more. But core competencies in areas where we think that it is going to be really important for the type of business that we are going to be going forward. So things like creating great customer experiences, digital data, analytics for example, credit operational risk and lastly partnerships.

So if we get all those priorities right then we will deliver on our objective. And if we deliver on our objective then our vision will be achieved in terms of being a great financial services organisation for Sainsbury's customers.

So what does that mean for the business? Well the business, the balance sheet will be completely reshaped versus what we had in previous plans. And you will see here first of all if we just look at lending, we try to give you a bit of a flavour without sharing with you all the numbers. But essentially the areas that we will grow are around Argos store cards and credit cards and there will be very modest growth in terms of balance sheet in those areas. We do expect with some of the initiatives around products and pricing, that we can improve the earnings significantly through Argos, but also improve earnings through credit cards as well.

Personal loans we think are, I believe they are a core part of the consumer finance proposition, but we are not looking to grow that. It will be there to support customers who want personal loans and a lot of those will be no doubt sort card and credit card customers as well. So that will be flat.

Mortgages, we will look at how we exit. We are looking at options on that right now, but over a period of time, depending on what the strategy is to exit. That book will run-off relatively quickly so it will go to zero and obviously we lose the earnings from that as well.

Net:net, the overall balance sheet for the Bank over the next five years will reduce and that is primarily driven by mortgages running down, offset partly by the increase of portfolios and some of the store cards, but as I said, those are modest.

Deposits, an important part to fund the business, we are adequately funded today. We see that through running off mortgages or selling them what you will see is that we don't have any need to grow the mortgage book, in fact there is an opportunity here to improve our margins and widen our pricing because we no longer need to be top of the league in terms of pricing to fund the growth that we were needing to do to support mortgages. So an opportunity to grow revenues there.

And last, but not least, on our commission based products, we see a real opportunity to do a lot more on the insurance space and also to do more in travel money as well. ATMs probably this, so because that is a very good business for us. But we expect cash uses to decline over time. So net:net, reshape the balance sheet. It will reduce, but earnings will grow, deposits relatively flat and will grow commissioned income.

I would just like to touch on the risk profile for a minute. Clearly getting out of mortgages will significantly reduce our risk in terms of credit exposure to those products, it reduces the liquidity risk that we would have had, operational risk as well because we are more simplifying the organisation too.

But there are a couple of other things that I would like to highlight as well. Coming in from the outside and having a look at the business, this book, this Portfolio is very good quality and looking at that, not just from our own eyes, but comparing it to the market as well, this Portfolio performs very well. And that is across all products. The interesting thing to note is that when we look at dissecting the Portfolio further, you can see here is that the credit performance of customers who have a Nectar card as well as having in this case a loan or a credit card, is significantly better than those that don't. So firstly, credit rating, when we onboard them but also the absolute performance in terms of arrears is significantly better than the market. Now what that will enable us to do going forward as we further refine the business is really look at how do we create great customer experiences around that? How do we price for risk and so on as well? So that puts us in a very unique position versus the rest of the market.

The second is that with mortgages gone, which were a long duration product, our Portfolio is relatively short duration. So if there are stresses at any time, we can stand down very quickly. But of course the key to improving our resilience is actually as we increase our underlying profitability for the business. Our ability to absorb volatility in the market significantly improves.

So, we said there were six key areas, strategic questions that we needed to answer as we were putting the strategy together. The first of those was when will we stop putting cash into the Bank? Well the answer is, from today. And the reason for that is that we will no longer need more capital to support mortgage growth first of all. And because of the actions we are taking on pricing and cost, we are actually cash generative as well. So the bank will be creating capital.

Secondly, in terms of returns, with the plan that we have put in place we believe we can increase underlying profitability, we can double that in the next five years and that is in total. Looking at total financial services. And we also believe that we can get a double digit return on equity through that period as well. That improvement in profitability will then allow us to upstream cash to the rest of the organisation. We will also need to rely on transforming the business to do that. A big focus on cost, but also revenue generation as well. We will drive our cost:income ratio to around 50% within five years as well. Importantly the risk profile for the business will improve as well, obviously stopping mortgages and we are looking at strategic options as to what we may do with that Portfolio over the coming weeks. But that improves the risk profile for the business as well.

Last, but not least, I think the real opportunity for us going forward after or as we transform the business is that by increasing our connectivity between financial services and the Sainsbury's customers as a whole, we have a real unique opportunity to really create real value for the overall organisation.

Thank you very much. Over to Mark.

Nectar
Mark Given

Great, thank you very much. Good afternoon everyone. My name is Mark Given, I am Chief Marketing Officer for the total company. In line with the plan, Kevin talked this morning, I have been seven years in Sainsbury's and in line with that currently integrating marketing organisations across Sainsbury's and Argos general merchandise and clothing. I also have responsibility for the overall Nectar loyalty and coalition and that is what I am going to focus on for the session today.

So I am sure you are all avid Nectar collectors, so I will spend a little bit of time telling you what it is and I will talk actually about why we think the coalition model is pretty unique and a pretty powerful one for Sainsbury's. Give a bit of an update on what we have been up to since 18 months into the acquisition. I will talk a bit about where we are in the plan to digitise and how we think those opportunities act more like a media business going forward. I will then talk a little bit about the value we think the Nectar plan adds to the business right now and how we think it is a platform for greater personalisation and some of the commercial opportunities that will come with that in the future.

Nectar is the UK's most recognised loyalty scheme. We think there are three things that you need to have a successful loyalty scheme in the UK. The first is scale, you need maximum possible coverage of your customer base and the UK population. Nectar, we have got 18 million members, 12 million of which are active in Sainsbury's every 12 weeks and we issue 46 billion points annually which converts to about £200 million of value. Second thing you need is digital contactability, so the ability whether it is email or whether its App, to have that regular conversation with customers. And you can see from the stat, we are in a really good place with plans to supercharge that in 12 months coming up.

The third thing you need is for the scheme to be cost effective. If you look at our proposition, we issue one point per pound spent, that is worth 0.5p to a customer or 0.5% dividend in exchange for your data. If you compare that in the market, Tesco would be about 1%, Boots would be about 4% and actually if you look internationally, some of the French retailers would be in the 7-8%. And we think it is the coalition model that means we can keep it at that level.

In terms of the last 18 months, you will recall Sainsbury's was part of Nectar for quite a long time actually. Nectar was owned by Aimia inc, listed on the Canadian Stock Exchange and we had an opportunity to acquire it back in February 2018 and that has been fantastic for us and just giving us a real element of control and deliver the revitalisation that we needed. We were pretty quick out of the blocks and we got a digital trial live in the Isle of Wight in about April of that year. We then focused by June on standing up the business entirely off the Aimia systems as quickly as possible and get it fully standing up in the Sainsbury's systems and work through our GDPR requirements.

Last summer we then focused on the coalition. So we re-signed existing partners like Ebay and American Express on long-term deals and then we focused on new partners. So we welcomed Esso to the coalition in June on a long-term deal. They will use Nectar points as the reward strategy and we actually run all their CRM analytics for that business as well. We also stepped up our reference to roll Nectar across the various bits of the business and particularly Argos, and I will talk a little bit about that in terms of later. If you are back in the store you were in this morning over the next couple of weeks, it will be a sea of purple. We are going to roll the digital App out nationally throughout October which we are excited about and I will share that in a little bit more detail.

And then I would say looking to the future, we have got a healthy pipeline of potential new coalition partners that we are in discussion with, and actually over the next couple of months we will announce a household name in a large industry vertical, who will be the next major partner in that coalition, just to fuel that growth over the long-term.

In terms of how the coalition works, it is really simple. You know customers earn points from the stable of brands at the top and they redeem them on the stable of brands at the bottom. And there is a number of advantages of this model. Firstly, because of the number of partners your balance builds quicker. So you are just more engaged in the scheme and you can see that grow. Secondly, if you are saving for a particular award, it might be a trip to Paris on Eurostar or a Christmas gift or a toy in Argos, we know you are more engaged at collecting and more likely to shop at the brands that issue points in terms of this one.

It has also got a number of financial benefits. So as a business we earn a margin on the points that are issued and from the brands at the top level. Many more points are redeemed in Sainsbury's than are issued driving a sales benefit value, and of course you get to share the fixed cost of the coalition across a wide range of partners in the marketplace.

I will talk a little bit about data. One of the huge advantages on the level it gives you on your customers and the marketing permissions that come with that to target. If you think about the view it gives us on our data, it is where customers live, how many people are in the household, the level of affluence they have got, the level of loyalty they have to the various different bits of the business, even looking at things like, do they scratch cook, are they ready prepared meals? Are they health conscious? It gives us a huge amount of data to look at. Very conscious that there is a debate on how customer data is necessarily used in the marketplace and we take privacy and our privacy pod very seriously. And we actually think that Nectar is a trusted brand and Sainsbury's is a real advantage for us as we navigate that landscape going forward.

The Nectar data and a few presenters have referred to this already, underpins an awful lot on the customer and the commercial decisions we make in the business. It is probably impossible to overstate how intertwined it is with a lot of the decision making we do in the business. If you look at something like pricing, it lets us look at pricing sensitivity by different customer groups. If you looked at promotional strategy, we can help the teams with incrementality at category level or halo benefit from particular promotions across different category groups. Looking at range reviews, we can go down to down to an individual skew level and look at substitutability if you change the range what is the reaction going to be? And it also creates a dialogue between our suppliers and the category teams in terms of what are the fundamental customer drivers driving your sales in any particular area.

Within marketing, it powers all of our marketing. It gives us an ability to personalisation at a huge scale. And then in the wider business it helps us plan our innovations, helps us look at what new products we want to bring and what trends are growing in the marketplace. It helps us with macro store layout, understanding a particular area and even reference to some of Patrick's work, what concessions are more suitable for that area. So fundamental to an awful lot of things we do.

I talked to this earlier, we have made good progress in using Nectar across the food business and in fact we talk internally about Nectar as the glue that binds the different brands of the business together. Within Argos customers can redeem their points now in any part of the business, in-store or online and we know that is a big advantage given the seasonal peak in that business. We have also got lots of projects where we are using

Nectar points to get more Sainsbury's customers to shop into Argos and with existing Argos shoppers to drive more frequent purchasing and to move across categories from one to the other.

Nectar, and Jim referred to this fundamental part of our Sainsbury's Financial Services Business, customers earn double Nectar points on their food shop with their credit card and we use point incentives to drive car insurance as an additional product into the basket as well.

I talked about this earlier, we are ready to launch a digital version of Nectar, we are very excited about this, we have been working on it for quite some time. A number of advantages of that. One, it is simply how customers expect today, using their mobile phone versus the plastic card. And two, it helps us use a lot more automation and machine learning in terms of driving the individual offers for customers. How we constructed it, it gives a single destination for offers from Sainsbury's and all of the coalition partners. And then we are also taking the opportunity to refresh the Nectar brand, really positioning it as sort of the modern digital brand that we want it to be.

As I said earlier, we have been in the Isle of Wight initially trialling it and actually we have trialled this across all of Wales over the last year and we have made lots and lots of iterations based on customer feedback. And given I couldn't work the clicker and download this on my phone, so fingers crossed, I am just going to open my App, you can see on my phone. This is live right now so this is the main interface. You can see, good afternoon Mark, I have got just over 11,000 points worth, just over £56. A couple of features, first is the card, so this is my digital card, no need to carry plastic, and this will talk to any till across the Sainsbury's estate, cafes, petrol filling stations etc. I can also see my activity. So I can see my points and check I have got my balance. It will show in Sainsbury's which store local you bought, it will show your online purchases and importantly it will also show the benefits you get from some of the banking products you can see on a credit card statement how much value you are getting across that bit. And also show across the coalition partners all in one place as well.

I then have got my offers, if we click in, at the minute the algorithm is looking at my previous purchasing history, looking at my loyalty level, my potential spend and is giving me points offers based on relevant products across that period of time. So you can see what I have been shopping at and thankfully I have been pretty healthy recently as you can see. So I just save the offers into that, it goes into my saved offers and then next time I am in store, I buy these products and the points are automatically added into the basket. If you then, if I scroll back, that is my Sainsbury's offers. I have got my coalition offers all in one place. So you can see here I have got an offer from Ebay, Nero card, I have got something for a coffee at Cafe Nero which is one of our partners or a view cinema for the weekend in terms of leisure time. And you can also search any brand within the coalition scheme that brings up your offer period.

So we are really excited we think it is a great product, we think it benchmarks for any digital products, so I think we have got a really good capability now of developing fantastic customer experiences and it is built on a platform that we can constantly upgrade it many times daily if we want to across that bit.

Now you saw in there that I had a number of points based on product offers that are refreshed weekly, we think that is just scratching the surface of the level of personalisation that we can build into the platform. So you can look at weekly offers and to daily and then in real time we have got points offers we will move to cash offers at a basket level, or cash offers at individual product level. In the not too distant future we can see it where you can use location as a variable to trigger offers. So this example you have got a customer who has come into store, they maybe shopping fresh produce, we know that they are a value conscious customer. So as they pass meat, fish and poultry you could serve an offer of points on a product like chicken breast that we know is relevant and something they buy regularly.

Similarly we think there is an opportunity for suppliers if are Coca Cola and you are launching major piece of innovation into the UK market, you can easily use the App, scan the outdoor advertising poster, add a point to your basket and next time you are in a store it will prompt you in your Nectar digital wall across that. So I think location is a variable point, we think we have got a really strong platform for everybody for personalisation and for the future.

Changing tack a little, we saw this report from Bernstein I think it was a couple of weeks ago, some of you may have read, it said what if the future of retail is in advertising, a profit pool transfer from CPG to retailers. You imagine, we quite liked reading that. In terms of some of the drivers of that, UK retailers have huge footfall across the physical estate and they have huge traffic to the ecommerce sites. And they have a huge amount of data on the category and individual skew levels of those individual peoples. And CPGs look for you know a greater RoI on the marketing, that is where I think the thesis is driving that. And we think we are really well positioned to benefit from this trend.

If you take a step back, we have got a business called I2C, Insight communication, and that was a joint venture with Aimia as well, we took full control of that business about 18 months ago. And very simply, it is a shopper marketing business. So any of our suppliers, Coca Cola, Unilever or some of our smaller ones come to us and they are launching a new product or a marketing campaign. We can build the campaign across Sainsbury's, that might have point of sale, it might have digital outdoor, it might have Aimia to drive trial marketing. That business is profitable today and it is in growth, but we think given the dynamics and the media market there is an opportunity to grow that in the future.

UK media market is worth £24 billion, it is absolutely huge. Of that the CPG suppliers we work with are about £8 billion of that and increasingly that spend is moving towards digital platforms. And when they are advertising across Facebook, Google or across the internet, you can use Nectar data as an audience, so they can more effectively target category purchase, non category purchase or build audiences in terms of this. We are doing this today with a number of suppliers etc at a smaller level and we have made a number of technology investments over the next couple of years that we think can help us access this profit pool and using that to help them target those markets.

That is it from me. So I think in summary, we are really pleased with the progress we have made in Nectar across the last 18 months and the coalition is pretty unique and a pretty powerful one that we are going to grow and we are locked and loaded to go fully digital. Nectar is fundamental to driving the commercial performance of our business today, but actually we think personalisation and the platform we have now got can do that to a greater extent in the future. Thank you very much.

Digitising the Customer Journey
Clo Moriarty

Thanks Mark. Good afternoon. So digital is integral in our customers lives. And as such is a key part of our multi-channel, multi-brand business across food, general merchandising and clothing. And these customers engage with more of our propositions, are our most loyal and spend the most with us. So a customer who shops online store spends 2.1 times that of an in-store only customer. And the customer who shops extensively digitally with us, spends 3.1 times that of an in-store only customer.

But we have a strong set of digital propositions to cater to this valuable and growing customer need. Sainsbury's groceries online makes up almost 8% of our sales. It is growing at 6.8% year to date and as we talked about in-store this morning, over the last number of years we have improved its efficiency by over 40%. We talked extensively about Smart Shop this morning and in the 200 handset stores where it is active today, we are seeing sales participation of 13%.

Argos is the third most visited retail website in the UK. We see 60% participation through the digital journey and over 20,000 of our items are available anywhere within four hours. Mark has shared our digital Nectar journey, but in this space where it is active our customers are engaging 52% monthly participation versus original Nectar where it is 19% monthly participation.

Habitat is predominantly digital with 70% share of sales and that is growing at 12% year-on-year. And Tu Clothing online at 8% share of sales is growing at 50% year-on-year. We have 1.4 million active customers using our Argos financial services App. Just under 50% use this as the sole mechanic for payment and just over 50% use it as a way of going paperless. And finally, over the last year we have sold 1.4 million products from our Bank online.

So putting all these things together, we believe we can show up whenever, wherever and however our customers need us to be. We have made a very deliberate choice to invest in our base infrastructure over the last number of years. Across our monolithic systems, migrating to the Cloud and investing in our overall connectivity and hardware. Now Phil Jordan is just in the back row so for any detailed questions on our text stack, he will be more than happy to take them in Q&A.

But in brief we are predominantly becoming micro-services based which in essence means taking our large monolithic systems and breaking them down into components. Components like log-in, my account, my recommendations and then reusing them after we have built at once across each and every proposition.

We are already benefiting from being predominantly Cloud based both in terms of increased stability and our ability to be able to bring new functionality updates to our customers more frequently. Our page-load speeds are 50% faster. Our processing time is reduced by 75%. And in the world gone by we used to be able to bring new functionality to our customers 5-6 times a year and each time we committed the cardinal sin of a customer outage. Today we can release much more frequently in day with no customer outage.

Simon spoke at length about the till upgrades so I won't dwell on that right now, but I would like to share the story about improved WiFi. So after the last number of years we have been tackling this twofold. The first is increasing in essence the pipe going in and out of store so we can get more data in and more data out. That job is complete. The second element is optimising the connectivity around the store and that job is almost done.

The next step on our journey is integrating the propositions, functionalities and brands. I will do it in a number of ways. The bull's-eye is knowing our customers better than anyone else and we can do this as I was speaking about in store this morning, through our identity programme. A single account, single log in, single password, once and done. 10 million of our customers are already using this platform and over the coming 6-12 months we will onboard each and every one of our digital propositions.

Enabling universal discovery means that if we have it and our customers want it then they can get it. And this autumn we extended our Argos search engine in our test environments, such that it can find food. So more to come there. We are building the single basket and that will make use of our unique fast and flexible fulfilment options. And we will make payments more seamless at our SmartShop this morning. And integrate our financial services throughout our journey.

As we converge we will do so choicefully. We are really aware of the brand warmth that these brands hold today and equally conscious of the unique customer journeys and experiences that our customers expect when shopping for different missions. However we will converge where it makes it easier for our customers. We will integrate and surface up new propositions, more of our missions, more of the time. And we will do this where we can reduce development and maintenance costs. We are starting with food. We are experimenting with all of our grocery needs in one place. And last year to a cohort of our customers we created a one App where we brought our groceries online, our SmartShop proposition and our 60 minute Chop Chop proposition all in one place. Our customers loved it, they loved it because of the convenience, they loved it because the control in their hands. And ultimately they expect food fulfilment anywhere. But more than that, what was really insightful for us was what they did. 11% of our groceries online customers started using SmartShop as a result of being exposed to this. 80% expected digital Nectar inflow, hence digital Nectar. 82% wanted a single account once and done, hence our identity programme.

So as we think about the propositions we have today, the investment we have already made in our base infrastructure and our customer centric development and testing, we can deliver for the now and we are also fuelling our pipeline for future growth.

So over the next few minutes I would love to share a number of the concepts that we have already got in development and test and you can expect to see in our customers hands next calendar year. The reason you can expect to see them is we have already built those modules, those pieces of work and the job of work at hand is piecing them together to create the scale propositions.

So our first example is in cross brand and cross channel shopping. By exposing all of our catalogues and all of our categories to a customer, they never have to leave our ecosystem to be able to fill their needs. This creates a single shopping destination with general merchandising and food together, bringing all our brands in one place.

So I am going to go on a customer journey here so if you can indulge me. So hey Google I'm having a barbecue. Our customers need us to solve that mission. Last year we brought our Argos products to life on Google and we brought our food products to life on Alexa. The next job is making both available on each. Because of our recommendation engines we know the most appropriate product for this customer. Equally we know the other elements that should be included in their basket, be that the warranty, the tongs for the barbecue, the actual burgers or because it always rains in this country, an umbrella for the barbecue.

Now this customer is feeling pretty lucky, adding everything to their basket, save the umbrella. And we are creating and building that single basket and ultimately enabling our customers to pay through one of our many financial services mechanisms. This gives us accessible intent base general merchandising and clothing. It creates frictionless multi channel shopping through a single basket with single payment.

Our second example is personalised real time offers in-store. By digitising our in-store experience we can make it as interactive or as passive as our customers choose it to be. We see real power in combining SmartShop and the functionality of groceries online. Equally by exposing stock availability through the stock App that David spoke about earlier. And we see how Nectar can engage our customers throughout the shop in-store.

So you saw me earlier on, it was a mug earlier on, now it is the red meat, scanning it via the SmartShop App. We can now start bringing recommendations of what goes well with that red meat and prompt the customer to tell me more. And this example is a perfect bottle of Taste the Difference spread. We pull on three elements. First is location stock levels. In order to be as efficient as we are in groceries online we need to know where every single stocking point is in the store. And by understanding that information we can direct our customers to that stocking point. Equally we can surface up the stock levels that we know are available through the stock App. So our customer knows if it is in stock or if there is an appropriate substitute. We have in-depth product details, origin, ingredients, make-up of our products through our online catalogues. And equally as you know we don't live in a world today where it is trust me, it is trust the 5,000 people who have already tasted it and loved it. So we can serve up those rating and reviews through the same mechanism.

And then finally, our stores are a major asset to us. So for digital to sing, it is about combining the power of technology and our people for that value added service.

So returning to our customer journey, we have now directed our customer to the appropriate location in the store where we know the wine is and encourage them to click on it and buy. And to do that we may offer them a personalised offer just for them. They can add it to their basket and we want to keep that behaviour circular so we add some points via digital. So we have personal recommendations, digital offers just for you and rewarding our customers for shopping with us.

And then finally, we have an example here about making your money go further because this is an area where our customers are telling us they really struggle. And they are asking us to help them live well for less stress by assisting them in this manner. Combining Nectar, savings and pre-paid gift cards offers us that opportunity.

So today for again a cohort of our customers we have a round up proposition available where in and out of Sainsbury's on every transaction our customers can round up to the nearest pound to create that pot. Mark has shared how easy it is to gain more and more points through engaging with Nectar. And then finally we have a gift card business which is analogued today that we are digitising.

So each of those elements adding up to something a little bit more substantial with all your money in one place. And at that point we have the opportunity to encourage our customers to spend that money back with us across our business by applying a loyalty multiplier. And of course paying whoever you want. And this example, this is our pay@browse which is available in 450 of our Argos touch points today.

So this is your savings, your points and your pre-paid cash in one place. We will make it really easy to spend that across the business and loyalty keeps behaviour circular. So by combining our range and our reach, our core digital assets that we have today, our unique fast and flexible fulfilment models, the investment we have already made in our core infrastructure, the digitising of our in-store customer experience, the linking of our online and offline customer journeys and our true data driven and customer centric development, we are best placed to be able to anticipate or rapidly respond to where our customers knowingly or not expect us to be.

Thanks a million, I'll just hand over to Kevin.

Financial Summary
Kevin O'Byrne

Thank you Clo. So final session before I hand over to Mike to wrap up and take questions. Hopefully this afternoon you have heard a lot. We have got some very robust plans for the business, very experienced and strong Management Team, clear opportunities and additional opportunities that Mark and Clo shared with us. There are three things I would like to do before we hand over to Mike. One, I would just like to talk about how we think about our business, our financial model and creating shareholder value. Secondly, I would like in that context just pull together some of the points that you have heard this afternoon, some of the numbers we have talked about and how that underpins our confidence in delivering a sustainable profit and robust free cash flow, and then talk about our key financial targets.

So just looking first at our financial model and how we think about creating shareholder value. We are not going to share today with you margin targets for the business. We don't think that is the right way to manage the business. This business is capable of generating strong free cash flow so our focus is on generating a sustainable profit flow and then in a very disciplined way turning that into a strong free cash flow so that we can one, pay a strong dividend which is well covered. Two, pay down debt and deliver the Group and of course that adds to the enterprise value of the business as we do that.

Now this is not a new plan if you like, this is something we have been doing for the last number of years, this focuses on free cash flow, paying down debt. What you have got here is just looking at the last four years we generated free cash flow of £1.5 billion. We paid dividends of over £800 million. And you can see the dividend cover there improving from 1.3 times to 2.1 times so your dividend is secure. At the same time we paid down debt of about £680 million, over £200 million a year. So this is something we have been focused on over the last number of years and something as a Management Team we will continue to focus on.

So going back to the operating model, you have heard lots of things today about how actions to drive sales, actions to protect the margin clearly without a sustainable profit stream, we can't be confident in a sustainable and robust free cash flow. And just to wrap up a number of things that you have heard this afternoon. Just on the left-hand side, Graham in-store and Paul were talking about how important the margin mix is in this business. We are very fortunate with our profile of customers, our store locations etc, the strength of the Taste the Difference brand, that we have a good mix across the business and that is so important. Quality where it matters, price where it matters. And that allows us in the underlying business we can invest in the economy area of the business because it can be funded by the premium area.

You also heard about the actions we are taking and the further opportunities to buy better for less. First of all what we call PQF, our Product Quality Framework which in effect is the way that we look at all our range reviews. As Paul outlined, the range reviews we have done to date, about half the volume has increased our cash margin by 3½%. And we have the other half to go after.

Value Chain Analysis, again where we work with our own brand providers, suppliers to take costs out of the supply chain end to end. And again we still have a third of that to go for and to date we have taken 7% out of the costs, but another £2 billion cost base to go for and then of course you start that process again. So lots of actions taken by the Commercial Teams to underpin to create funds to invest in the offer.

And then finally, there is the mix of products in the store. Sam talked about the new Beauty offer in the store and the great opportunity we have there. You have heard from James as well in the store about our General Merchandise and Clothing Business. And Patrick talked about concession income coming into the store. So we have got a number of opportunities to bring more margin into the business. And we are very pleased that our sales intensity in our big supermarkets has increased every year in each of the last three years. So again that puts more fuel in the tank to invest in the offer.

I talked earlier, you heard lots of examples in the store from David, you heard from Simon etc. and actions we are taking right across the business to cover our £120 million of cost inflation every year and we will continue to do that.

In addition there were some other points that were made in the afternoon. Additional opportunity to grow our profit from the growth in some of the new stores, 110 new Convenience stores etc. that Patrick outlined generating about £120 million we think over the next five years. Plenty of opportunity to monetise Nectar and I must say I am very excited about what we can do there and Mark outlined that. And then finally with the new plan we have for financial services and a real focus on not growing a Bank, growing profitable financial services for the business. We see it as an opportunity there to further underpin the profit delivery.

And then finally, the opportunities we have which are significant, unique to us as we bring the businesses together in a very disciplined way to take out structural costs, to take out fixed costs in the order of £500 million over the next five years.

So all of those actions give us confidence and should give you confidence that we can underpin the profit delivery of the business. So then the job in hand for us is to turn that in a very disciplined way into free cash flow to cover the dividend. So I would just like to talk about each one of these just briefly.

Capital expenditure. One of the challenges that a number of you in the room have places, you are spending £550 million capital on the stores, your depreciation is about £700 million, it is not enough capital. £550 million is enough capital. There is a couple of reasons why that number is different. The primary reason if I was to lay out for you, where is the capex, where is the depreciation? The biggest difference is in our big stores. We are not opening big stores the way we used to open big stores, and as Graham pointed out earlier, we are investing in our stores in a different way. We might do two or three sort of big refurbs in a year, when we used to do a lot more. But we are putting in the case, I think he gave you some examples this morning, where we are getting into lots of stores. So it is 50 investments, sorry it is one investment in 50 stores, rather than 50 investments in one store. And that is working. We are managing our capital in a different way. Small projects fail fast etc. So we can absolutely invest in our infrastructure and in our digital infrastructure which you have seen a lot with the £550 million.

The other message I would like to leave you with here is we do this in a very disciplined way. We allocate our capital carefully, we have very clear targets for returns. When it comes to growth we want four year returns because who knows what the world will look like in four years time. In efficiency we look for 18 months return. Now some of the energy saving work that Patrick talked about can be four years, but it is absolutely guaranteed, but generally we don't want any cost saving activity that doesn't pay back in 18 months. And then we manage the maintenance spend, that is across our store fabric and all our digital and IT fabric, we manage that relative to the depreciation in the business. So that we are keeping the estate fresh.

The next item I was just going to touch on is our pension scheme. I am really, really pleased that we have reached an agreement with our Trustees for the funding of the pension scheme over the next number of years. And it is a real, you know there aren't many win-wins in this world, but this is a real win-win. The pension scheme is more secure which is very important for us as Directors, and we are putting less cash into the scheme. So we have agreed a new asset backed scheme that we already had an asset backed scheme with the pension scheme. We have added an additional £500 million of freehold property to give an asset back. And we have agreed a long-term funding arrangement. So when it comes to the next triennial valuation, we have the shape of that already agreed, so it isn't. We are not going in every three years and starting from afresh. That gave the Trustees the ability to go to their members and to the Regulator and say, we can accept less cash which is not an easy thing for them to do in the current environment. And of course it is all signed off by the Regulator. The net result is a more secure scheme, we have completely, not completely, you never completely. But we have largely reduced the risk of trapped cash going into the pension scheme, because as we know once it goes in, it never comes out. And we have reduced the cash payments from £124 million a year to £76 million per year. Now the slide is a little bit confusing because the timing of year ends. But if you add the first three years and divide by three you get £76 million and that will probably drop to about £69 million in the fourth year.

Moving on to the other areas. Property, you heard the opportunities that Patrick outlined for mixed use developments. We are very well placed with our London store base to develop some of the properties and turn them to residential student accommodation etc. So we anticipate getting £150-200 million in the five year programme that we have got. And we have got more planning applications in the pipeline.

And financial services, Jim laid out the plan there. The main message from a cash point of view is no more cash injections into the bank. So that allows us to be more confident in our robust delivery of free cash flow which then underpins a strong dividend and allows us to reduce debt. And today we are pleased to confirm our dividend policy which we think is the right dividend policy maintaining at two times earnings cover, but ensuring that it is well covered from a cash point of view. And increase our ambition to repay debt, at least £300 million in the year we are in from the £200 million we talked about before. And at least £750 million over the next three years. So if you imagine the dividend and that £750 million, that is about £1.5 billion of cash that we are generating to pay dividend and pay down debt over the next three years. And it is about 15% of our equity value as Mike said, so improving the enterprise value.

So hopefully you can see that we are very focused on this Agenda, we have got some clear plans behind this Agenda, and how we think about value creation and financial discipline within the business.

So that is all I was going to say. I am now going to hand you over to Mike to wrap up and take us home. Thank you.

Summary
Mike Coupe

So I'm just going to make an attempt at summarising and then we will open up to our final Q&A before allowing everybody to go home. But before I try and wrap up, could I just thank all the teams for all the work they have done. A day like today takes a huge amount of energy and personal investment. All of the guys live and breathe the kind of stuff they have been talking about. And it doesn't happen by accident. So many of the things we have talked about during the course of the day are literally years and years of work, grinding through a whole bunch of detail to get to where we are as an organisation. And I genuinely believe for all the reasons you'd have seen during the course of the day, there is a huge amount of energy in the organisation to make the changes that we have talked about, both in terms of our core business but as importantly in some of the assets we are now bringing to the market and our unique ability to join our propositions together from a customer point of view in a world of very rapid change in the world of retail. And that fundamentally is what we set out to do, I set out to do five years ago.

So going back to the core. What are we here for? We are here as a business to help our customers live well for less, that is at the heart of what we do right across our organisation. We have talked in our core business about the actions that we need to deliver in order to be able to do that going forward. Competitive on price, we have covered that at some level of detail today, probably more detail than ever in my time in the organisation. We have talked a lot about how we can offer distinctive ranges of services and products in our organisation, that differentiates us. And relative to our competitive set, our customer base allows us to add value to our business in a way that our competitors can't. Clearly we want to make our business more convenient, whether it is in the shops, the way that we layout our shops, the services we offer within our shops and Simon has talked a lot about how our colleagues drive our business and some of the investments we are making in making our paper based tasks go away and allowing our colleagues to spend more time with our customers.

We have recognised that this is a hard market. The reality is the discounters aren't going to go away. Amazon is not going to go away and then there is a whole bunch of businesses in virtually every market that we compete who are in various stages of start-up and funding that have the potential to compete with us in the future. And therefore we have to continually challenge ourselves to reduce our costs. But we are uniquely placed for the reasons we have outlined, not just to pay to play in our cost reduction, but also to bring our businesses together to allow us to better serve our customers, but also drive a whole bunch of efficiencies that are not available to our competitor sets.

Grow connected services, so we have talked about the Bank, we have talked about the digitisation and Nectar, these are exciting opportunities. We have to prove them, but nevertheless you can see that there are some opportunities for future earnings growth in the world of financial services and certainly the world of data and the monetisation of that data is an exciting area which we think we have a unique business model that will allow us to develop over the next period of time.

And then last but by no means least, Clo brought to life the properties that we have in the digital space that can offer our customers a seamless digital experience, a seamless customer experience wherever they want to shop with us. And that might be in a conventional supermarket, it might be in a convenience store, it might be online. And of course we haven't spent a lot of time talking about our supply chains, but actually we have the ability to deliver virtually anywhere in the UK, same day groceries and same day Argos 20,000 products, and that is something that today is a source of competitive advantage. And we can do that cost effectively. So think about how we join those assets together and that again creates a very exciting opportunity for a business that is already 20% online and you can't say that about any of our mainstream competitors today.

We talked about the metrics, we start with the premise that if we have got engaged colleagues we will deliver great service to our customers that will make our customers more satisfied with our business, that will drive our volume share. Our profitability, as Kevin has already said, translates ultimately into free cash flow and that will improve our return on capital employed.

So in summary, we are confident in the core. There are lots of levers we can pull and we are not pretending for a moment that it is not a competitive market, but we have a whole bunch of things we can do to maintain our earnings and to grow our earnings into the future. We have a whole bunch of things coming down the track which are very exciting and not just unique in the UK, but actually unique in the world. We will create one multi brand multi channel business. And again you can see the building blocks really coming together. There are a whole series of sustainable cost reductions that we can make. We can cover the cost of inflation and we can certainly invest back into our core offer knowing that the market will become increasingly competitive over time. That will allow us to generate cash, reduce our debt and pay a dividend and of course in what is incredibly uncertain times in the UK at the moment, that will give us the financial flexibility and resilience into the future.

So that's it in terms of the Presentations. I am opening up the floor one more time to questions. The less questions you ask the quicker you get home. So we will start that side.

Question and Answer Session

Question 1

Victoria Petrova, Credit Suisse
Victoria Petrova, Credit Suisse. Thank you very much for Presentation. I have three short questions. First of all, how sensitive is your performance and likelihood of achievement of targets to pricing policy of discounters, especially in commodities and ELP products?

Answer: Mike Coupe
Well we could spend hours waxing lyrical. In the end it is an incredibly competitive market, pricing is very transparent and the ability to change prices is virtually immediate in our marketplace and that is not going to go away. In the end I have talked about the pressure on the discounters and Aldi were making 5% net margins four years ago, they are now making less than 2%. And you have to believe ultimately their Lords and Masters will require them to make a return on the massive capital investments they have made over the last years.

But if there is one risk, or one of the risks in what we have talked about, is the fact that it wouldn't take much in a business that makes 2½% net margins to put our profitability under pressure. But I go back round full circle, there are a whole series of things that we can do from a pay to play point of view, but then there are some things that are unique to us which will enable us to maintain a robust position into the future. But you can't get away from the fact that any one of our competitors, it is not just the discounters, could seek to gain advantage by always investing in price and therefore putting margins under pressure. But as I say, if people behave rationally the market should be recovering margin rather than investing margin, but I can't speak for privately held German companies.

Further question
Thank you very much. My second question is about seamless customer experience. Your online operations are 20%. What percent of your sales you can handle with existing platform? And are there any targets maybe I am not aware of?

Answer: Mike Coupe
Yeah well actually that's an interesting question. We haven't set any internal targets because in the end what we would say internally is that we are there to serve our customers whenever and wherever they want. And so however they choose to interact with us we need to be in a position to adapt to those customer needs. But it is fair to say, you know if you look at online groceries, the rough rate of growth in the market let's say is 7-8%, we have got more than enough capacity for the foreseeable future to be able to deal with that.

We have got some new propositions like Chop Chop which you know are exciting but very early stages. Those are in I think seven stores currently in Central London. Who knows where that might take us, but that relieves some of the capacity and without putting words in John's mouth, wherever John is, the Argos model has plenty of headroom in terms of capacity and growth and that has moved on even in our period of ownership in terms of online sales by I think 10% of the total sales.

So there is plenty of capacity for growth and we, again thinking about the business, because of our store base, there is lots of infrastructure going down building warehouses at the moment in the online space. We have those, they are called shops. If the world if about speed and utility, forward deployment of stock is absolutely essential to that idea and having shops actually gives you the forward deployment of stock which is one of the reasons why we bought the Argos business in the first place.

Further question
Thank you very much. And very last question, in the store where we were today, what percent of selling space is occupied by groceries, by sort of your core business?

Mike Coupe
Where is Graham?

Answer: Graham
So I think of the 63,000 square foot, I think about 40,000 is food and grocery.

Further question
And it is sort of representative for all large supermarkets?

Answer: Graham
For large supermarkets yes. It obviously, as a percentage increases as you go down the estate.

Victoria Petrova
Thank you very much.

<u>Question 2</u>

Maria-Laura Ardurno, Morgan Stanley
Thank you. The first question that I have is with respect to the investments that you have done both in terms of prices and in terms of like the product for your reshuffling. In terms of customer perception, have you already started to see some improvement in that particularly on the price perception? Or how long would you think it can take to achieve that?

Answer: Mike Coupe
I think we covered it earlier. I mean in the end the thing that we have seen most immediately is volume growth and so we see a reaction to that pretty quickly, literally within days if not weeks. And that is in the highest velocity categories. So basically the more frequently a product is bought the quicker you see the volume response.

As far as price perception is concerned, we showed the chart, we haven't seen that much change. And it is probably the most difficult thing to change because we did some research many years ago with 10 year old kids to see what their perception was of the supermarket sort of hierarchy in the UK and already at the age of 10 you have an embedded view of the quality, price framework as we would describe it. And that means it is very deeply embedded in the average customer psyche. So when we fix the toilets people notice it immediately. Driving price perception is a much, much more difficult thing to do over time, but to the question that Clive asked me earlier, if you see volumes growing and you manage to maintain a good price position in the minds of customers, ultimately that will reflect in their overall perception. But my experience is it is notoriously, I used the term before, internally that it moves at a glacial pace which is probably about right, even in the world of global warming.

Further question
And then the second question. This morning we had some examples of like cultural changes done at the store level and I was just wondering if there has been any changes in the way the Managers are incentivised from the financial side more, or if you have any sort of like free cash flow KPI at the different levels of those stores and above?

Mike Coupe
I'll ask Simon to respond to that.

Answer: Simon
Hi. In terms of the question you have asked, the main focus that we have put in place over the last year was put the changes in place I talked about earlier and really focused on how we get the right teams and the right service experience in stores. So the one thing that a store manager has absolute accountability for is to pick and have the best team in their store to serve their customers and so we are very focused on the leadership components on the customer service that we talked earlier, and particularly on the engagement of our colleagues. We have just completed for the first time in a while actually the ability to speak to so many colleagues in our business. So we think we have had the highest participation rate of any colleague engagement survey in the UK in the last few weeks. And all of those colleagues talking to us mean that we really want to make sure our managers are listening to what their colleagues say so we can give you better customer service.

So in answer to your question it is leadership, it is customer service focus and it is colleague engagement. And if we do that in our stores we will serve our customers better.

Maria-Laura
Thank you.

<u>Question 3</u>

Charlie Storey, Citadel
Charlie Storey, Citadel. You mentioned your cost as a percentage of sales opportunity, I think it was 150 basis points. And you said before that you have not phrased it like that before. Is that you flagging to us that you see a margin recovery opportunity that you haven't seen before? You used to talk about 3-3½% EBIT margin when the world was a bit different a few years ago.

Answer: Mike Coupe
I don't think you have heard us say that at all. I think we have tried to steer away from, in fact we are steering away from giving direct margin targets for obvious reasons and I go back to what I have already said in answer to some of the other questions. We are in a notoriously unpredictable set of circumstances within the UK economy and the potential knock-on impact to our customers could be quite significant. And nevertheless for all the reasons that we have talked about, we think we have the capacity to structurally reduce the costs in our organisation. How much of that goes back to our customers is really, really difficult to predict and ultimately what we want to give you reassurance about is that we have all the levers that we can possibly pull in our control. But the things we can't control is what is going to happen to the economy and whether or not our friends from Germany or Cheshunt or wherever they live now do a whole bunch of stuff that you know creates more noise in the marketplace. But as I say, in the end we believe that we have got robust plans that can deliver earnings over time, cash flow and therefore pay dividend etc.

That aside, if you believe the numbers you can model all sorts of scenarios that look fantastic, but my experience in the last five years is that no matter how many times I look at that hockey stick it never quite comes through because something happens. And therefore I think we are better to be conservative and be realistic in our outlook.

Charlie Storey
Okay, thank you.
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<u>Question 4</u>

Andrew Gwynn, Exane
Andrew Gwynn from Exane again, usual suspect. Let's go for three questions. The first question is for Kevin. I have got a bit of missing cash flow I think. You have increased the cash flow target by 150, but you have increased or decreased the pension contribution by 150 and obviously now there are no more payments into the Bank?

Answer: Kevin O'Byrne
The original. When we set the target of £600 million plus, I had line of sight of the pension cash improvement because we effectively had an agreement with the Trustees, we just hadn't got the HMRC sign-off. So that was in that £600 million. So it was there.

Further question
Okay fine. So that is one question. The other one was choose one, I suppose of all the things that you think could step change your business over the next five years, which of the things you have spoken about today could be the one that might do it?

Answer:
I think the thing that is a defendable source of competitive advantage is all the work that we are doing in the digital space now. We can make it as broad as you want. I mean I could give a very glib answer, it is all of that stuff. But you know you go back round the opportunities to monetise data, real time access to customers wherever they are in our ecosystem, the simplicity of joining the offer together. Being able to anticipate that you are having a barbecue at the weekend because you have a barbecue every time the temperature gets above 23 degrees because we can see that in the Nectar data.

All of those kind of things are realistic, are real in our business in the foreseeable future. And it is the connectivity of all of the above and the work that we have been doing behind the scenes to use data and digital connectivity that will drive that experience. And as I say I genuinely believe that this is unique, not just in the UK, but in the world more widely.

Further question
And then the last one is on the Bank. Maybe a question also for Mike, but it was my understanding on the Bank that you had created a bit of a fixed cost monster in some respects. Obviously transitioning to its own platform and therefore it needed assets of round about £10 billion. Obviously to get to assets of £10 billion you would need more capital and obviously that is clearly not the message today. So how can you manage down the cost base without managing up the asset base?

Answer: Jim
So it is true that there is a significant amount of cost that is fixed particularly around the IT piece so infrastructure from the migration programme. But having said that, there is a significant amount of cost that is not fixed that we can address. So for example without getting into too much detail on it. We have not yet integrated the backend or middle office, back office for example between Bank and AFS as one example. There is an opportunity you know for example when we stop mortgages, there is a significant cost to take out as well. Also around reshaping the entire organisation, there is an opportunity around there,

course into consolidation etc. etc. So there are quite a number of things that we have already identified and many more.

The key for us is really around sequencing them and how we actually execute them. If you look at a lot of consumer finance organisations. Their cost:income ratio is significantly better than 50%, the reason why we haven't gone below that is because of the fixed costs you are talking about. And that doesn't preclude us from trying to renegotiate contracts which we would look at, but contracts are contracts. So that is really the story.

Further answer: Mike Coupe
And from a top line view, I have been in rooms like this too many times where we have made promises about the Bank that we haven't been able to fulfil. And you know part of the challenge to Jim is to give us a plan that is if anything on the low ball side and brings the level of conservatism in what the art of the possible is.

Now there are all sorts of, again, dynamics within the marketplace that could make the delivery challenging, not least the regulatory situation, but we are starting with what I think you would see as a relatively "D-Risk" plan?

Answer: Jim
Yeah absolutely. I mean it is all about getting the plan executed and I think you know in 90 days we have done the strategy, we have already made one big strategic decision which allows us just from that to take out costs, improve margins and so on. So there is a whole range of other things that we have got to do. But it is about getting the plan implemented and we have started, basically.

Andrew Gwynn
Thank you.

<u>Question 5</u>

Rob Joyce, Goldman Sachs
Rob Joyce again from Goldman Sachs. Sorry Kevin I am going to ask about this cash flow again quickly. So about 250 of retail free cash after divvies, you got into flat PBT, so 750 over three years makes sense. But then I am sort of getting 50 less pension, 100 less going into the Bank versus last year, 100 fewer exceptional I think as well. You know a lot fewer exceptional?

Answer: Kevin O'Byrne
I would just say Rob, have a look at your maths. We generate, let's say you take your 640-630 whatever profit, then take, add back depreciation, take off capex, refund the pension scheme roughly whatever, 76. We pay our tax, we pay our interest. You know you get to that number, you can see. And then there are some one-offs and we talked, we guided this year to one-offs being around £100 million of cash. So we have that currently. As we take out some of the structural costs we are anticipating, there will be some one-offs, I have got that built into the cash figure we are talking about.

But I think, you know, in a normal year this business would probably generate £400 million, pay £250 dividend, £150 million, we are saying we are going to do more, we are going to do about £200 million. If you just do it. So we can spend a bit longer and go through it, but, and we are saying £750 million is the at least number, but the numbers work.

Further question
Fair enough, apologies for that. And quickly on the pension. Just what has sort of really driven that big decline in the pensions? Obviously, is it at yields at March ’18? Or the triennial pension deficit?

Further answer: Kevin O’Byrne
Yeah well there are a number of factors, pensioners who have left the scheme. We have probably dropped about 10,000 pensioners. Some have died, but some have left and taken their funds out. We have better returns on the scheme. We have contributions to the scheme. There is a combination of those factors.

Rob Joyce
Thank you.

<u>Question 6</u>

Nick Coulter, Citi
Thanks, Nick Coulter from Citi with two, last of the day. One each if I may although I am a bit scared that Kevin might tell me. On the Bank targets, you said it is about total financial services which obviously draws from both AFS in Retail, but also the Bank. In terms of keeping promises in the future will you be able to just actually see that combined profit pool growing over the future years?

Answer: Kevin O’Byrne
Well we showed it to you today. I guess we probably could, we haven’t in the past. The thing you have got to be careful though. When you look at the AFS profit in Argos, because remember it is effectively a gross margin on a product. So we could show you the gross margin on televisions and it would be a very big number. Gross margin on toys would be a very big number. So you just have to be careful, we are comparing a gross margin with a bottom line profit. You couldn’t generate those profits if you didn’t have stores online, customer contact etc. So there is a whole machine that generates that gross margin. But we will talk about financial services total returns on financial services going forward.

Further question
Yeah I guess the point is, if you are including that in your target then we need to have?

Answer:
Yeah that’s right, but the reason. We are for obvious reasons very conscious of disaggregating all of the various profit streams in the business. And going back to multi-channel, multi-brand, you can start getting to all different ways you might cut and paste the various contributions. You take Nectar as an example, you know the Nectar scheme wouldn’t exist unless the supermarket existed, but it clearly makes money. So how we attribute that and how we think about that is clearly quite sensitive within the organisation. But we will endeavour to give you the right level of disclosure so you can see that we are delivering against what we said we would deliver.

Further answer:
Nick one point. The point I was trying to make there, maybe too subtly was in the past we might have been accused of growing a Bank. We are not interested in growing a Bank, we are interested in growing financial services as an income stream that helps our customers shop in our stores etc. So hence we will talk more about total financial services.

Further question
Great, thank you that’s very kind. Then lastly, a strategic one if I may Mike. A lot of the Presentation has been quite future facing and I think you yourself have kind of

acknowledged an intergenerational shift towards online. When we look at something like the US grocers, Walmart are working with Alerts, Kroger are working with Ocado. Albertsons and Arhold are working with Take-off as an automated solution. Do you think you will look at micro fulfilment centres or how do you think your fulfilment will pan out over the next few years?

Answer: Mike Coupe
Yeah I mean we, without getting too carried away on what the art of the possible is, inevitably lots of companies will be talking to us and we will be talking to lots of companies about a whole series of opportunities. We can spend hours debating the rights and wrongs of Ocado getting into bed with Kroger. But in the end we are starting from a position of actually having a very strategically well placed fulfilment model even from our existing infrastructure. If over the next period of time you start looking at different fulfilment models and that is certainly something that we have talked to other third parties about, that certainly represents an opportunity. And it is self evidently the case that if you take somewhere like Hedge End, it has a massive amount of Warehouse space with access to literally hundreds of thousands of customers in this area. And at some point you might choose to redeploy that space differently. It is not immediate, you know we are actually doing trials with Diliveroo, which will be another example, you know I am not saying that is the right answer to the question, but it is an alternative to our own home delivery model which we have trialled through, through Chop Chop.

So we are very conscious of the opportunities. Again we think we are building the intellectual properties to be able to protect ourselves rather than necessarily partnering with third parties. It doesn't mean we wouldn't partner with third parties where it is appropriate. But I go back to the asset base that we have built. You know the reason why people are getting into bed with some of the people you are talking about is because they haven't gone through the process. They are starting a long way behind the curve and we actually have a lot of the infrastructure in place having invested quite heavily over the last 3,4,5 years in the base plan.

But we never preclude the opportunity and there are plenty of people out there with lots of money, very keen to access all sorts of parts of our business. And we will be very thoughtful about it if we were to ever partner with anybody.

Nick Coulter
Super, thank you.

Closing Remarks
Mike Coupe
Good. I think we are through. So I know it's not in your nature, but can you give the Presenters a round of applause because they have worked extremely hard. There were just a few moments when I thought we might get a spontaneous ripple, but it didn't quite happen. But anyway thank you for your indulgence. Hopefully we have gone through at pace and with energy. And I am now going to hand over I hope to James who I think is going to tell you how you are all going to get home. So thank you for your attendance today.

End