Centrica plc 2017 Preliminary Results Announcement
Thursday 22 February 2018

Iain Conn – Group Chief Executive
Well ladies and gentlemen good morning and thank you for coming to Centrica's 2017 Preliminary Results Presentation. This morning we will be reporting on our 2017 results and also providing an update on the implementation of our strategy. I should forewarn that this presentation will probably last about an hour and twenty minutes, slightly longer than normal given a number of things we want to address.

But first a word on safety in this building. There are no planned fire alarms today and any building evacuation will be announced by tannoy. Emergency exits are marked at the front and rear of the auditorium and Goldman Sachs staff will direct you to the muster point which is towards the rear of the building on the junction of Stonecutter and St Brides Street.

Let me now provide a summary of where we stand and what we will be addressing today before Jeff takes us through the 2017 results in detail.

Our performance in the second half of 2017 was weak, particularly in business energy supply. This weak performance announced in November at the time of our Trading Update combined with uncertainty around our future prospects in UK energy supply significantly amplified by the Prime Minister's announcement in October that the UK Government would pursue a market wide price cap of the standard variable tariff and other default tariffs taken together resulted in a significant fall in our share price in 2017 particularly over the fourth quarter. Some of the drivers were clearly beyond our control, but I regret the outcome deeply and the impact it has had on our shareholders. I am determined to restore shareholder value and remain firmly of the view that Centrica's strategy can and indeed will deliver attractive total shareholder returns. We have excellent people, assets and market positions and are one of the companies shaping change in our markets at least as much as we are being shaped by it.

Our focus in the near term is on performance delivery, managing through the political and regulatory uncertainty in the UK and maintaining the strong balance sheet which we've worked so hard to achieve. Although we delivered our 2017 published targets in terms of operating cash flow, cost efficiency and headcount reduction, capital discipline and net debt, our financial results in the second half of the year were weak with a material miss in North America Business. This was both in terms of the performance of our power supply book and from a charge relating to historical revenue recognition in one of our billing systems going back to 2013.

Performance in UK Business energy supply was also poor. Given this performance and uncertainty over our future prospects, I do recognise there are important questions arising from 2017 which we are aiming to address today. Let me come to these in a moment.

In 2015 we embarked on a return to the core of Centrica, energy supply and services, and there are clear and encouraging signs of progress. At the end of 2017, phase one of Centrica's repositioning has been completed. We have materially repositioned the asset businesses and delivered on our £750 million per annum cost efficiency programme three years early. We ended 2017 with a strong balance sheet with net debt at £2.6 billion in the lower half of our end 2017 target band and our credit metrics at levels in line with our target strong investment grade credit ratings.

As we look forward to 2018 to 2020, although we have still got some portfolio repositioning to complete, the focus is on performance delivery and financial discipline. In performance terms it is about growing gross margin through our customer relationships and driving the next phase of cost efficiency. Today we announced an increase cost efficiency target of £1.25 billion per annum by 2020 relative to 2015. Representing additional efficiencies of £500 million per annum.

Despite the uncertainties we face in the UK energy market we are also targeting to deliver on average £2.1 to 2.3 billion per annum of adjusted operating cash flow over 2018 to 2020 and to keep net debt in a band of £2.25 to 3.25 billion designed to accommodate a range of scenarios and commodity prices and being consistent with maintaining our strong investment grade credit ratings.

In terms of the dividend, we have indicated since 2015 that it would be linked to operating cash flow and we expect to maintain the current level of dividend over the period 2018 to 2020 subject to meeting these operating cash flow and net debt targets. I will return to forward guidance later in the Presentation.

Let me now turn briefly to 2017 financial performance. Adjusted operated profit at £1.25 billion was down 17%. Earnings were down 22% at £698 million equivalent to 12.6 pence per share. Adjusted operating cash flow was £2.07 billion. EBITDA of £2.14 billion was down 9%. Centrica Consumer delivered robust performance with adjusted operating profit down only 1% despite the impacts of warm weather, the UK Government pre-payment cap, competitive intensity and investing for growth. Centrica business saw adjusted operating profit down 67% reflecting the very poor performance in the energy supply business units. I have already covered our efficiency programme delivery and net debt at the end of the year.

Finally we announced a full year dividend of 12 pence per share unchanged on a year earlier. I recognise that 2017 has given rise to a number of questions about Centrica's performance and uncertainty about our prospects in the face of stiff competition and political and regulatory intervention in the UK. Therefore after Jeff has presented the 2017 results, I will provide a strategic update designed to address the following questions. We know these questions are on the minds of a number of you and it should not surprise you that I have also been reflecting on them. I will review our strategy and how the component parts combine to reinforce each other as we deliver for our customers. This will include looking back at Phase I of repositioning Centrica and the priorities we see for the next phase.

Delivery of cost efficiency has been a material part of underpinning our performance over the last three years and we will outline the role it will continue to play in offsetting competitive pressures on gross margin. I will address the resilience of Centrica in the face of strong competitive pressures and the specific issue of a potential price cap in the UK energy market. Although there remains uncertainty, I will explain why we believe that the actions we are taking will improve the market and allow us to maintain a healthy and attractive business in UK Home Energy Supply.

I will cover the customer account losses in consumer, our focus on value not volume and the relationship between customer numbers and gross margin. I will also describe how we are doing in growing gross margins through customer facing propositions other than energy supply. There are some very encouraging indications of growth potential.

Jeff and I will share our findings and response to the issues in North America Business we encountered in the fourth quarter of 2017 and why it remains an important part of the Portfolio. We will cover our intentions and the outlook for both exploration and production and our Nuclear shareholding. We will also address the capability we are building for the future needs of our customers and our attitude towards acquisitions and disposals before finishing on our financial framework, sources and uses of cash flow and 2018 to 2020 guidance including the outlook for the dividend.

Taken together I hope this will help substantially in answering many of the big questions on the minds of those who follow Centrica. Let me now hand over to Jeff to take you through the 2017 Results.

Jeff Bell – Group Chief Financial Officer
Thank you Iain and good morning everyone. Before getting into the financial results, let me first start with the backdrop of commodity prices and weather. First commodity prices. Brent Oil, NBP Gas and base load power prices were all significantly higher on average than in 2016 and remained in the band between the 70-50-50 scenario from the time of the 2015 strategy review and our 35-35-35 low case.

With respect to weather, temperatures in the UK were warmer on average compared to 2016 resulting in lower energy consumption. In North America temperatures were slightly colder. However more significantly there was limited gas price volatility which reduced optimisation opportunities for North America Business.

Let me now move onto the financial headlines. Revenue was up 3% which included a full year of NEAS Energy revenues following its acquisition in October 2016, partially offset by the impact of lower average customer holdings compared to the prior year.

As you just heard from Iain, adjusted operating profits fell by 17 per cent to £1.25 billion reflecting significantly reduced profit in Centrica business. Adjusted earnings also fell to £698 million. Including the net effect of higher interest costs and a lower effective tax rate driven by business profit mix, US tax rate changes and tax provision releases. Adjusted basic earnings per share was 12.6p and the full year dividend per share is 12 pence.

On cash flow EBITDA reduced by 9% to £2.14 billion in line with the reduction in adjusted operating profit. Adjusted operating cash flow fell 23% to just over £2 billion inclusive of the one off working capital inflow in UK Business in 2016 of £357 million. Adjusting for this and for foreign exchange and commodity price movements, underlying operating cash flow fell 13 per cent compared to 2016 and on a cumulative basis is broadly flat since 2015.

Group net investment which includes over £800 million of disposal proceeds in the year fell to £46 million and reflecting this net debt fell to £2.6 billion. Return on average capital employed was 14% above the 10-12% boundary contingent set out in our financial framework. A net post tax exceptional charge of £476 million was recognised in 2017 predominantly relating to impairments of E&P assets and the Rough storage asset, but also including profits and losses on disposals from our divestments and restructuring costs incurred as part of our group wide cost efficiency programme.

Returning to adjusted operating profit, here you can see the split across our customer facing divisions with Centrica Consumer profit about flat compared to 2016 but significantly down in Centrica Business. Profit from our asset businesses was up primarily reflecting increased production at Rough following the change in its status from a storage asset to a producing gas field.

Looking now in more detail at Centrica Consumer where operating profit fell slightly to £890 million. UK Home profit was up 1% to £819 million. Within this Energy Supply profit was up 3% to £572 million with strong focus on cost efficiency and a focus on more valuable customer segments more than offsetting a reduction in account holdings, warmer weather and the impact of the pre-pay tariff cap.

UK Services operating profit declined by 4% to £247 million. A strong cost efficiency delivery was not able to fully offset a 10% fall in gross margin from the lower average customer holdings and increased pension costs. Ireland operating profit was at a similar level in both sterling and Euros with the impact of competitive market conditions largely offset by cost efficiencies.

North America Home profit increased to £119 million up 28% in sterling and 26% in dollar terms reflecting reduced losses from the closure of our residential solar business. A focus on more valuable customer segments and cost efficiency measures. Total cost per customer was down 2%.

In Connected Home, gross revenue increased by 27% to £42 million reflecting growth in the volume of products sold and the diversity of customer offers. With incremental investment in the development of products, platforms and apps, the business reported an increase to operating loss of £95 million. We expect 2017 to be the peak year of losses in Connected Home as continued revenue and gross margin growth will outstrip operating cost investment.

Overall Centrica Consumer operating cash flow declined by 16% to just over £1 billion mainly reflecting the timing of working capital flows.

Here is more detail on the drivers of year on year changes on adjusted operating profit in Centrica Consumer. External factors specifically weather, foreign exchange movements and the impact of the pre-payment tariff cap reduced operating profit by around £134 million. As I just mentioned, we say an increased operating loss in Connected Home due to our choice to invest ahead of growth. Another like for like change reflects the loss of customer accounts. However our efficiency programme delivery of £219 million largely offset these factors.

Now let me turn to Centrica Business where full year profit was down 67% to £161 million. Adjusted operating cash flow fell 43% reflecting working capital recovery in 2016 in UK Business and materially lower operating profit in North America Business. Profit was down in each business unit and I will cover the drivers of decline in the energy supply businesses, Distributed Energy and Power and Energy Marketing and Trading in the next few slides.

In Central Power Generation, operating profit was down 53% to £35 million principally reflecting 2% lower generation volumes and a 4% fall in realised prices in our Nuclear joint venture results. In a similar format to Centrica Consumer here are the primary drivers of the year on year reduction in Business operating profit. External factors, the combination of warmer weather, foreign exchange movements and commodity price changes had a small negative impact of £8 million. Our choice to invest in Distributed Energy and Power growth and dispose of our wind farms and CCGTs reduced our operating profit by £35 million. However we benefited from £55 million of cost efficiency. But nearly all of the change versus 2016 was driven by like for like decline with poor performance in UK Business and North America Business in the second half of 2017. Lower profits from our flexible legacy gas contracts in Energy Marketing and Trading and lower output in realised prices already mentioned in Nuclear. Let me now take you to these in turn.

First UK Business profit fell in 2017 as the reduction in gross margin was not sufficient to offset lower operating costs from the efficiency programmes and an improved bad debt charge, both of which were enabled by strong operational performance. The gross margin

decline reflects a 9% fall in customer accounts due to high levels of market switching, lower unit gross margins from continuing competitive intensity on acquisition and renewal pricing and the affect of high wholesale electricity costs in the first quarter of the year.

Against this competitive backdrop we are focusing our attention in acquisition activities on the higher value, small and medium enterprise segments with further development of our online offerings, greater emphasis on customer segmentation and value and increased cross sell with services and energy. As a result of these actions we would expect to see a recovery in UK Business operating profit back towards 2016 levels in 2018.

In North America Business the operating profit decline was driven entirely by the fall in gross margin, slightly offset by lower operating costs. For the gas supply business, consumption was broadly flat while warmer weather in the first and fourth quarters reduced the opportunity for wholesale optimisation. And as a result total gas unit margins declined slightly.

In electricity supply we saw a 7% reduction in customer consumption partly driven by a 3% fall in customer sites, but also the impact of increasing energy efficiency measures. In addition the unit gross margins fell by nearly 50%. Approximately half of this fall in unit gross margins was due to a £76 million pre-tax one-off charge relating to a re-assessment of a historic recognition of unbilled power revenues with the other half reflecting a number of factors which I will describe shortly. As a result total North American gross margin fell by just over £$00 million year on year shown in the chart on the left hand side of the slide. Total gas gross margin declined by about 40 million dollars reflecting the lower optimisation opportunities I just mentioned.

However the biggest driver of reduced profitability in 2017 was the power supply business shown in light blue on the chart. This reflects the lower unit margins and volumes seen on the prior slide as well as the one-off accounting charge.

The North America Business power supply margins were significantly lower due to a combination of factors impacting the business at the same time. They included heightened competitive intensity, depressing acquisition and renewal margins and changes to the market structure and related input costs including higher unit capacity market charges.

Realised margins were also impacted by reductions in customer volumes as commercial customers increased their take-up of energy efficiency measures including distributed generation. Lower customer volumes also meant that unitised non-commodity costs were under recovered.

Finally management actions in response to these pressures were hampered by poor visibility in our load forecasting and risk management systems due to the magnitude of internal change projects concurrently underway.

In response to these issues and the inherent risk exposure in power supply, we have undertaken a full review and investigation and the Business is implementing a number of changes. These include a new standard product offering that more closely matches input cost recovery. Completion of system enhancements to provide greater granularity of gross margin drivers and improvements to the processes and controls around load forecasting and risk management and improving the level of capability. The aim of these actions is not only to improve the profitability of the power business but also to reduce its volatility. As can be seen on the left hand side of the slide, the performance of the gas business with its physical asset positions and contract flexibility has meant that gross margin delivery even in years of extreme weather and volatility like 2014 during the polar vortex has remained within a narrow range. The power business is more effected by extreme weather and the knock on impact that has to electricity price spikes and ancillary charge increases, where unlike gas we don't

have the assets and positions to optimise and mitigate adverse factors in the same way. As a result we have seen more volatility in gross margin in recent years and is why we are taking actions with respect to the products we sell and the risk management processes we have in place.

Going forward we expect unit power margins to remain at 2017 levels this year. And therefore after adding back the onetime accounting adjustment we anticipate limited growth in underlying operating profit in North America Business in 2018.

Moving now to Distributed Energy and Power and Energy Marketing and Trading. In Distributed Energy and Power revenue and gross margin were both up in 2017 reflecting organic customer growth and a full year of results from ENER-G Cogen which was acquired in May 2016. Although the segment operating loss increased to £53 million driven by planned incremental investment in growth, we are seeing good momentum on building the future order book and recurring revenue streams. We expect Distributed Energy and Power to deliver continued revenue and gross margin growth in 2018, although unlike Connected Home, we will continue to make further investment to drive this growth and therefore expect the current year operating loss to be similar to that in 2017.

Energy Marketing and Trading reported a 35% reduction in operating profit despite continued gross margin expansion from the core route to market trading and LNG activities. The capabilities we have build up over the past three years as well as those acquired with Neas Energy leave us well placed to deliver ongoing growth in these areas going forward. Neas in particular is delivering well ahead of its ahead of its investment case. However as you can see from the chart on the right, the level of gross margin from our three flexible legacy gas contracts which we have been optimising for value since the demerger declined. This will be a continuing trend as the two most profitable of the legacy contracts end during 2018. The one remaining contract is expected to be loss making this year based on the current commodity price input that make up the contracts commercial terms. This will create a year on year headwind for Energy Marketing and Trading operating profit in aggregate this year. And we would expect 2018 operating profit to be no more than the level of 2017.

Moving on to E&P which following the disposals of our Canada and Trinidad and Tobago assets in the formation of Spirit Energy will be focused on our European gas operations. Overall production was down 14% to 61 million barrels of oil equivalent, principally reflecting the impact of the disposals. Production in Europe was down 5% as a result of our decision to undertake asset integrity works at Morecambe to help improve safety, operational efficiency and underpin the residual life of the asset.

Production from the rest of the European portfolio was similar to the prior year with gas from Cygnus which came on-stream last December offsetting the impact of the natural decline in the rest of the portfolio. In 2018 we expect production from Spirit Energy to be in the range of 50-55 million barrels of oil equivalent. Gas and liquids achieved sales prices were up in the year which offset the lower production volumes and therefore realisations were in line with 2016. Operating profit was also commensurate with 2016 as total cash lifting and other production costs and DDNA were higher on a per unit basis but with lower overall volumes which therefore broadly offset each other. In 2018 we expect Spirit Energy unit cash lifting and other production costs to be similar to Centrica's in 2017.

Adjusted operating cash flow fell 32% to £448 million reflecting higher decommissioning spend and the phasing of Norwegian tax payments between years. However E&P was still cash flow positive even excluding the impact of disposals.

Centrica Storage reported an operating profit of £17 million for 2017 compared to a loss in 2016. This reflects better well performance and stronger gas production volumes at Rough

following its return to service and the decision to produce a portion of the Cushion gas for safety reasons in the fourth quarter. Having received final consent in January 2018 to change Rough status from a gas storage facility to a producing asset we would expect it to produce 8-10 million barrels of oil equivalent of gas in 2018. Going forward we will report both Spirit Energy and Centrica Storage in one E&P performance segment.

Turning now to costs. Total reported operating costs were down 7% in 2017 after adjusting for items such as depreciation and amortisation, impairments, smart metering and portfolio change to get to a like for like number, adjusted operating costs declined 5%. And after excluding growth investment they were down 7%. This reduction reflects the progress made in our £750 million cost efficiency programme and including controllable cost of goods sold, we delivered a further £308 million of efficiencies in 2017.

Foreign exchange movements impacted our 2016 baseline by £83 million. While inflation added a further £103 million. However when also including other net savings, not part of our efficiency programme, total like for like controllable costs were 3% lower in 2017 than they were in 2016. The efficiency savings delivered are from a combination of the annualisation of 2016 savings and new 2017 initiatives, including the transformation of our customer operations, the utilisation of digital and technology capabilities to enhance customer service and reduce call volumes and the creation of a more integrated field operations model to drive efficiency and further supply chain improvements.

We also saw a continued reduction in our global functions cost, as shared service operating models became more embedded and the procurement function continued to leverage the Group's scale to reduce 3rd party costs. Viewed over the last two years and excluding the £103 million of cost efficiency delivered in the second half of 2015, we have delivered just under £700 million of efficiencies over the last two years. And when including the end 2017 run rate which will deliver £54 million of additional annualised savings in 2018, we have delivered on our £750 million cost efficiency target and we have done so significantly ahead of our original 2020 time frame. Iain will talk about the next phase in cost efficiency in his Presentation later.

Moving on to net investment. Total capital expenditure increased 12% to £943 million. With the acquisition of Restore and the development of merchant assets and Distributed Energy and Power more than offsetting a £79 million reduction in E&P capex to £439 million. Towards the bottom end of our targeted £400-600 million range. As I mentioned earlier, total net investment was only £46 million after taking into account £819 million of disposal proceeds predominantly relating to the sale of the Lincs Windfarm, Langage and Humber CCGTs as well as Canada and Trinidad and Tobago E&P assets.

Turning to cash flow the disposal proceeds were a material contributor towards the net cash inflow of £939 million. As already referenced EBITDA fell by £223 million or 9% which when combined with a return to a more normal level of working capital in UK Business resulted in a decline in adjusted operating cash flow of £617 million. Cash interest payments increased in 2017 in the absence of net realised foreign exchange movements and a one-off interest benefit relating to the GLID Windfarm disposal in 2016. While a higher scrip take-up on the first half dividend payment resulted in lower cash dividends paid. Other cash flows were down slightly with lower exceptional payments.

I wanted now to turn to the Group's balance sheet. We have been very successful in reducing net debt over the past three years, although given the maturity profile of our debt this has resulted in an inefficient cash to gross debt mix. Reflecting this, we have announced today a £600 million to £1.1 billion debt repurchase offer. Including the one bond due to mature in 2018 we forecast an aggregate reduction in gross debt of £1 – 1.5 billion by the end of the year. We currently expect this early repayment will result in a one off exceptional

interest charge and cash outflow of between £80 and 140 million and generate annual interest savings of £25-35 million per annum and £250 to 400 million in total over the life time. With the range in both cases depending on the amount of debt we will purchase. This will materially improve the efficiency of our Balance sheet.

Finally I will cover credit metrics. We said at the start of the year we were targeting to be at or above the financial metrics currently required for our existing investment grade credit ratings. As a reminder our rating with Moody's was Baa1 with stable outlook and BBB+ with negative outlook with S&P. We estimate we have achieved the target financial matrix at the end of the year although of course the final calculations of the 2017 numbers are yet to be confirmed by the rating agencies which they consider alongside other qualitative and business risk factors in determining the overall rating.

With that let me hand it back to Iain.

Iain Conn – Group Chief Executive
Thank you Jeff. As I outlined earlier in this second part of the Presentation I will provide a strategic update and in so doing also hope to address these key questions on the subjects of strategy and performance.

Let me begin with a summary of Centrica's purpose and strategy. Centrica is an energy and services company and our purpose is to provide energy and services to satisfy the changing needs of our customers. This is the core of the company and we have been supplying energy and services to customers since 1812. We are re-emphasising and returning to that core. However it is not 1812, the needs of our customers are indeed changing and as we deliver for them, the propositions we offer must change too.

The reason for these changes in customer needs arising from three fundamental trends which have risen significantly as a result of the response to climate change and advances in digital technology. First the energy system is becoming decentralised as new renewable technologies are developed and become viable with many deployed at smaller scale and nearer to the point of use.

Second, customers have more and more choice of how they can obtain energy supply and the services they wish to see alongside it. This means that power, influence and rent is shifting towards serving the customer.

Third digitisation and technology developments are accelerating the changes enabling much more sophisticated management of the distributed energy system. And enabling customers to have more control over their energy, their services and the management of them.

In response as an energy and services company, Centrica's strategy is to deliver for the changing needs of our customers. We aim to deliver long-term shareholder value through returns and growth, be a trusted corporate citizen, an employer of choice and to become a 21st century energy and services company.

Centrica is therefore directing more investment into the customer facing businesses. Centrica is also becoming simpler. We now only have three divisions, Centrica Consumer, Centrica Business and Exploration and Production. Each has a clear participation strategy and strategic framework. The vast majority over 90% of our gross revenue and gross margin generation is within the customer facing divisions. In 2017 unit gross margins on revenue were over 20% in both the consumer division and exploration and production. Although much lower than this in Centrica Business overall. Distributed Energy and Power and parts of Energy Marketing and Trading also exhibited high unit gross margins.

The reason we have established Group wide consumer and business divisions is because we have found that customer needs are very similar globally and many are seeking more than simply energy supply. Indeed pure energy supply is commoditising and energy use per unit GDP is falling. In response we have built new capabilities and propositions in both divisions and the divisional structure enables Centrica to be more scalable, replicable and efficient.

Finally there are significant opportunities for growth associated with adding new propositions to energy supply with high unit gross margins. Technology is increasingly important in our propositions and our customers whether consumers or business customers are responding very favourably to new digital platform offerings and innovations. The world of energy supply and services is on the move driven by the customer and we are responding accordingly. We have developed the capabilities to deliver and established clear, strategic frameworks for each of consumer and business.

This is the strategic framework for consumer. The anchor of our business has always been in energy supply and in in-home installation and servicing whether on demand or through protection plans and warranties. This remains the core of our business today. Through installing boilers, heating and cooling systems, their meters, thermostats and controllers, we have always been in the home energy management business. As boilers become more intelligent and home energy management becomes more digital, with data analytics providing new insights and opportunities for the customer, we have had to develop the ability to install and maintain new home energy management systems. This led to the development of Hive, starting with the digital thermostat and the intelligent boiler, Boiler IQ. Hive is the next phase of evolution of home energy management and a direct extension of our in-home servicing capabilities. Hive Home Energy Management requires a digital hub to be installed in the home and our customers are asking for other home management applications which can be easily served from the same hub. These are in areas of home security, remote diagnostics and home automation.

Simply stated, consumers want the propositions within our four services pillars and are willing to pay for them. We are also finding that many consumers value receiving these services from the same provider as their energy supply, either separately or as part of a bundled offer. As a result growth in services including Hive, is a natural extension of who we are and what we are good at. Our customers want it, like it and it reinforces them and leverages the historic core offerings of the company.

Similarly in business we find that in addition to the commodity offerings of energy supply and energy wholesale, business customers are wanting access to more distributed energy generation solutions and we are moving from building large central power generation plants to many more smaller distributed units. Our customers want combined heat and power units, solar and the grid operators want distributed power systems and technology to assist with the optimisation of local energy markets and micro grids. Along with this, customers want to be able to gain insight from their energy use to save money and improve their operations including in preventative maintenance.

Customers who have distributed energy assets want to be able to optimise them and are willing to pay for optimisation services rather than do it themselves. The business customer is therefore also on the move and we are responding to their needs. They want more than just commodity energy supply and the new capabilities and propositions we have developed once again reinforce the core of the relationship.

Finally the returns in value added services tend to be higher than in pure commodity energy supply. The big message therefore, whether in Centrica Consumer or Centrica Business is that the new propositions and services that we have developed are not a distraction or somehow unrelated to our legacy businesses, they are to the heart of what our legacy businesses now have to incorporate. They are to the heart of what important and valuable customer segments are demanding.

The good news is that Centrica has developed the capabilities to offer them in a high quality way. We are seeing improvements in the customer experience and the growth in demand is feeding through to revenues and at attractive margins.

I would now like to summarise what has been delivered during the first phase of the strategic repositioning of Centrica. As at the end of 2017 we are on track with the objectives we laid out in 2015. We have already reduced the resources allocated to the asset businesses by £1.5 billion through lowering our capital investment into exploration and production by £300 million per annum and with divestment so over £900 million, towards the top of our target range. We have created a new exploration and production joint venture, Spirit Energy which will allow Centrica to participate in a stronger and more sustainable business while limiting our exposure. We have sold Canadian E&P, our wind assets, large UK CCGTs and resolved the future of Centrica Storage.

We have in turn so far invested approximately £700 million into the customer facing businesses as we improve service, develop new propositions and build capability both organically and through targeted acquisitions in response to the customer needs I described earlier. We have delivered on our material cost efficiency target of £750 million per annum three years early.

Finally, we have maintained financial discipline and in each of the last three years we have ensured organic sources and uses of cash flow were more than balanced. And with the proceeds from the divestment programme we have strengthened the balance sheet so that net debt is now towards the bottom of our targeted end 2017 range.

Let me now turn to what we need to focus on in this next phase. In the next phase to 2020 as we continue to focus the Group more on the customer and energy and services. Although there remains some portfolio issues to address, the main focus is on performance delivery and financial discipline. In performance delivery there are four key priorities we must deliver on and all at once. First and crucially we must demonstrate that we can grow gross margin through our customer relationships. Without getting to this place Centrica cannot grow cash flow. We can rely upon a significant contribution from cost efficiency in the near term but this must eventually give way to a higher proportion of cash flow growth from gross margin.

Second, and while we are improving gross margin capture and growth, in the near term we must therefore drive cost efficiency as hard as we can. During 2018 to 2020 we must aim to get as close as we can to being the most efficient price setter in our chosen markets, consistent with our targeted competitive position and brand. This is the basis for the next phase of our cost efficiency programme of £500 million per annum. Much of this will be focused on the UK in both our business units and Group functions.

Third, we must improve the effectiveness with which we operate and go to market. We have established a scalable platform but we must become more agile, collaborative and joined up.

And fourth, we must also work to secure the capabilities that we will need for 2020 and beyond. The energy and services world is changing rapidly, particularly in areas of digital and physical technology and we must have the capability to respond and develop new products and services. We must do all of this while continuing to deliver improvements in safety, compliance and conduct and in operational excellence across the company starting with customer service.

So this is the performance agenda for 2018 to 2020. It will require a huge amount of focus, determination and delivery. I am excited by the progress that we are already making and the momentum we are beginning to see.

I would like to begin with cost efficiency and we will return to gross margin in a moment. This slide shows the £750 million per annum efficiency programme delivery from 2015 to 2017 and then the additional £500 million per annum target we have announced today and which will be delivered between end 2017 and end 2020.

As you can see including other cost reductions outside of the core programme our actions from 2015 have resulted in a reduction of our overall nominal controllable costs from £5 billion per annum to £4.5 billion while eating adverse foreign exchange impacts and inflation and funding our growth. On operating costs alone, again the nominal costs at the end of 2017 are below those of 2015. The additional efficiency target will allow us to build on this track record and should materially offset gross margin pressures while aiming to drive nominal costs down further. We said in 2015 that by 2020 our nominal operating costs would be below those of 2015 having absorbed inflation and funded our growth and we are on track to deliver this.

So where will the additional £500 million per annum of savings come from? As in the period from 2015 to 2017, about two-thirds of the savings will be from Opex with about one third in the cost of goods. About 60% of the total or £300 million per annum will directly within UK Home in both energy and services and its supporting group functions. We estimate that in UK Home Energy Supply, the targeted efficiencies will deliver an improvement per dual fuel customer of £20 per annum by 2020 relative to 2017. These efficiencies will improve the underlying profitability of UK Home Energy Supply and will increase resilience in the face of any default tariff cap.

The new efficiency programme will involve an additional cost to achieve of £300 to £400 million and I regret it will also involve an additional direct headcount reduction of 4,000. This is in addition to the 5,500 direct headcount head count reduction to date, taking the total reductions to 9,500 or a quarter of Centrica’s end 2014 workforce. Against this will have created over 2,000 new jobs as we grow new propositions and businesses.

The new programme will be focused on the following areas: Meeting customers desire to self serve through digitisation of customer journeys, improving field operations supply chain effectiveness and efficiency. Using technology to improve productivity. Continue transformation of Group functions including finance and HR, IT system improvements and further procurement and supply chain efficiencies. The cost efficiency programme is the anchor which will underpin net margins and our competitive position while we enable top line growth which I will turn to now.

This slide shows the revenue, gross margin and gross margin as a percentage of revenue for both the consumer and business divisions. In Consumer, although revenue has been falling gradually as has gross margin, unit gross margins have been steady to rising slightly and have been over 20% in each of the last three years. Further as customer accounts have been falling, the gross margin per account has been stable to rising at £104 to £110. This is as a result of our focus on customer segmentation and on value, not volume. We are not focusing on customer segments and channels with negative or zero gross margin because these will almost certainly be loss making especially if there are not cross sell or up sell opportunities.

In Business gross margin has also been falling gradually. Unit gross margins are much lower at about 7% whereas gross margin per account was around £650 in 2015 and 2016. In 2017 for the reasons discussed earlier, Business unit gross margins fell materially because of the issues in energy supply. Business energy supply has high turnover, lower unit gross margins and can be volatile as a result of the impacts of weather and other factors. We will need to focus on reducing volatility of unit margins and improving consistency of returns in this area.

This next slide shows the number of customer accounts in Consumer. We have seen a fall of 1.25 million accounts over 2017. The majority of this reduction, 1.1 million accounts occurred in the UK and Ireland as shown by the dark section in each bar. Of the total fall across the Division, 85% or 1.17 million accounts in the yellow bar were either the result of choices we made to end channels or not to renew collective switch populations or customers switching away but in very low margin channels.

The gross margin impact of these 1.17 million account losses was £6 million. And therefore these accounts were loss making at the operating profit level. Given the nature of these customer segments and channels, I am convinced we could not have improved their economics. Losing these accounts was a major driver in the increase in gross margin per account I mentioned earlier. The higher value impacts are shown by the green bars where we have seen a net loss of 180,000 accounts which is actually an improvement of 96,000 relative to the 12 month picture we showed to the end of June as we saw growth in both British Gas Services and Connected Home, more than offsetting losses from other channels.

You can see we lost 195,000 pre-payment meter customers in the UK, added 373,000 in Connected Home and lost 358,000 other higher margin accounts. Of these higher margin accounts 214,000 were in UK Energy but we were successful in moving a net 700,000 SVT accounts onto fixed term contracts during the year in line with our stated objectives to encourage customers off the standard variable tariff. The total year on year gross margin impact within the core portfolio represented by the green bars was £128 million. Approximately half in energy supply and half in services. The pre-payment meter cap impact represented most of the year on year energy gross margin erosion. And in services it related to pension and environmental programme costs. It is our goal to stabilise the net position in the core portfolio and then begin to grow it. The unit gross margins in our profitable consumer channels are typically above 20%. And if we begin to net grow revenue from these accounts then we will begin to be able to grow gross margin in consumer.

Zooming in on UK Home and looking at the interaction between gross margin and cost efficiency, you can see that although gross margin has been falling over the last three years our cost efficiency delivery has been keeping pace with the gross margin decline so maintaining EBIT margins per account at about £39. Our goal is to focus on value, not volume at the gross margin level, while driving costs down to underpin EBIT margins. This is our focus across the consumer portfolio until we get to a position from which we can then net grow the total number of accounts. The resilience of consumer was demonstrated in 2017 with adjusted operating profit only falling by 1% despite intense competitive and regularity pressures.

The ability to maintain competitive pricing, healthy unit gross margin quality and drive cost efficiency is crucial in the face of the potential default tariff cap in the UK. Let me therefore turn to this major external uncertainty and how we plan to deal with it.

As you know the UK Government published a draft bill on a proposed temporary default tariff cap in October and this draft bill has undergone pre-legislative scrutiny in front of the BEIS Select Committee. We are against this intervention because we believe it is based on fundamentally flawed analysis of consumer detriment and will have unintended consequences including negatively impacting competition, customer choice and average prices for consumers. We have laid out our proposals for improving the UK's supply market without a cap in the 14 point plan which we published in November. Irrespective of whether a cap comes into effect or not, we will continue to push for all 14 points including those which we encourage the Government and Ofgem to implement. This includes levelling the playing field for market participants and removing energy policy costs from people's bills, something which is highly regressive.

Whatever the outcome, we are implementing the 7 points we committed to unilaterally. These will improve the market but also lower Centrica's exposure to any proposed cap. By March 31st, we will withdraw the standard variable tariff for new customers, introduce a new default tariff and measures to make it harder to end up on a default tariff. We will introduce new attractive fixed term propositions including fixed price, online only and bundled tariffs. British Gas rewards will drive customer loyalty and are already reducing churn.

Finally, we will continue to drive cost efficiency to ensure we are competitive with healthy returns even in a cap scenario. In the meantime we will continue to press the Government and Regulator on wider market reform.

So what is the risk to Centrica of a price cap? To understand this you need to look at our exposure, our competitive position and the result of our own cost efficiency plans. Firstly we had 4.3 million customers on SVT at the end of 2017. We are expecting to have reduced this to about 3 million by the end of 2018 as the measures I described a moment ago take effect. This will reduce our exposure to any cap.

Secondly, as a result of our own cost efficiencies to date, our current SVT is cheaper than 85% of the SVTs in the market and is £41 below the average of large supplier SVTs. As a result if we were to maintain this competitive position, any price cap will impact the majority of the market first before it impacts us. The impact on those with the highest of all SVT prices including some of the smaller suppliers will be even more significant. This £41 per customer provides a competitive buffer against the cap. When we introduce our new default tariff to replace the SVT which will happen by 31st March, we intend to continue to make it competitive relative to the market.

Thirdly, our efficiency programme will deliver an additional £20 per customer by 2020. In terms of financial projections, our forward plans assume declining underlying unit gross margins by 2020 and now also incorporate an assessment of a temporary default tariff price cap impact from early 2019. Clearly depending on the level of the cap initially, it is possible that the reduction in gross margin from the cap may happen more quickly than our cost efficiency can keep up, in which case relative to our plans we could see some EBIT margin compression particularly in 2019. However we must remember that the Government has also said that when setting a cap, Ofgem must have regard to incentivising efficiency, enabling effective competition, maintaining incentives to switch and that efficient operators are able to finance their activities. Although the Select Committee has concluded it might be hard to meet all of these conditions all at once, the intent is clear. The Committee also underscored the need to guarantee the temporary nature of this intervention.

Recognising that the formula for any potential cap is not yet known, given the steps we are already taking, our competitive position and efficiency potential, we believe that we can deliver a sustainable energy supply business in the UK with healthy returns under most conceivable scenarios.

Staying with the UK I have included once again this breakdown of British Gas dual fuel bills with the data for 2017 added. You can see that other than wholesale energy costs which on average fell in 2017, the largest elements of the bill are those of delivery to your home and environmental and social policy costs. Our profit margin after tax was £59 on an average dual fuel bill, once again in the range of £42-65 which has been the case since 2009. Over the last six months wholesale prices have on average been rising as have projected policy costs. And very recently Ofgem announced a £57 increase in the average pre-payment tariff cap to a level just below our current SVT. We are monitoring such cost increases carefully.

Let me now briefly cover some of the other indicators of growth we are seeing within Centrica Consumer. In North America Home we have been growing protection plans as we learn from the UK experience and have seen 18% growth year on year. Local Heroes started from nothing in January last year and we now have 7,000 technicians signed up and we completed 25,000 jobs in 2017. As you can see from the graph, this on demand offer continues to accelerate and complement our own contract relationships through British Gas. In British Gas on a half year basis we have seen the number of accounts in in-home services grow in the second half of 2017 for the first time since 2011.

Finally, British Gas rewards sign-ups have now reached 700,000. Rewards allows us to enrich the relationship and proposition for our loyal customers in combination with our other offers and has reduced customer churn by on average 1.4 percentage points. These growing propositions demonstrate that consumers want additional services beyond commodity energy and unlike many competitors we are in a position to fulfil all of these needs at scale. This is also true in Connected Home.

You can see the momentum we have started to build. We have seen installed hubs grow by 71% during 2017 to 900,000. As of last week we were at 950,000 hubs and therefore are likely to hit our one million hub target very shortly, albeit one quarter late. We did exceed our target for 1.5 million products sold, delivering a cumulative 1.63 million by the end of 2017 and we now stand at 1.8 million as of last week. Revenue increased by 27% in 2017 with unit gross margins remaining attractive. Connected Home continues to grow in all of our geographies and our first international partnership with ENI in Italy will see its full commercial launch in April.

We forecast that 2017 was the peak year for net cash investment in Connected Home and in 2018 we are now targeting a doubling of revenue, 500,000 new customers and over one million incremental product sales. We continue to target a billion of revenue from Connected Home by 2022.

This slide shows our competitive position in Connected Home. The internet of things market has thousands of participants. As you can see in terms of smart thermostats, we now rank 4th globally and are the market leader in the UK and Western Europe. On the right, we rank 7th globally in terms of integrated multi-function eco system deployment and again are the leader in the UK and number 2 in Western Europe. We are competitively well positioned in Connected Home. Other third parties are exploring partnerships with HIVE and it materially strengthens our other core propositions.

Let me now turn to the Business Division and the area in which our performance let us down in the second half of 2017 North America Business. As we have covered, the demands of business customers are similar in all markets and this is very much the case in North America. We have a material and established business in the World's largest energy market, serving 240,000 customers in 24 US States and 8 Canadian provinces. We are the second largest retail energy supplier by market share in the United States.

The market plays to our strengths, it is large, we operate a large customer book and it requires sophisticated energy price risk management and increasingly the offer of a broader set of energy risk management and other services. The propositions of Distributed Energy and Power are increasingly important for the business energy customer in the US. However the US energy market is a volatile one with significant weather extremes and regional differences. The acquisition of Hess Energy Marketing materially strengthened our capability particularly in natural gas. Our recent track record is generally a good one, particularly a natural gas supplier and optimisation. In power supply the track record is more volatile. The issues we had in the second half of 2017 predominantly relate to the power supply book. As discussed on the call following the Trading Update in November, in addition to the accounting re-statement the weaker performance in the power supply book was initially caused by compressed unit margins due to competitive pressures and lower volumes from efficiency and distributed generation take-up.

However as Jeff covered earlier, changes in the market including backwardated capacity curves, combined with unsophisticated legacy power products, further reduced realised margins in 2017.

Visibility on the degradation of performance and forecasting quality were simultaneously impacted by a new IT system under installation which ironically is designed to give greater granularity on elements of power gross margin. Market change was occurring at the same time as we were managing significant internal changes.

In summary the methods, products and processes had served us well in the past but we failed to adapt to a changing situation which required more sophisticated products, systems and processes. Faced with this it was imperative to investigate comprehensively what went wrong and why and we have made changes to ensure we manage the book differently going forward.

Our response which Jeff also described is designed to reduce the volatility of the North America Business Power book, increase transparency and visibility of cost component risk and improve planning and forecasting. We are also making some changes to personnel to improve capability.

North America Business is an important part of the Group. Over 2015 and 2016, post tax ROACE was 10% but in 2017 was a third of that. Adjusting for the accounting error it would have been 6%. The recent volatility and results is a concern, but returns have been generally attractive and the business has the potential to grow. The customer base and the capability we have give us the ability to offer new propositions and services which will add gross margin and stickiness to customer relationships. And we have the potential to grow the customer base.

North America Business therefore fits within Centrica's strategic framework and has the potential to deliver attractive returns and growth, but we need to demonstrate that more consistently in the period to 2020.

Moving now to our growth node of Distributed Energy and Power. We have built good momentum in this business. Active customer sites increased by 22% over 2017. Gross revenue increased by 6% and by 34% on an underlying basis when reflecting disposals and discontinued activities. We also saw a 26% increase in order book revenue with accelerated growth over the fourth quarter. We have also put in place enablers for future growth. We have enhanced our demand response optimisation capability with the acquisition of REstore which complements the energy insights and energy solutions capability acquired through Panoramic Power and ENER-G Cogen acquisitions.

We have transformed the way we go to market, including increased sales capacity, development of new propositions and bringing our products together under one brand, Centrica Business Solutions. These enablers will drive an acceleration in the growth rate. In 2018 we are targeting revenue growth of at least 50% and like in Connected Home we remain on track to achieve our 2022 target of £1 billion of revenue.

Before I return to the Group as a whole let me tough on exploration and production. The E&P Division now consists of two business units, Spirit Energy and Centrica Storage. The formation of Spirit Energy has created a stronger and more sustainable E&P business bringing together two likeminded shareholders. Our goal is to further develop Spirit, through additional consolidation or partnership. We would expect to have a lower ownership percentage in any larger entity while maintaining exposure to E&P and we would wish to retain sufficient influence to shape the strategic direction of the business. We would also be prepared to reduce our shareholding in Spirit Energy to below 50% if the right opportunity came along.

Ultimately the formation of the new business has created optionality for both shareholders and as we said at the time of the announcement, we also do not rule out the possibility of an IPO in the medium term.

Centrica Storage is now also an E&P business. We will look to create synergies between Centrica Storage and Spirit while continuing to explore the commercial optionality of the Easington Terminal.

Touching briefly now on securing the capabilities we will need for 2020 and beyond in a changing world for energy and services. The environment is fast moving with an increasing focus on integrating new technology. We have built enhanced capabilities over the past 3 years both organically and through bolt on acquisition with improved customer service, customer segmentation, propositions, digital platforms and technology. The technologies we focused on are directed at specific customer needs. In bolt-on acquisitions we have targeted top quality competitive capabilities and the initial results are very encouraging.

We have also accessed key new talent both through acquisitions and through attracting new skills and capabilities organically. We have a strong focus on bringing forward the next generation of leaders and are working hard on succession planning.

Before moving onto our financial framework and outlook for 2018 to 2020, let me cover how we are thinking about acquisitions and disposals over the period. In the last three months of 2017 the risk envelope for Centrica changed and as a result we will not be pursuing any major growth M&A. This is because of the uncertainty over the UK price cap and our desire to maintain our hard fought balance sheet strength. We may however make small bolt-on acquisitions to build our customer facing capability within the capital reinvestment limits of our financial framework. For example, a priority would be to build out our capability in Distributed Energy and Power in the United States. Spirit Energy is likely to see a second step transaction as I mentioned a minute ago.

Finally a word on our Nuclear shareholding. Subject to ensuring alignment with our partner and being very mindful of UK Government sensitivities in this area, we would hope to divest of our shareholding in UK Nuclear Power by the end of 2020.

Having highlighted many of the developments in our businesses and hopefully answered some key questions, let me summarise the conclusions on strategy before I move to future financial guidance.

We have completed Phase I of repositioning the Company. Centrica is returning to our strengths of energy supply and services. We have strong positions in those core areas. However that core is also moving as customers demand different things and our capabilities and propositions are moving with it. In the near term the uncertainty around the Company has increased largely because of UK political and regulatory interventions and we face challenges of increasing competitive intensity. As a result of this and as we mitigate the performance issues in North America, our focus remains on performance delivery and financial discipline. We will focus on customer led gross margin growth and there are some encouraging signs from our new propositions. We will drive efficiency hard and we have significantly increased our cost efficiency target to 2020 and we will maintain capital discipline and a strong balance sheet and we will not pursue major growth M&A.

So let me now turn to the Group financial framework and provide some financial guidance going forward. Our financial framework has been updated to show a revised Capex target for 2018 to 2020 reflecting continuing capital discipline. We are delivering on many aspects of our framework although we have yet to demonstrate consistent growth in adjusted operating cash flow. As a result we have yet to restart a progressive dividend. However we have delivered on our cost and capital discipline and ROACE is currently running well above threshold levels.

Our financial framework remains valid over the medium term. However today we are also providing over the 2018 to 2020 period. We will be targeting on average £2.1 to 2.3 billion per annum of adjusted operating cash flow from 2018 to 2020. While we believe this is probably also deliverable in each discrete year taking into account the unknown formulation of a potential price cap, there remains a slight risk to being outside this range in 2019. Capital expenditure including the consolidated total for Spirit Energy and any bolt-on acquisitions will be limited to £1.2 billion per annum and we would expect the outcome to be in the £1 - £1.2 billion range in any year.

In terms of the dividend, we expect to maintain the current dividend level out to 2020 subject to two conditions. Firstly, being able to generate adjusted operated cash flow on average within the targeted range. And secondly to manage net debt to within the range of £2.25 to 3.25 billion. A range designed to take into account a number of scenarios, commodity price projects and consistent with maintaining our strong investment grade credit ratings.

We believe we can manage within both these constraints under most scenarios based upon our current projections, but clearly there are always risks associated with extreme commodity price movements and extreme regulatory interventions.

Finally in line with the Group financial framework we would intend to restore a progressive dividend when in addition to the criteria already mentioned, underlying cash flow growth capability is demonstrated. Our medium term plans continue to show underlying AOCF growth rates of 3-5%.

Let me now bring this all together, expressed as sources and uses of cash. This chart shows sources and uses of cash flow for 2015 to 2017 and what we currently expect the picture to look like from 2018 to 2020 on average. Future projections are based on commodity price curves which were prevailing at the beginning of 2018. We are targeting on average £2.1 – 2.3 billion per annum of adjusted operating cash flow and £1-1.2 billion per annum of Capex. With our dividend obligations, interest payments and other commitments including pension payments, we would expect sources and uses of cash flow to be broadly balanced. And certainly to allow the Group to remain within the target net debt range. This is obviously before any disposal proceeds. We therefore remain confident in the sustainability of the Group in the current environment and despite the uncertainties we face.

Let me now cover specific targets for 2018. Adjusted operating cash flow is targeted to be £2.1 to 2.3 billion. Capex is targeted to be below £1.1 billion including Spirit Energy capex of about £500 million. In line with the earlier guidance the 2018 full year dividend is expected to be flat at 12 pence per share. We will target delivery of £200 million of efficiencies as we progress towards a total of £1.25 billion per annum by 2020.

As part of this, like for like headcount is targeted to reduce by 1,000. We expect net debt will remain within an in-year target range of £2.5 to 3 billion. All of these targets assume normal weather patterns, current forward commodity price curves and the absence of major operational outages.

So now let me summarise. 2017 was an extremely challenging year for Centrica. Both in terms of our own performance delivery in Business energy supply in the second half of the year but also given the levels of political and regulatory uncertainty and intervention in the UK. Despite these pressures we delivered on our 2017 targets. However the shareholder experience was extremely disappointing. We are absolutely committed to restore shareholder value and to demonstrate how the strategy will deliver this over the medium term.

I hope today we have succeeded in addressing the important questions raised by 2017. Centrica has a clear strategy as we reposition the company back towards the core of energy supply and services. Phase I of the repositioning of the Company has been completed with many important milestones met. The next phase to 2020 is all about performance, delivery, and financial discipline as we marry customer led gross margin growth with continuing to drive material levels of cost efficiency while maintaining capital discipline and a strong balance sheet. It is this combination and our track record of efficiency and financial discipline to date which gives us confidence to deal with the uncertainties posed by any default tariff cap in the UK and to indicate a stable dividend outlook within defined boundary conditions.

It is undeniable that at this moment Centrica faces a higher level of external uncertainty. It is therefore imperative that we focus on the things that we can control to underpin our performance and that is what we are doing. This is how we will rebuild shareholder value and confidence and I am determined to demonstrate this through our actions one step at a time.

Thank you. Mark Hodges and Mark Hanafin will now join Jeff and me on the stage and we look forward to taking your questions. As ever our Chairman Rick Haythornthwaite is also in the audience should you have any questions for the Board, thank you.

Questions and Answers

Q1. Sam Arie, UBS
Thank you very much it is Sam Arie from UBS. I have two questions. I also want to thank you for the Presentation I think it was extremely helpful this morning. I particularly appreciate the extra detail I think you gave us on British Gas and on the tariff cap situation. And that is actually where my first question is on the British Gas business. You mentioned that the average EBIT margin is just under £40 per account. But you also said you are succeeding in moving the customer base away from default tariffs. Can you tell us what the average margin per account is when you exclude default tariff customers because I think that would be a helpful indicator of where the business might be post tariff cap? Hopefully that one is an easy one.

The second question is more about overall results where you landed for 2017 and what we should expect for 2018. My read is that you have landed absolutely bang on consensus for 2017 but with EBIT a little bit lower than expected, but some positives that you mentioned in the tax line. Can you just talk to us about how that rolls forward to 2018 and how much if you like of the EBIT negatives are one-off and don't recur next year? And then what sort of tax rate we should expect for next year? I think the consensus at the minute implies a step up of about 10% from 2017-2018 so we are just trying to check if that is still fair? Thank you.

Answer: Iain Conn
Sam thank you for that. I think Mark Hodges should answer the first one and Jeff the second. Makes my life easier!

Answer: Mark Hodges, Chief Executive, Centrica Consumer
Thanks. Morning Sam. It doesn't matter how much we disclose there is always more. In terms of, when you say default tariff inside British Gas, we don't typically disclose the gross margin or the EBIT profit, it is obviously a highly sensitive number. The thing I can tell you is that Iain mentioned we had moved 700,000 customers from SVT to fixed products. What we are seeing is that we can move people onto our fixed products at margins that are very, very similar to our SVT book. So we are not seeing a big degradation as we move those customers. And if you remember back to last year when we contacted all of our SVT customers, we had something like half a million move. This year 700,000. Iain has pointed to 1.3 million customers we would like to move during 2018. So we are seeing, we are working with our customers to make that change happen. We are not seeing a big degradation in margin, but obviously overall competitiveness will end up determining the overall level of profitability from the book.

And the other thing is that £39 just to remind you also includes the services margin, that wasn't just residential energy, that is also residential services and that is a book as we pointed to in H2 of 2017 that we finally started to see some growth and of course the ambition is to continue that growth trajectory now as we go into 2018.

Iain Conn
Jeff the EBIT and tax?

Answer: Jeff Bell
Yes, let me take both of those. In terms of 2017 and the EBIT, Sam you are right, there were a handful of things that we saw post the Trading Update in December that affected the full year profitability. Virtually all of those were one-off or we wouldn't expect to repeat so they included the fact that our Sizewell Nuclear station had to come off generation in early December. It is now back on stream. We saw in the E&P business the Forties pipeline issues

which backed in some of our production. That issue has now been resolved. And we had some extreme weather in the last week to ten days in North America which made, in particular the NAB business slightly worse than what we were projecting. But we would expect all of those to normalise out.

I think the second part of your question was round the effective tax rate. I would probably think about it going forward in the following way. We disclosed the effective tax rate for 2017 at 22%. But in the Preliminary Announcement we flagged a number of items that were in 2017 that are less recurring in nature. Things like the US tax rate change as well as the level of PRT credits and provision releases although we tend to have some of that in a year, not to the level we would expect in 2017 every year.

The other kind of boundary we then had within there was we said if you stripped all of that out, although we expect not necessarily all of it you know would come out year by year. You would end up with an upper range of around 40% of an effective tax rate. Wouldn't expect the effective tax rate to be that high, but I think we would with the Business mix that we will see in 2018 more profitability from the E&P segment both with the combined Spirit Energy as well as with more production from Storage. We would see a higher tax rate just on business mix alone and therefore it will be more towards that higher range than the 22%.

Q2. Fraser McLaren, Bank of America Merrill Lynch

Good morning, McLaren from Merrill's. A couple of questions on the new efficiency savings please and then one on supply costs. So first of all you suggested that the Change Programmes in North America meant that management's eye was off the ball. As you embark on another substantial efficiency programme across the Group what makes you confident you will be able to avoid problems as you remove another 4,000 jobs?

Next just to check if the £20 per account number is after inflationary pressures and would therefore be around £120 million net in UK supply? And are you therefore saying that your base case is no EBIT margin erosion as a result of the cap by the time we get to 2020 versus today?

And then the last question is about upward pressure on external energy supply costs. You have delivered respectable supply margins despite having the lowest prices in the market. To what extent is this helped by favourable hedges? When will they roll off? And to what extent would higher input costs impact on margins this year without a tariff rise?

Answer: Iain Conn

Well quite a lot in there Fraser. So let me touch on a couple of them and then I will ask Mark Hodges to talk to the £20 per account and the hedging impact inside the margin.

So first of all the new efficiency programme generally. As with any efficiency programme we have got to be extremely careful. One of the challenges for Centrica as we go through this 6 year repositioning of the company, is clearly change. And you are right that change both market change and internal change collided in the North America Business Unit last year. But I do want to emphasise that about three-quarters of the impact was to do with the accounting issue and market changes. So it was not like all of it was down to our own change issues. But it was a factor. So answering your question. Look over the last three years in general we have managed to drive efficiency while strengthening the system of internal control, improving compliance, improving safety and very importantly improving customer service. We have seen complaints, if I take UK Home Energy as an example, improved between 20-30% on average each year. We have ended up I think 50% down on end 2014 levels, up rather!, down on complaints but better. But this does show that in general we are able to walk and chew gum if you like. Are you highlighting a risk around change? Absolutely you are and our focus is going to be on managing change really carefully. Mark Hodges has a significant

Change Team inside the UK and that is where a lot of the change will occur and I am confident that we can manage it. But is there always risk? There is always risk associated with change.

The second bit I would like to answer just on this, are you saying your base case is no erosion to EBIT margins associated with an unknown tariff cap? Well of course we are having to make some assumptions. I indicated in my remarks that we have incorporated an impact of a tariff cap and that would imply we do see some EBIT margin impact from a tariff cap and I especially highlighted the issue of while we are driving costs down, if they get out of sync with the gross margin impact of the tariff cap. And again we don't know what the formula is. Then of course we would see an impression on our EBIT margins until our cost efficiency programme caught up. So we can't give you and we are not prepared to give you a forecast for what the impact is going to be, but hope that some of the indications around our exposure to it, our competitive position and what we are doing on costs actually improves our relative resilience significantly.

And the other final point I would make, why is relative resilience important? Because the Government and the Regulator are going to have to consider the impact on the market as a whole not just on British Gas. And we are significantly competitively advantaged relative to the average. And some other companies that are actually loss making are going to be impacted by the cap as well. And I don't know yet but my assertion is that must be a factor along with all those other things that Ofgem have somehow got to balance.

Now Mark on the cost per account element of all that and energy supply costs and hedging?

Answer: Mark Hodges
Cost per account on Iain's slide contributes to the £500 million and that is pre-inflation so there will be an inflationary impact on that £20 over the three years.

And on the whole hedging strategy, obviously we don't know yet the mechanics of the cap, we don't know how it will operate. Not just what level it will be set at, but how often will it be reviewed. We are looking as I have already said to shift more and more of our customers onto fixed term deals. That is something we are used to, in the way that we hedge. I think part of the question was, is there some kind of big event where a whole bunch of hedges roll off. That is not a risk particularly. We are thoughtful about the commodity that we are buying into a price cap scenario and where we think the customer numbers will be by product. So we have been working very hard on that. So I don't see a big event from a hedge perspective in the UK Energy Supply book.

And I just would go back and stress, I know Iain mentioned it on the change. I mean it is something I am very, very conscious of is the amount of change we are going through in the Business. But just to go back to that complaint statistics. That is a million complaints less over the last three years in UK Home Energy whilst going through cost reductions, whilst going through the headcount reductions, whilst improving service more broadly. So you now we are starting we believe to build a track record of being able to balance the risk with the execution and make sure the customer really does see the benefit.

Q3. Mark Freshney, Credit Suisse
Hi, it's Mark Freshney from Credit Suisse. Two questions. Firstly on the British Energy stake. I believe there are a number of restrictions on who the potential buyer could be and in terms of their competency. Can you talk about the stages that you would need to go through to assess and how likely it is that you could divest that? And also what you would potentially do with the proceeds because the amount of net debt that you are running is actually fairly low relative to the underlying cash flows for the business.

My second question is on Hive. So you increased the number of products sold during the year I think by 70%. But the revenues only went up by 30%. So can you talk about what that disconnect is there please? Thank you.

Answer: Iain Conn
Great questions, thank you very much, particularly the last one which I will give to Mark Hodges to answer. Seriously, firstly on Nuclear I am going to ask Mark Hanafin in just a second to talk about the set up if you like and some of the sensitivities. Just on the proceeds point, obviously let's get there first. But we have to recognise as you say first of all that the balance sheet is quite strong. And I hope I have indicated and happy to work that with you a bit more that the sources and uses of cash ought to be reasonably balanced over this period. But we do have a number of other things that we have to take into account. We are going to have to spend the money on the debt repurchase programme. We have got to spend money on the cost to achieve. We have got other obligations like our pensioners that we have got to think about as well as wondering about reasonable ranges of commodity prices. So that is in brief why we have got that slightly expanded net debt range, but you are right, the net debt to EBITDA ratio of this Company is now in pretty good shape.

So while the balance sheet might be a customer for some of the cash we have got to think about, if we ever get any which is the bit Mark will answer, we have got to marry up all the different possible beneficiaries of cash. Obviously I have mentioned the balance sheet. We have also got to think about our pension obligations and then of course we have got to think about the growth of the business and we have got to think about our shareholders. What I can undertake is that if we sell the business we will look at appropriately balancing all of those things.

But Mark on the complexities of this?

Answer: Mark Hanafin, Centrica Business Chief Executive
Yes, obviously the identity of the buyer is a very critical consideration in any sale, but the sensitivity is not really about competence. You know EDF is the Nuclear licence holder, they are the competent authority. They run these assets. So a new buyer we are not restricted in that sense in terms of Nuclear competence. The issue is more around the acceptability of a new buyer to our partners and also to the Government.

Iain Conn
Thank you Mark and now Mark Hodges on Hive product sales and revenue growth?

Answer : Mark Hodges
Yes so as you said Mark, 71% increase in install base, 27% increase in revenue year on year. I think four reasons for the disconnect. We are changing the channel mix so as we moved into 2017 versus 2016 more through our retail channels, less through something like the British Gas channel which is a positive. So we are now, we actually have 46 retail arrangements in the UK. We are in something like 1,700 stores across the country. So the channel mix has an impact. The US entry so we entered the US working through Direct Energy. We are an unknown brand and an unknown quantity so we have kind of primed the pump in the US in 2017 for further growth in 2018. That had an impact. And then I would say there is a kind of product mix aspect as we move forward. We are seeing people entering the Connected Home space, some of them in lower value overall products. So a Hub with some lights or some plugs as opposed to the thermostat as the first purchase. What that puts us in the position to need to do next is to obviously cross sell and up sell to the existing base. I think you know to date a lot of the focus has been rightly on growing the total numbers. That will continue, but as the held base gets bigger we need to get much better at our CRM, at cross sell and up sell to the existing customer base and that will start to help improve that revenue percentage growth in relation to the overall product and Hub growth.

Iain Conn
You can do the math for yourself. Our growth rate needs to be pretty high between now and 2022 to hit a billion pounds, but actually it is approaching the rates already that in terms of sales growth and we would expect obviously revenue growth to catch up with sales growth eventually.

Q4. Iain Turner, Exane BNP Paribas
It's Iain Turner from Exane. You have announced the sale today or the intention to get out of British Energy. You have pulled back capex. You are issuing further M&A potentially. Is this now a company that is sort of runoff in terms of its strategic ambition?

Answer: Iain Conn
I don't think so at all. As we moved from a company that is, has been very asset heavy and capex heavy to a company that is more oriented around the customer, the capital reinvestment intensity should go down and indeed is going down. But actually we are also deploying significantly more and we believe the right levels of resource in order to grow the company at an appropriate rate. Also we had to build a lot of capability in new propositions and business models require capacity and capability in order to start to grow the business at scale, it takes time.

And you are also right, that inferred in what you are saying that with some of the challenges we have got, including political and regulatory intervention, we have ended up with 13% cash flow growth one year and sort of negative 13% the next year. We haven't yet demonstrated that the model can grow. However from a cash flow perspective, it is not shrinking and indeed if you look at the last three years and strip out big working capital recovery programmes like in UK Business, we delivered about £2.1 to £2.3 billion of cash flow and we are indicating a consistent £2.1 to £2.3 billion cash flow in the next three years. Now a negative interpretation of that is ex-growth. A positive interpretation of that is that must require a number of sources of new cash flow to overcome some of the decline and clearly we have to demonstrate that gross margin into cash flow starts to overtake the proportion that is coming from cost efficiency.

So I don't believe in any way that this company is somehow ex-growth or not pursuing its strategy and I believe that we can demonstrate that the company's strategy will both pay for all of our obligations and be able to maintain the current dividend level obviously within the bounds that we have laid out.

On your point about the major M&A or the inference there. You are right that we signalled last year that we were looking at whether to grow through acquisition, we didn't say how large. In the current environment, given the uncertainty and given the desire to maintain a strong balance sheet, we don't, are not pursuing major M&A. But actually the more important thing is we have looked at an awful lot of possibilities and really there is nothing that attractive out there that we should be pursuing right now. Therefore we can make that commitment, but we are going to be pursuing small bolt-on acquisitions as we have been doing to build out capability. So the simple answer to your question is no I don't think it does. Deepa?

Q5. Deepa Venkateswaran, Bernstein
Thank you, Deepa Venkateswaran from Bernstein. I have three questions. Firstly with Centrica Home. Can you quantify what is the headwind from the weather impact in 2017?

And the second question is the transition of the SVT customers to fixed tariff during 2018. What do you think is the impact on the gross margin from the 4.3 going to 3 million?

And secondly would there be other additional opex costs, I don't know, more extra staffing in the call centres to contact all these customers? If you could just quantify those two.

And the third one is on upstream. Could you clarify whether the unit lifting cost you expect that to be flat at 14.9 per barrel going forward? Thank you.

Answer: Iain Conn
Let me take the lifting cost point and just say that obviously what tends to happen with costs in E&P is that costs follow price. And the E&P industry has a habit of costs following price, industry costs following price with a delay of about 18 months to two and a half years. And that track record has been borne out recently. However the main driver of our lifting costs or one of the main drivers of our lifting cost increase last year was actually the loss of production i.e. the denominator because we deliberately shut down Morecambe for a very long time in order to improve its reliability and safety performance. So the increase is exaggerated in 2017. There are some inflationary pressures coming through in the industry, but not dramatically as yet. If prices stay high I would expect inflationary pressures to continue.

On the weather impact in 2017, Jeff we don't disclose the weather impact as a separate item typically. I mean we can say across the whole company depending on the metric or whether it is pre or post tax, £100 to £200 million I think was the overall impact, is that right Jeff?

Answer: Jeff Bell
Well we try to build in one of my slides the impact of foreign exchange and weather and those factors, about £130 million. So weather is less than that and obviously some of it is in North America and some of it is in the UK. But I think as an estimate you kind of take half to two-thirds of that £100 million.

Iain Conn
Mark Hodges moving the customer book?

Answer: Mark Hodges
Moving the SVT to fixed. As I said earlier we haven't seen a significant degradation in gross margin through the moves that we'd make. Obviously at the end of the day the gross margin is partially just a function of the market price and so it is very hard for me to give a prediction because who knows where market prices will be going through the next 12 months. But our belief is that we can make that move and retain valuable relationships with our customers. And I would also say segmentation is a big part of this. We have been stressing now as you saw again today, value versus volume. There are differences between groups of customers depending on a number of different factors that we need to assess, whether that be their propensity to churn, their propensity to buy another product, their consumption, their dept profiling. You know the amount of calls we take from them. There are a lot of science going in as we explained before going into the whole segmentation model. So with competitive pricing, with the segmentation, you know hard to give a prediction but our experience to date has been there hasn't been a significant impact on gross margin.

And to answer your, I can be more definitive on the Opex. We are accounting effectively for any increases that we need to, or any increased costs that we need to bear to make those transfers happen successfully for our customers within the cost efficiency targets that we are setting overall. So I don't see a big ramp up of costs being needed. Lots of this can be done digitally. Lots of this can be done with the great people that we already have. And so any small increase will be more than offset by the efficiency targets that we set.

Q6. Martin Brough, Deutsche Bank
Thanks, Martin Brough from Deutsche Bank. A couple of questions. One, on the debt buyback could you just give us a little bit more detail as to why you think that is a sort of overall NPV benefit. You are obviously buying roughly at market value I guess, but for the bonds, is there something structurally that means you have a higher value than what you are being forced to pay in the market for the debt?

And then secondly, obviously Ofgem is looking at the idea of this reversed auction for groups of sticky customers and sort of doing a trial at the moment. Do you think that is just a non starter for customer concern reason reasons or are you factoring in that as a possibility that if it is successful and turns out to be highly competitive that Ofgem might try and roll that out? So what is your perspective on trial? Thanks.

Iain Conn
Martin thanks. So that is very easy, Jeff and then Mark.

Answer: Jeff Bell
Yes so I think on the debt repurchase I think two things are happening. Obviously spreads have moved in our favour in the sense that the premium that we would expect to pay on buying back the gross debt is less than it would have been previously and effectively we are buying back and arbitraging our sort of credit spread against that. So that over time then makes it equate valuable to us in terms of our reduction in interest costs versus what we have to pay up front in terms of that premium and therefore get a better mix of gross and debt in cash on the balance sheet.

Answer: Mark Hodges
Ofgem, yes very well aware of the trial and a number of the other ideas that Ofgem are exploring. I mean we are always concerned about data, data privacy and consumer consent to these kinds of things. It is a trial for a reason. We don't know if it will work, we are not convinced. The challenge that Ofgem believe they are trying to tackle is this concept of a disengaged customer base. From our perspective if we can start moving people from SVT which is why we are closing it to new customers and why we are engaging our whole customer base to try and move them onto an alternative product, that means we've engaged with them, that means they have made an active choice, that means they don't come under the remit of either the default tariff cap or these kinds of interventions that may or may not happen from Ofgem. So the strategy we are pursuing is the right one for a number of reasons. That is another good example of why engaging our customer base directly and moving them onto products that they are actively choosing is the right thing to do. I don't know how successful that will be. We have our doubts. As I say customer privacy and customer data privacy is very top of our mind as these kinds of things are being considered.

Q7. John Musk, RBC
Morning it's John Musk from RBC, two questions as well. Firstly on the dividend and don't want to simplify it too much, but are you saying that 2018 dividend you can be very confident of hitting your targets for the 12p but in 2019 the main variable is obviously going to be the price cap and that is where there is some uncertainty?

And then on services or the Home Services business, can you just give a bit more colour why you think the customer number started to grow again in the second half? Is that your actions or is that a change in market dynamic? And also within there you have seen a fall in the gross margin by about 10%. So other than pensions is that a change in the market again and something we should be worried about?

Answer: Iain Conn
So look on the dividend, clearly what we have said is we expect, which is quite a strong word, that subject to the cash flow generation and staying in the net debt range that we would expect the dividend to remain at the current level. Clearly our confidence is highest in the near term and there is more uncertainty further out. But I am, from my perspective, I expect that is something we are going to be able to do. We clearly need to deliver within those boundaries. So I think your assumption is a good one, but as always the final decision on dividend at each period is a matter for the Board, but that is what we are signalling.

So in terms of services Mark?

Answer: Mark Hodges
Yes I can guarantee you it has been a lot of hard work and a lot of intervention. So a number of things have happened on Services which were going on actually through the first half of last year and even the back half of 2016 to get that growth to start to happen. I have mentioned a number of times in meetings pricing sophistication, so we have been investing in the quality of our pricing capability for what effectively is an insurance product so that we can more accurately risk base price which is both helpful from a sales perspective but also from a retention perspective. We have been through a huge amount of retraining, I mean our contact centres so that our people are better equipped to sell the product. We have changed some of the product features, you know there is just an awful lot gone on. And in terms of the way we incentivise sales, that is another area we have been focusing on.

So the market dynamics at the high level are pretty much unchanged, there is a broad shift to on demand, that is why the Local Heroes capability is very important because that not only meets a customer need, it is also ultimately a potential sales channel for the full services product.

And then on margins and profitability, you did highlight the single biggest factor which is the gross margin is down. That is because the cost of our engineers is within the cost of goods, it is within the gross margin and obviously the pension costs impact that we had last year gets run through that line. There are other things that we can do. We are still working on the efficiency and services as well more broadly, productivity, but the biggest impact on margin was pensions.

Q8. Chris Laybutt, JP Morgan
Morning it's Chris Laybutt from JP Morgan. Just first of all a follow-on from Deepa's question on the transition from SVT to fixed. With those customers, if price protection is introduced at a level which is lower than your fixed tariff customers are paying, will you offer that price protection to those customers as well?

And then just quickly on E&P. Your liquid sale price rose around 7% in 2017, that is European liquids, but spot prices are up considerably more than that, 25-30%. Can you give us some sense for the shape of the hedge book going into 2018 and 2019, that would be very handy?

And just lastly on Smart meters. More of a top down question. Are you concerned at the rate of the smart meter rollout industry wide because Ofgem and BEIS do seem to be putting some emphasis on the smart meters being rolled out to contribute to getting rid of the cap in the future?

Answer: Iain Conn
On smart meters Mark Hodges will answer that. I mean clearly we have indicated as part of our 14 point plan that we think there are aspects of the smart meter rollout that the Government should review. I will leave that one to Mark.

On the liquids realisations in E&P I will leave that to Jeff.

I mean just on the SVT to fixed and Mark Hodges can add anything to this. Clearly the tariff cap is currently directed at default tariffs. Why is it directed at default tariffs? Because there is a sense that if you defaulted you are not engaged. So right now the cap is not applicable to non default prices, it is not applicable to non default energy components in bundled offerings and we therefore believe we have freedom to offer energy as a component in a bundle or other formulations other than on a default basis at different prices to the cap. But until we understand the specific formulation of a cap and the calculation and how long it is going to last, currently the legislation being proposed is until 2020 with a possible extension to 2023. It is difficult to understand where all the different offerings are going to be relative to that. But we are very conscious of it and I will leave Mark to add any comments.

So why don't we start with Mark, add any comments to that, smart meter rollout issues and then we will come back to Jeff on E&P.

Answer: Mark Hodges
Yes not much to add. I mean we obviously want to try from our prospective to minimise the number of people who end up on the default tariff, that is one of the things we have said in our commitments by making sure that at the end of any tariff agreement we have they get lots of choice of other attractive offers. So we will try and minimise the customer numbers. To answer your question bluntly I don't think we can give a guarantee about where other fixed deals will be priced going forward. It will depend on the nature of the product. Is it bundled? Does it come with rewards and the benefits that the rewards programme brings? So it is not just a very straightforward comparison.

On smart meters, just to reiterate again, we are supportive of the whole smart meter rollout. We think it is good for consumers. We actually think that, we have continued to do our research. We see a reduction in consumption amongst the customers who have smart meters, it is about 3.5% compared to the average. So it is saving real money and hassle. We do have concerns, hence the point that Iain mentioned about the 7 point plan. The biggest challenge to the whole programme as I see it ultimately is customer demand. This is an opt in scheme, we can't force people to take a smart meter. We can resolve eventually the technology issues, it is frustrating that the DCC has gone back again to October, but we continue to play a very active role in trying to make sure that that works and that happens. I believe that it will work, I believe that interoperability of SMETS1 meters will happen. So for me the biggest challenge that we all need to face into is ultimately customer demand and what do we do with groups of customers who just may not want to have a smart meter? I don't think there is an easy answer and to that of course and the challenge becomes as well over time. It becomes expensive to keep chasing the same people so we all have to bear in mind as well that there is a kind of marginal benefit from chasing the last groups of customers. So I think that is where the debate needs to be had.

Answer: Jeff Bell
Prices, we have talked previously, in our asset businesses, E&P, Rough now or indeed Power Generation, we typically follow broadly a two year rateable hedging strategy for the majority of the volumes we produce or generate. So you could use that as a rough rule of thumb. Obviously with that type of strategy the much lower prices that we saw 18 months or so ago are starting to come out of those hedges and are at currently anyway at higher prices. Probably only the Rough volumes don't quite follow that because having just switched to a producing asset, it is more open to the current forward curve than the other assets.

Q9. Dominic Nash, Macquarie Securities
Hi, yes it is Dominic Nash from Macquarie so a couple of very quick questions then on your cash placed numbers. Your £2.1 to £2.3 billion out to 2020. First of all presentationally how does the adoption of Spirit effect your consolidation of their cash flows into those numbers? Are you going to be proportionately consolidating that or will that be 100%? And does that mean the underlying number is actually lower than those headlights?

And secondly, it is pretty clear to me that the dividend policy is now extremely linked to cash and does that mean that if the cash and earnings diverge in any way, the number that is more important for us, for investors to look at your potential dividend, is your cash flow cover rather than your earnings cover going forward?

Answer: Iain Conn
Let me answer those if I may Jeff. I think first of all the £2.1 and £2.3 billion does include Spirit 100% on a consolidated basis, but I wouldn't think about Spirit as somehow not being underlying. I mean it is part of the Group's cash flows. And if you do the math around the cash flows and if you take £2.2 billion as a mid point, and £1.1 billion as a midpoint of the capital spend, obviously what is left. You know with the dividend spend and interest payments on a slightly reduced basis and there are pension obligations. You can see that the organic cash flow should just more than balance in that scenario. And just briefly the flex around the capital and cash flow depending on the exact scenario in each year recognising we have got working capital movements from time to time that affect it, adjusted operating cash flow. I mean that is the reason for the slightly expanded net debt range.

On your last point, our dividend policy has always been explicitly linked to cash flow from 2015. We laid that out very explicitly and we have laid that out again today very explicitly So I think you can conclude from that that the primary driver of our dividend policy is our ability to pay for the dividends. Obviously broadly speaking earnings and cash flow should follow each other, they both derive from EBITDA on different bases, but it is all about cash flow. Because you can buy things with cash flow.

Follow up question: Dominic Nash
To follow up from that then, if your earnings fell below 12 pence but your cash flow was fine then you would be comfortable paying a 12 pence dividend?

Answer: Iain Conn
No. I mean my answer to that is companies do have periods of negative dividend cover from earnings and still consistently pay. We have given no conditionality around the dividend to do with earnings over the next three years. It is to do with operating cash flow and obviously the net debt range. However we are not signalling either that we are expecting to go into negative territory on dividend cover from earnings. But it is not part of our financial framework.

Q10. Elchin Mammadov, Bloomberg Intelligence
The dollar fell about 10% in the past year, could you please give us a bit of sensitivity in terms of your earnings to dollar changes going forward? Because you have talked a lot about commodity prices but maybe not so much about effects.

And the second question is about slide 50 where you talk about your market position in terms of Hive versus the other market players. We see that Nest is up there near the top. Are you comfortable being like 4th or 5th player in the market and are you expecting to bridge the gap going forward as you roll in new markets? Thank you.

Iain Conn
Foreign exchange Jeff and then Mark on our competitive position in Connected Home.

Answer: Jeff Bell
Yes I think a couple of ways to look at foreign exchange. Obviously the impact is most easily seen in the financial statements around the North American operations if it is against the dollar and you can fairly easily do that with reported operating profit by and large. And to a much lesser extent the Irish business. I think the piece that is harder to frankly estimate at any particular point in time because it is involved with E&P cost base is that particularly in Norway, a lot of the costs are effectively in underlying US dollars. So we do get this play of an impact on the cost base which, even if the pound is weakening, is helping us from a revenue perspective, but is then offset from an underlying cost perspective. So that impact is much more muted, but can at times have an impact on our result but much harder to estimate.

Iain Conn
Mark are we going to beat Nest?

Answer: Mark Hodges
We already are in the UK. Look I think Nest obviously have a very, very strong position in the US, our stronghold is the UK. That gives us I think a really great platform into the rest of Europe, hence the ENI deal. I think from our perspective really interesting, we have another very large energy supplier who wants to be in the Connected Home space, who does not want to start from scratch, who has a field force, who can do the read across to what we have done and think that we are a great partner because we understand their business and we can help them.

So I think across Europe we have an amazingly strong position given the start point. In the US we have great technology, we have the DE brand to leverage, but it is harder because it is a more competed market and so we are having to think very carefully about how we go to market, what channels we will sell through. How much money we will invest in marketing. We are talking to a number of really important players. We have a great relationship with Amazon here in the UK for example, that is a relationship I would love to expand in the US. So there are ways for us to take Nest on in their home market, but I think the way I would think about it is the US and Europe, we could definitely leverage all the experience in the UK more easily in Europe. In the US we are going to have to really prove ourselves from scratch.

Answer: Iain Conn
I think there is room for us and Nest and in the World. The penetration at the moment is still reasonably low. There are an awful lot of people out there who want energy in these types of services and last time I looked, Alphabet didn't offer energy and so I think we can find our own way competitively.

Q11. Nick Ashworth, Morgan Stanley
Hi thanks, it's Nick Ashworth at Morgan Stanley. Firstly just quickly on EM&T. You talked about the legacy contracts rolling off. You showed a slide on 19 which looks at the core EM&T and then the legacy. Is the core EM&T a good place for us to be thinking about over the next few years and how does the one final legacy contract evolve from here and what needs to change to turn that from negative to positive and how much of a drag is that?

And then secondly, just going back to the 14 point document that you put to the Government in November, what has their response been? Have you committed at all to moving away from the standard variable tariff by a certain date? And I guess given the run rate moving from standard variable to another type of default tariff it sounds like you could even get to zero standard variable tariffs by 2020. Is there some sort of internal point that you are looking towards?

Answer: Iain Conn
Look on that last one I will ask Mark Hanafin to talk to EM&T. We've had very continuous conversations with the Government about their plans. And I am regularly in touch with the Secretary of State and his department. We indicated that our 14 point plan was going to be deep and comprehensive and they were impressed by those factors. Now some of the things we are proposing they do aren't easy. Politically aren't easy. But I know that the Treasury are intrigued by the revenue neutral nature of moving policy costs out of bills into taxation. The problem is it is a political issue. It is called de-risk, stirring up the hornet's nest with rates of income tax and so on. But we have got the Government's attention on this. On the nub of the issue you are highlighting, the Government recognise that we in some ways want the same outcome. We want to get people off standard tariffs, we are disagreeing on how. And that has been an open dialogue between me and the Secretary of State and we just disagree on how.

You are right also that it might be that we find that our exposure to standard variable tariffs makes the impact of a price cap on default tariffs much lower than people expected, but let's wait and see.

And on your timing question, we are going to withdraw the standard tariff for new customers by 31st March. We can't forcibly remove everyone from standard tariffs. We did ask the Government to consider and the Regulator to consider doing that market wide, but they have passed on the issue. We tend to find that Governments don't act when the politics of the situation is difficult.

Mark Hanafin, EM&T?

Answer: Mark Hanafin
So on the core EM&T business we do see continued growth in that business. We have a very good capability there so we see growth around route to market origination, LNG and Gas and Power Trading. The legacy contracts there are three of them left and they have been profitable in recent years. We have got two profitable ones rolling off next year, this year sorry. And then we are left for a number of years with a loss making contract. These go back a number of decades they go back in fact to a time where there were no gas indices to price off. And therefore the loss position on that remaining contract really depends on that basket of indices which are some quite strange energy indices in there versus the gas price that we can sell it. To give you an indication of it, Jeff referred to some guidance around operating profit being about half this year versus last year in EM&T. I would say that most of that delta is related to that loss making contract.

Iain Conn
Thank you. So we have got Fraser very briefly and Gus, and then I am going to wrap it up. I think we have been going for a while.

Q12. Fraser McLaren, Bank of America Merrill Lynch
Thank you, McLaren from Merrill's again. Just a very quick one. You have spoken in the past about how the LNG contract that starts next year might be loss making in the early years. With the recent rise in Asian LNG spreads, have you changed your view?

Answer: Mark Hanafin
Yes look let me give you a quick overview on it. It is 91 million MMBTUs a year that we lift. There is a fixed liquefaction fee of three dollars. We can load it on our ships and we can take it anywhere in the world. So we are exposed to that spread. If you look at the 2020 prices coming on in Q4 of 2019. So let's take 2020 as the first year. And you look at recent forward prices for 2020 and you assume the backstop of the UK so just MBP versus Henry Hub. It would be contributing about a dollar 40 to that liquefaction cost or if you like a loss of a dollar

60 just in terms of a simple movement of a cargo from North America to the UK. However since we signed the contract a number of years ago we have been building up our LNG capability. We have been out there, despite difficult market conditions selling marketing. And about half of the volume in terms of price exposure is mitigated by that marketing effort already. So that gives you an overview.

Now in terms of how we see supply demand, I still think we are seeing an oversupply in those early couple of years. But it is interesting that we haven't seen that oversupply that was expected this winter. Hardly any cargoes came to Europe and some commentators, notably Shell are pointing to that and saying look it is quite difficult to predict what demand is and maybe that glut isn't there. We are still assuming it is but others are being more positive in terms of their outlook on supply and demand.

Q13. Gus Hochschild - BEIS
Just if I may circle back to Iain's question about asset shedding. I am mindful of the block of sale of CCGTs earlier this year, well last year rather including Langage. So is this a signal that within the strategy that you might contemplate getting out of Central Power Generation altogether?

Answer: Iain Conn
Well we signalled that to some degree in 2015 that we saw the rent moving to distributed systems and we are therefore investing in batteries, rapid response engines, peaking as well as installations in customer's premises and this is, I think this is a trend that has been proven even more intensely than when we announced it in 2015.

The second thing is I think it has also been proven that the rent isn't looking like it is heading back towards large central power generation and you only have to look at some of the subsidies that it requires in order to keep capacity going. So as a general sense, we will be heading away from central generation. And we will only have, if we sell Nuclear, the White Gate Power Station in Ireland. But we will be replacing that portfolio to some degree with more distributed assets.

Closing Remarks
Iain Conn

Thank you, well ladies and gentlemen this has been a long session, but I think it is very important that we covered everything that you felt you needed to hear. Just a few points in closing.

The first thing is that our performance was weak last year but I hope that to a degree you can now look through that with some confidence. The second thing is the largest impact on our shareholder experience last year was actually not our performance, although it was probably the last straw, but it was actually this uncertainty around politics and regulatory intervention in the UK in our largest market.

I hope we have given you some sense of how we are thinking about it and how we are going to deal with it.

The third thing to say is that we have got a clear strategy and all the elements of it are interrelated and the one thing that I hope we have also demonstrated is that customers actually want the components of the strategy together. Many customers do and it is not as though we have got some satellite activities that aren't related to our core business. This is all about reinforcing and strengthening the core of energy supply and services.

Fourthly, given that there is a lot going on that we can't control, our focus is on what we can control and it is on performance delivery and financial discipline and that is something we have demonstrated over the last three years.

And finally, what gives me confidence about Centrica going forward. The first thing are the people in this Company and the capability that we have got. The second are the assets and market positions that we start with from this point. And the third is the strength of our cash flows and the fourth is the strength of our balance sheet.

And so, if you like the starting point and the covenant that we can offer is a strong one and we hope that we can demonstrate our performance through our actions and we look forward to updating you with the Trading Update and then at the middle of the year. Thank you very much.

End