Centrica Preliminary Results

Presentation Transcript – 23 February 2012

Sir Roger Carr - Chairman

Good morning ladies and gentlemen. Welcome. For Centrica 2011 was a mixture of unprecedented world events that produced material business challenges all requiring great management skill to deliver a strong set of numbers. In the wake of Fukushima, escalating wholesale gas prices, political uncertainty at home and abroad and mounting consumer hostility to all energy companies, I am pleased to say that Sam and the team did an effective job in delivering the goods.

In a few minutes as usual, Nick will provide details of the financial performance and he will then hand over to Sam who will provide greater colour on the strategy and operational performance. But before handing over, I wanted to confirm our commitment to three key business principles, however turbulent the outside world.

First, our business model has consumers at its heart. Our commitment to service and competitive pricing both here and North America is central to our thinking. Our objective is to make a fair profit by delivering strong customer satisfaction. We use our profits to invest in the security of supply and to reward our shareholders. To achieve these goals Sam and team have acted promptly and professionally to reduce costs and our employees have acted in their own way positively and responsively in their willingness to be flexible in rostering pension terms and remuneration. We have been able to make substantial investments, reduce our electricity prices to consumers and reward shareholders with an 8% dividend increase. All of this has been achieved without overstretching our balance sheet, dislocating the business, disturbing our employee relationships or diluting our commitment to apprenticeship training and executive development, which is a tribute to management and a reflection of Centrica values.

Secondly, we are a vertically integrated customer facing business underpinned by carefully judged investments in upstream power and gas assets which in their own right must deliver value and growth. The Board has also given its support to a number of major contracts during the year, including the LNG with Qatar, the contract with Statoil and a series of smaller but equally important investments made to secure long term supplies, deepen our reserves and enhance our earnings. Our balance sheet is strong and the retention of our rating is key to our counterparty relationships. We have strong cashflows from new investments and the financing of our standing 2011 acquisitions.

Looking to the future, I would emphasise that the application of our funds to all our investments, including wind and new nuclear will be made only if the economics are sound and the returns attractive and secure. Shareholder value is our priority when making these investment decisions.

Finally, we are an international business and our geographic balance is proving to be effective. We are now a significant player in the Norwegian North Sea and our upstream business also has a presence in Trinidad and in the Netherlands. In North America, disciplined investment replicating our proven business model in unregulated markets with customer and service led expansion is serving us well. Growth has been strong in 2011 and prospects for 2012 are encouraging. We have witnessed however sudden changes in UK government tax policy that disrupted the certainty on which investments may be planned. We are a major contributor to the UK paying some £800 million in tax, £700 million in dividend and providing employment for over 30,000 people in this country. It is hoped that our representations to government on the need for fairness and certainty have been heard. In an uncertain world however, whilst our commitment to the UK remains strong, having alternative opportunities for investment has proved to be wise.

Looking forward, 2012 will continue to be challenging, but I remain confident that the top management team we have, supported by the increasing bench strength of talent that they are developing, will be successful in building the business in the year ahead.

I will now hand over to Nick.

Nick Luff - Group Finance Director

Thank you Roger, good morning everybody. As usual I will start with some commodity price context before going into the results. And 2011 was certainly a turbulent year for commodity prices. Oil didn't hit the peaks of 2008, but it averaged 110 dollars a barrel, its highest ever level across the whole calendar year.

UK gas prices were volatile, low demand, mainly due to warm weather, pushed prices down at the beginning and at the end of the year. But events in Japan caused them to spike up sharply in March. NBP averaged 58 pence per therm, 50% up on 2010 and the trend remains upwards. Gas prices for next winter are currently around 15% higher than for the current winter.

Power prices followed gas prices upwards, but with a squeeze on spark spreads which remained depressed throughout the year. Spark spreads have fallen even lower in recent weeks as gas prices have risen and coal fired generation does have a significant advantage for 2012, but this is, of course, the last year of free carbon allowances.

In the US, gas prices fell further from the levels that were already very low by international standards. We have seen some recovery in recent weeks, as some companies have scaled back their shale drilling, but the differential to prices elsewhere in the world looks set to stay.

Our integrated model stood up well to that commodity price volatility. We were still able to post an increase in earnings, despite the winter months being some of the warmest on record, and despite the increase in tax rates for our gas and oil production in the UK.

Here are the key financials for the group as a whole.

As you can see, revenue rose 2% to £22.8bn, mainly due to higher upstream revenue resulting from the higher prices. Downstream revenue was actually lower than 2010, despite higher retail prices, as consumption fell due to the warmer weather, with the result that average customer bills were actually lower than they were the year before.

Operating profit was also slightly ahead, with strong growth from the upstream, and from North America, offsetting a return to more normal levels of profit for downstream in the UK, after an exceptional 2010, and a lower result from storage.

Interest costs fell due to the bond buyback we did at the end of 2010. In contrast, the tax rate rose, to 40% due to the shift in mix back to the more highly taxed upstream, and due to the increase in tax rate for UK gas and oil production, partly offset by the benefit of lower ordinary corporation tax rates.

The net result was earnings up 3% to just over £1.3bn, which translates to 25.8 pence per share.

We are proposing a full year dividend of 15.4 pence, which will give growth of 8%, around 3% ahead of inflation. The robustness of our overall business and our strong cashflows has allowed us to push up the payout ratio and maintain our commitment to provide real growth each year.

Here's the breakdown of the divisional results, and you can see the integrated model at work, with higher upstream profits offsetting the lower downstream result.

Starting with UK downstream, British Gas, there we posted results of just over £1bn. Within that, we saw residential energy margins move back to more normal levels, and a lower result from BGB, but services still delivered 10% growth in challenging market conditions.

In BGR, gas consumption was down sharply, by over 20%, as we went from one of the coldest years on record to one of the warmest. That resulted in lower revenue, despite higher unit average retail prices,13% higher for gas and 10% higher for electricity. Margins were within our 6% to 7% target range, but were obviously well down on the unusually high levels of 2010.

Services continued to grow, despite the weak economy holding back the installations in particular. Revenue grew by 3% and the cost reduction steps we took allowed us to increase margins and deliver a 10% increase in profit.

BGB also faced challenging market conditions, with the warm weather and weaker economy both impacting consumption. We were pleased to be able to hold margins, but we are seeing more competitive pressure in the B2B energy sector, emphasising the need to push on with the development of our services offering for business customers.

Turning to UK upstream, here operating profit was also over £1bn, an increase of some 33% from 2010.

That growth was driven by the much higher gas and oil production profits. As you can see, gas production volumes actually fell, entirely due to lower output from Morecambe. The field, of course, is in decline, but more significantly is that we chose not to run Morecambe for several weeks as we prioritised economic value over short term profits.

Much of that shortfall in gas volumes was made up by higher, more valuable oil production, which was up 6%. We also benefited from higher realised prices for both gas and oil, up 24% and 22% respectively.

In power, the CCGTs continued to suffer from the low spark spreads with realised spreads and power generated both down significantly. Four of the stations were put into preservation mode for parts of the year, and we have now announced proposals to close two stations and switch three others to peaking operation.

In contrast, the nuclear fleet performed extremely well, generating over 55TWh for the first time since 2005, and benefiting from higher power prices. Wind also did well, with much better load factors resulting in a 21% increase in output.

Overall, the power segment increased profit to over £250m, as you can see, despite the CCGTs only breaking even.

The storage result was well down, as expected. Average SBU prices were almost 30% lower, reflecting the collapse in summer/winter differentials, and that flowed to the bottom line, resulting in the profits you see there of £75m.

In North America, Direct Energy had a very strong year, with profits up by a third to £312m.

Within the overall DE result, residential energy fell back to £161m as we were not able to completely offset the decline in Ontario with growth in Texas and the US North East. The business was also impacted by the sharp spikes in Texas power prices due to extreme weather in both February and August. Nevertheless, margins remained healthy and, at 6.7%, were actually higher than those for residential energy in the UK.

Business energy continued to grow strongly, adding volume and expanding margin.

In Services, this was the first full year for the Clockwork business, acquired mid-way through 2010. Good growth in on demand work and tight cost control enabled us to almost double profits to £28m.

Upstream, our power stations were beneficiaries of the price spikes there due to the extreme weather with output up some 36%. We also increased gas production in Alberta, by 39%, due to the Wildcat Hills acquisition, which also contributed to much lower unit operating costs. Overall, we were able to eliminate the loss seen in 2010, and DE's upstream business recorded £13m of profit.

We did have a number of exceptional items within the 2011 results, as shown on the screen there. Continued low spark spreads, and our proposal to close or downrate five of the stations, has resulted in us taking an impairment of £226m on the CCGTs in the UK.

We have a group wide cost reduction programme underway, with related restructuring costs of around £150m this year, and a similar amount expected next year. That cost reduction programme includes substantial savings in pension costs, with a 2% cap being put on increases in pensionable pay. That is lower than the previous assumption for pay increases, and results in a one-off pension credit of over £300m, in addition to the ongoing savings. The UK pension schemes now show a surplus rather than a deficit, at least under the IAS19 accounting rules. We are scheduled for a valuation as at 31 March this year, but we do expect to have to continue to have to make deficit payments into the schemes, as the trustees will apply very low gilt yields to discount the liabilities, not the more generous corporate bond yields used by IAS19.

Our exit from continental Europe has caused us to reassess the pipeline capacity contracts we have there, and the tolling contract we have for the Rijnmond CCGT in the Netherlands. With lower gas spreads, and spark spreads even lower than the UK, these contracts are out of the money, and we have made a provision of over £200m.

The last two exceptional items, the deferred tax impact of the higher tax rate on UK oil and gas production, and the loss on the Oxxio sale you saw in the first half. Note that there will be a further deferred tax hit of around £60m in 2012 due to the restriction of tax relief on decommissioning costs to 50%, which is only being legislated for in this year's Finance Act, a year behind the increase in SCT.

Turning to cashflow, you can see that the business remains highly cash generative, with EBITDA of over £3bn. The working capital outflow from 2010 was reversed as downstream volumes in the UK returned to more normal levels. So the cash we generated was broadly sufficient to cover interest, tax, dividends and £1.6bn of capex, leaving net debt up only a little, at £3.4bn.

As expected, upstream capex stepped up, to over £600m, as we put capital into a number of projects, including Ensign, York, Seven Seas and Rhyl. We also continue to invest significant capital into offshore wind, with the spend on Lincs making up around two thirds of the £300m spent in the power segment.

At the bottom, acquisitions in 2011 included PH Jones within British Gas, Wildcat Hills in Alberta, and the US downstream acquisitions of Gateway, First Choice Power and Vectren. These were partially offset by the proceeds from the sale of Oxxio.

Looking into 2012, we foresee further significant organic development. In upstream gas, there will be further spend on York and Rhyl, with significant investment also planned for Kew and on Valemon, which we are acquiring from Statoil. Subject to the timing of the final investment decision, we may also see significant spend on the Cygnus project.

Power includes most of the remaining expenditure on Lincs, although our net investment into the joint venture could vary depending on where we get to with project financing, and on the potential sale of the transmission assets out of the project. 2012 could also see the first significant spend on Race Bank, our next offshore wind project.

Our current estimate is for organic capex of £1.4bn this year, but there are a number of variables that could swing that up or down. There will also of course be substantial spend on acquisitions, with the £1.4bn you see there representing the acquisitions we've already committed to upstream and in North America.

As you know, our credit ratings are important to us. I thought you would find it useful to see how the rating agencies look at our financial position. Rather than simple EBITDA/debt multiples, they look at a range of cashflow and economic debt measures. The key ones are FFO, funds from operations, to debt, and RCF, retained cashflow to debt. In both cases adjusting debt for operating leases and similar commitments. The calculations for 2011 are shown there on the screen.

It's not just about one year's figures of course, and other non-financial factors come into play. But typically the agencies look for us to have FFO/debt above 35%, which we comfortably do as you can see. And RCF/debt in the mid-twenties. We are tighter against that measure, but still have half a billion of headroom. Remember as well, of course, that spending on acquisitions, such as the three upstream deals that we have announced, adds to cashflow as well as adding to debt.

So in summary then, a good set of results, with profits ahead of 2010 despite some headwinds across the group. Upstream gas and oil production, and nuclear generation, together with a very strong growth in North America, were particular highlights.

We were able to increase the dividend by 8%, reflecting our confidence in the group's long-term earning capability, as well as our strong balance sheet position and strong cashflows.

For 2012, we are looking to improve on the profit growth we achieved last year. With retail prices currently above last year's average, and assuming normal weather, BGR should have higher revenue which, with normal margins, should translate into better profits for British Gas as a whole. Upstream, we expect higher production from the existing assets, with a further boost from the acquisitions, albeit the tax rate, and the interest charge, will climb as a result of those acquisitions. We will also look for further growth in North America, giving an overall positive picture right across the group, subject to the usual variables of weather, wholesale prices, retail prices and production performance.

With that, I will hand over to Sam.

Chief Executive's Review
Sam Laidlaw - Chief Executive

Thank you very much Nick, and good morning everybody. As you've heard, 2011 was a tough year, presenting both global and local challenges. However, against this backdrop, the business performed very well, delivering higher earnings, and these followed on from a strong performance in 2010.

And we've made important progress, which will position the business well for the future. Sharpening the business downstream; delivering our investment programme upstream and building scale in competitive markets in North America.

Turning to the performance in the year, let's start with British Gas. I'm particularly pleased that once again we achieved an increase in our net promoter score in both energy and services, and for the first time achieved a 4* rating from Consumer Focus. And we continue to differentiate ourselves through innovation, with constantly improving online offerings, new propositions for the smart home of the future, as well as our successful partnerships with Nectar and Sainsbury's, all of which are helping to provide customers with additional choice and value.

Early in 2011, we faced significantly higher wholesale prices, for electricity and particularly for gas, alongside rapidly rising environmental and transportation and distribution costs. This required us to increase our tariffs in the second half of the year, leading to increased churn and a small reduction in the number of energy accounts over the year.

In a rising price environment, it is even more important that the industry engages closely with customers, and all stakeholders. We've therefore led the way with our 'honest conversation', to help customers understand the drivers behind energy prices and to explain the steps we're taking to simplify their bills. And I'll return to this later.

We were also the first of the major suppliers to implement a price reduction this year, with a 5% cut in our standard electricity tariff, making us once again the cheapest major supplier for electricity.

In Services, the business performed well, despite the effect of the weak economy. We added 144,000 product holdings and the rollover of insurance based contracts is now complete, and the agreement we reached with our engineers allows us to offer a more flexible and responsive service.

In British Gas Business, the results for the year were impacted by the effect of warmer weather and the economy. The number of customer supply points reduced slightly, partly reflecting site closures. In this environment, it's all the more important that we deliver high levels of service, tailored to the needs of our customers, while expanding our range of business services offerings.

And we continue to achieve growth in New Markets. The business now generates revenues in excess of £250 million per annum, and we expect it to make a positive contribution to operating profits this year.

In summary, the downstream business is performing well, despite difficult market conditions.

Turning now to the UK upstream business, where we achieved strong performance across the portfolio. In gas and oil, work on our projects is progressing well. We've brought new production on stream, at F3-FA and Goosander. We've further improved the performance of existing assets, such as Grove and Chiswick. And we're benefiting from new acquisitions, such as the stake we acquired in the Statfjord field from Shell in 2010.

We have also added to our reserves, ending the year with 440 million barrels of oil equivalent 2P Reserves, more than replacing our production for the year. And as you can see on the chart, we have further reserve additions to come, with the recent Norwegian and UKCS acquisitions set to add over 175m barrels a year equivalent to our reserve base.

We have also strengthened our partnerships with leading worldwide gas producers to bring gas to the UK, taking delivery of our first LNG cargos under the Qatargas supply contract and entering into a new 10 year agreement with Statoil.

In power, conditions have been tough for gas fired generation. However, this was more than offset by improved output and achieved prices for both nuclear and wind. And on our Lincs offshore wind farm development, we are making good progress and expect to produce first power later this year.

Here is our upstream production profile chart as of a year ago, with the business capable of sustaining production at the 50m barrel a year equivalent level, in itself reflecting the scale and capabilities delivered through the Venture Production acquisition.

And here is the corresponding pro-forma position for 2012, with production comfortably around the 70m barrel per year equivalent level. This includes production from the recent Statoil and Statfjord transactions as well as the acquisition from TOTAL we announced yesterday. You'll see from the chart that in addition to increased cash flow and earnings we are now less reliant on exploration to maintain production.

Turning next to North America, where we've had a very good year financially and have increased the scale and depth of the business, as a platform for continued growth. Downstream in residential energy, we've increased our customer base by over half a million accounts. We've built on our existing positions in Texas and the Northeast, both organically and through acquisitions, adding some 700,000 customers, increasing our market share and delivering strong synergies. However in Ontario, the position is more challenging, with the ECPA legislation making it hard to acquire and retain customers. As a result, we're facing significant customer losses in Ontario, and are managing the cost base to minimise the impact.

In business energy, in North America, we had another good year, and although competition is intensifying, we were able to achieve further volume growth while sustaining our margins, and consolidating our position as the number 3 player in the US market.

In Services, following the acquisition of Clockwork in 2010, we now have a solid platform for growth. And through the Home Warranty of America transaction, we will have the capability to sell insurance based contracts, alongside our on-demand products.

While Upstream in North America, we delivered a much improved result, despite the low gas price and weak spark spread environment. In gas production, we're benefiting from high volumes and a lower cost base; and in power generation, we were able to capture the benefit of power price spikes during the extreme weather in Texas.

So in summary, 2011 was a year of considerable achievement across the Group, and our business model has proven to be both robust and resilient.

Looking now to the future, our immediate aim is to maximise the returns from our existing assets, both safely and reliably. Downstream, this requires us to drive efficiency savings, while still maintaining excellent levels of customer service, to leverage our scale and brand. Upstream, we have a strong portfolio of both operational and development assets. Here, we are deploying our capabilities to maximise returns from the existing portfolio and successfully deliver our in-flight projects.

And as we look to longer term growth, it is important that we take a disciplined approach to investment, maintaining a healthy and competitive balance between the upstream and the downstream, under the vertically integrated model.

Each of our investment options is considered on its own merits, but also in terms of the fit with the wider portfolio, incrementally strengthening the hedge, maintaining appropriate geographic diversity and delivering value and long-term growth as well as short-term earnings.

Turning now to our cost reduction programme. Towards the end of last year, we launched a Group-wide review of the cost base, given the challenging economic environment. In total, we expect to save half a billion pounds over the coming two years against our controllable cost base. £400 million of this saving will be in operating costs, more than offsetting the effect of inflation and allowing scope for continued investment for growth, within the existing cost base.

Headcount reductions play a significant role, with some 2,300 FTE reductions already announced, for example in field sales and across many of our support functions. However we remain closely focused on ensuring that customer service levels do not suffer as a result, and we will continue to develop our staff and recruit into our growth businesses.

In summary, our goal is to sharpen our competitive position across the Group, upstream and downstream, while also enabling the business to invest for growth, for the benefit of both customers and shareholders.

This slide gives some further colour. On the right, you can see the split across each area of the business, with around two thirds of the savings being targeted in British Gas, but savings will also be in Centrica Energy, Direct Energy, and indeed the corporate centre.

In British Gas, the savings amount to a 10% reduction in operating costs in our core business over the next two years, even after allowing for the effects of inflation. Here, we're benefiting from our systems investment, increased online penetration, back office efficiency savings and more streamlining of our support operations.

In Centrica Energy, the priority is to deliver continued growth from the enlarged business. However, we have also been able to identify efficiency savings here in our supply chain and support functions, together with savings from the proposed closures in our CCGT fleet.

In North America, we have taken the decision to relocate our Head Office, from Toronto to Houston, bringing together many of our activities on a single site. In addition, we continue to drive efficiencies and synergies across all parts of the business.

And in the corporate centre, we have reduced the headcount by two thirds, transferring many activities back to the business to drive greater accountability.
As I mentioned earlier, we launched the 'Honest conversation' towards the end of 2011, with the aim of building trust; building understanding; and delivering for our customers. In British Gas we now have our two principal tariff types and we're making it simpler for customers, to help them select the right tariff for them. We are also providing clearer information regarding the components of the bill, including the cost of Government environmental policy.

And we're also leading the industry in terms of help for the vulnerable, with the widest eligibility of any of the Big 6 for the Warm Homes Discount.

However, with affordability now a key issue for households, and the future cost of energy rising, it's important that the whole industry, including Government and the Regulator, engages in a process to build understanding and improve transparency. Any proposed redesign of the retail market needs to be proven to be transparent, simple and lower cost for the consumer, as well as continuing to promote innovation, choice and competition.

Turning to the Upstream. Significant investment is required to deliver the country's energy needs for the next generation. However, much remains to be resolved under the Government's Electricity Market Reform proposals before investment decisions can be taken.

As we set out in our upstream investor day in December, we see the most immediate investment opportunities in upstream gas and oil, and in offshore wind, with further options in new nuclear, biomass, CCGTs and new gas storage, subject in each case to the returns being appropriate.

In gas and oil, as you have seen we have made good progress towards achieving our target of 75m barrels equivalent production per annum, while in offshore wind the priority is to bring the Lincs wind farm development online and to take a final investment decision on Race Bank.

This is consistent with our objective of maintaining a competitive, post-tax energy hedge of around 50-60%, giving appropriate balance between the upstream and the downstream, and the geographic diversity across the portfolio.

In North America, we are making good progress towards our target of doubling the profitability of the business, with the potential to increase the scale of the business further, for the right opportunity.

Downstream, we continue to seek growth in our core de-regulated markets, Texas and the Northeast, increasing scale and delivering cost efficiencies.

We also now have a platform to expand our services offering, replicating the UK model with the introduction of annual contracts and, over time, cross-sell opportunities to our energy customer base.

And upstream, we continue to seek value-adding opportunities in both gas and power, moving towards the 35-40% cover level over time, but again only where attractive returns can be identified.

So in summary, the business is performing well in a challenging environment, maximising returns from the existing assets, putting capital to work through targeted investment and maintaining an appropriate balance across the portfolio.

Our business model remains resilient, delivering strong cash flows and year-on-year earnings and dividend growth, with this year's increase in the dividend reflecting our confidence in the future prospects for the business. We also have attractive investment opportunities to deliver long-term growth, and have an appropriate cost reduction programme in place, to ensure that we remain competitive, for the benefit of both customers and shareholders.

So I think with that, I would now like to open it up to questions.

Questions and Answers

Q1. Bobby Chada, Morgan Stanley

Given that you were the first to cut prices early in the year, can you give us a feel for how the churn rate has evolved maybe in the second half and what you are seeing in 2012 so far? That is the first point.

The second question is on the US business. Gas prices are very weak but noticeably they are much higher further out the curve and it seems like as soon as you get close to delivery they consistently collapse. Are you doing anything to hedge further out and try and capture higher prices before you get to prompt or is that not possible?

Answer: Sam Laidlaw
The first one is around churn rate and I will let Phil speak to that, but when we have a round of price increase or price reductions there is a brief period of churn and then it settles down. I think it is too early to see what the result of the most recent one is. But it also is a function of differentials between suppliers which have narrowed, Phil you might want to touch on this.

Answer: Phil Bentley
As Sam said, some of these haven't played through yet in the market. But if I take February, we are about flat on customer numbers. So it is sort of settling down. I think to answer your question directly, churn is at the lowest it has ever been, but we stopped field sales and other ways of selling. We are not discounting online as heavily as others have done in the past and not offering any sort of loss leader products, which is all part of the honest conversation. And again you are seeing SSE respond to that in a similar way. I think there is probably a little bit more discipline still to come in the industry before we get back to a level playing field. But certainly, if I look forward, I think we have got some good product launches coming. I think our relationship with our customers is excellent. Our service has never been better actually. And so we are pretty optimistic about 2012.

Further question
Is it fair to say churn, if I heard you correctly, is at the lowest it has ever been? The cost of churn by definition is at the lowest it has ever been as well?

Answer: Phil Bentley
It is, but again you know one swallow doesn't make a spring. We need to see how it all plays out throughout the year.

Further answer: Sam Laidlaw
And building on that it would be fair to say that quite a lot of the churn was driven by the field sales activity and as that has reduced the churn has come down.

The second question I think was around the forward curve in natural gas markets in the US. We do have a pretty well hedged position there. But I will let Nick speak to the strategy going forwards.

Further answer: Nick Luff
You are absolutely right Bobby and we do seek to capture some of that contango in the curve, so we are reasonably well protected for our 2013 production in terms of how we are hedged. Eventually it will catch up with you unless you have that continued collapse into the prompt. But we do generally hedge out a little bit further in the US than we do here.

Q2. Lakis Athanasiou, Independent analyst
Lakis Athanasiou, independent analyst. Just a couple of questions. One on North America and a couple on UK stuff. Ontario exit, are you managing to maintain your margins as you are exiting or are your margins also coming under pressure as well as customer numbers?

Albertan E&P, your 2011 numbers, have got about zero net contribution, but if you have been hedging for 2011 you may have a positive. Can you give me a rough indication of broadly what your EBIT was on Albertan E&P?

On British Gas residential you have a 21% fall in average household use, I estimate that is about 20% on weather, 1% on efficiency. Does that tie up with your own estimates? And could you also make a comment about household efficiency progression and if there has been a slowdown in the last year and why?

And on Rijmond 2, were you applying any credits from your provision in 2011 to the power generation numbers at all?

Answer: Sam Laidlaw
Okay, so I think four questions there. Let me start with Ontario exit. We have been as I said and we made clear in the statement, losing some customers. We have also been containing our costs. Chris you might want to speak to what has been happening to net margins in Ontario. And also Nick I think will touch on the profitability of our Western Canada business, recognising that we have hedged a lot of the gas sales out.

Answer: Chris Weston
So in Ontario over the last year you see Lakis we have lost about 200,000 customers and we will see continued customer loss over the next year. Margins have come down, but are higher than the average residential net margin still. So we are renewing customers on a lower margin, but they are still pretty generous.

Further question
Staying around the 10% level or a bit lower?

Answer: Chris Weston
They are higher than that.

Further Answer: Nick Luff
So on the Albertan E&P, we are actually expecting higher profit in '11 than '10 because we have expanded the business in Wildcat hills which has been very good reducing the cost. So we are making £20-25 million there, which isn't a fantastic return on the capital, but it is still a positive contribution. And just in the overall upstream, remember we did have the benefit of the price spikes in August and February this year so you would have to take that out if you are looking at the overall upstream segment.

Further answer: Sam Laidlaw
And I think your next question was around energy efficiency. You are absolutely right, it was gas and it was particularly focused on gas as I understood it. And overall gas consumption down 21% and the question was how much of that was energy efficiency versus weather? I think 1-2% level of energy efficiency is probably right. I think it is higher than 1% but probably similar to 2% territory.

Further answer: Nick Luff
And your last question was about the impairment of the CCGTs and what effect that would have? The benefit that you get is that you get a lower depreciation charge and that is obviously spread over the remaining life of the stations. I would say that benefit is relatively small compared to the pain of low spark spreads.

Further question
So there was no cost of sales type re-provisioning if you see what I am saying?

Answer: Nick Luff
No gas contract stuff in there, no.

Further question
But you haven't got any fixed assets in Rijmond 2?

Answer: Nick Luff
Sorry, I was talking about the UK. Okay so on the European ones yes you are absolutely right, we were losing money on those contracts and we provided for those loses. So there won't be losses in the European gas transportation contracts of the same scale that there would have been otherwise.

Q3. Martin Brough, Deutsche Bank
Martin Brough from Deutsche Bank. Just following up on the retail side. Given you want to maintain competitive position do you expect your competitors to actually be pricing in a way to try and get positive margins going forward?

And broadly, what kind of benefit would you see Centrica getting over the competition either through pricing or better cost efficiency?

Answer: Sam Laidlaw
I think the first part of your question is where do we think our competitors will be? I think it is dangerous for us to try and predict exactly how they will put price up and where they will position themselves. We have noticed certainly, and you saw that in Ofgem's report, that the levels of margin in the supply business are very low. But I think we aim through our cost reduction programme to remain as cost competitive as possible and we expect that that will enable us to continue to be very competitive in the marketplace, as Phil said earlier. I think where we are at the moment is roughly flat. It will obviously depend on new propositions that we bring out, new propositions that our customers bring out going forwards. But I don't think we are seeing any significant change in our competitor's behaviour at the moment.

Further answer: Nick Luff
It is interesting because what will happen when free carbon stops in 2013 and whether that will influence their behaviour in the retail market, we don't know.

Q4. Edmund Reid, JP Morgan
Edmund Reid from JP Morgan, two questions. First one was on the Ofgem liquidity proposals which came out yesterday. Maybe a bit unfair to ask you about them so quickly. But I was wondering if you thought what kind of impact you expect it to have on the business?

And the second thing is on services. Clearly one of your competitors Homeserve, has had issues with the FSA and I just wanted to make sure or to understand better whether you have had conversations with the FSA and whether you are happy with what you are doing?

Answer: Sam Laidlaw
The first question around Ofgem's liquidity proposals. I think the first point to make, and I will let Mark fill in on this, is that actually liquidity through the exchanges has gone up very substantially, fivefold in fact in the last few months. But it has all really been in the prompt. And I think one of the things that Ofgem is trying to encourage is the development of more liquidity in the forward market. And the position that we have consistently maintained is that we would like to see more in the forward market. We are of course probably a more active buyer than many of our competitors are. But actually the big issue for a lot of the smaller companies, apart from clip sizes, which I think we have already addressed, is actually one of, have they got sufficient

capital and balance sheets to be able to post the margins that are required if you buy electricity forward? So that is more of a problem I think for the smaller companies than liquidity per se, but I will let Mark speak to the proposals in more detail and then come back and talk about Homeserve.

Further answer: Mark Hanafin
So I think the positive thing was that Ofgem recognised that liquidity was improving and that a number of options were on the table to discuss further. In terms of your direct question, how does it affect us? We sell the majority of our power that we produce into the market anyway and we balance through the system and we balance Phil's business. So in terms of direct impact I am not concerned from that perspective. What I am concerned about is the point that Sam mentioned which is you can address liquidity, but if the underlying issue is credit worthiness then that is a much more difficult thing to resolve. And I think we have to face up to the fact that the energy business and being in retail in a volatile commodity market is a business for somebody with a balance sheet. That doesn't mean you shouldn't have lots of new competitors, but they do need to have a balance sheet to be able to weather those storms. And I think that is one of the things that we need to have a better conversation on.

Further answer: Sam Laidlaw
The second question Ed you had was around compliance and the issues Homeserve have had. And I will let the Chairman of British Gas Insurance speak to that. We have recently had a review and came out of it well.

Further answer: Nick Luff
Something very close to my heart. Yeah, absolutely we have just had the review from the FSA, come out of that pretty well. But you know absolutely no room for complacency. We continually work to make sure our scripts are as good as they can be, our controls are in place. And it is something we watch very closely and will keep working on.

Further question
Sorry, follow-up question. Has the competitive dynamic changed at all in the services market, given Homeserve's issues?

Answer: Phil Bentley
A little bit. I mean they are probably finding it harder to win customers, but they have always been pretty good at retaining existing customers. As you know, we have a couple of new water affinity deals with Wessex Water and Bristol Water and now with Thames Water. So it will take time, but that business is growing from our point of view and we are quite pleased with the progress.

Q5. Gus Hochschild, Mirabaud Securities
Just one question if I may on yesterday's announcement with the Total acquisition. So it is about 3.4 million barrels I understand per annum. And you have given guidance that they should come onstream, the first closing should be in July I think. So what sort of production should we anticipate for next, for this year and next year and what sort of decline rate should we factor into our models?

Answer: Sam Laidlaw
What was the second question? The first question was production and the second question was?

Further Question

Decline rates please?

Answer: Sam Laidlaw
I mean, the answer to the first question is these fields collectively produce about 9,300 barrels a day over a twelve month period. So you can assume half of that if you like on an annualised basis. And you know, what is attractive about this particular portfolio of assets and we know a lot of the fields well because we are already in three of the bigger ones anyway, is obviously they are near term production, they don't require a lot of future capital and generate therefore strong cashflow and headroom. And in terms of the decline rates actually if you look at Maria and you look at Alba, they would be normal North Sea decline rates in the sort of 10-11% range. Not the sort of Morecambe rates at sort of 16%.

Q6. Peter Bisztyga, Barclays Capital
Yes, it's Peter Bisztyga from Barclays Capital. Two questions on the US if I may. Firstly, could you indicate roughly what proportion of the year-on-year increase in operating profit came from acquisitions? And how much was underlying organic growth?

And then secondly, could you just sort of detail a bit what the end game for Ontario is? Is there a sort of level of customer numbers where you sort of expect to stabilise?

Answer: Sam Laidlaw
Two good questions. You have got a number of moving parts going on in North America. Having been very profitable in Ontario, we are now losing earnings there and actually you have got new acquisitions that are adding earnings. The two effectively, largely net themselves out. So you can think of the organic growth. Nick do you want to?

Further answer: Nick Luff
So the acquisitions actually didn't contribute a huge amount last year because you have got some integration costs and the like. And only really the full year effect of Clockwork and Wildcat Hills played significantly into 2010. I guess a bit of Gateway as well. But 10-15% of the growth would have come from acquisitions. The rest organic. And the organic as Sam says, clearly is a mix of decline in Ontario offset by growth elsewhere.

Further question
And sorry, the end game for Ontario?

Answer: Sam Laidlaw
The end game for Ontario, what we are effectively doing is managing a decline there and we will sustain it as long as possible. There is always the possibility that the legislation will change. We are not holding our breath and we are managing the costs down. But as Chris says, you know, as long as we can continue to write profitable business there, which we are managing to do at reasonable margins, then we will continue to do that.

Further answer: Chris Weston
In the Ontario market we will have a much lower number when this run-off occurs, but we also have a significant services business in Ontario. So we will maintain that and it will continue to grow, and that has about 2 million customer relationships in it. And that is important. And although the government was returned at the last election,

energy policy is still a fairly hot issue and the situation may change on the energy side.

Q7. John Musk, RBC

It's John Musk from RBC. Can I ask probably three questions on nuclear. Firstly what is your level of invested capital so far on new nuclear?

And secondly, if you decide to proceed on new investments, how affordable is the Capex on those plants, given the probably the uplift in Capex now on the upstream gas assets?

And then finally, on the flip side, if you don't proceed because you can't get comfortable with returns or the build costs, how would you look to exit that and what makes you think you would be able to recover the invested capital you have already put in?

Answer: Sam Laidlaw

Good questions John. I think if we start with how much capital we have put in. You know excluding anything we may have for goodwill around the British Energy acquisition, the capital we have actually put into new build is about £130 million at the end of the year. And we would expect to basically not spend more than £200 million getting to FID. And that is really our sort of top stop. If we spend any more than that we would be reimbursed if we dropped out by our partner.

In terms of how affordable it is, actually I think for us this is really around returns, but it is also of course around how much capital do we want in any one project relative to the rest of the Group and making sure that is appropriate. But I think in terms of affordability the transactions that we have been doing in the upstream, whilst some of them have some increase capital requirement, they also bring a lot of operating cashflow. And indeed the way, particularly in Norway, the way the system works you get tax deductions as you continue to invest. So actually the capital investments and acquisitions that we have made are not really reducing our capacity to do new nuclear. At the end of the day it is can we get a satisfactory return out of new nuclear and that is I think the biggest question. Obviously if we were to decide not to proceed then we would have a discussion with our partners around the terms of exit.

Q8. Jonny Constable, Nomura

Hi, Jonny Constable from Nomura. Two questions, firstly on residential supply. I was wondering if you might be able to give us some flavour on the hedging position for 2012 in particular your gas and supply business?

And secondly, just trying to understand the numbers on the cost savings from British Gas. If I take 60% or so, £500 million, that is £300 million over the next two years, if I read your results announcement correctly, you have got £1.4 billion of operating costs or so. So if I take 10% of that I have got £140 million of the £300 million. What is the rest? Does that fall within the £100 million or so of reduction coming from cost of sales? If so, what is that and how do you get it down?

Answer: Sam Laidlaw

Let me start with the hedging position first. I think we, in common with all our competitors, don't disclose the amount of gas or electricity we have bought forward. What we can say is that we buy some of our gas obviously up to two years forward, some of it a season forward and some of it in a month ahead and day ahead markets. And we have previously published bands around roughly where we want to be and we are still within those overall bands. So nothing exceptional on that.

I think in terms of your second question. You are absolutely right that we expect to take £300 million out of British Gas. We have got off a cost base of £1.4 billion, your question was?

Further question
If I take 10% of the cost base off, that is £140 million, so you have got to get to £300 million?

Answer: Sam Laidlaw
Yes because we have got growth going on in. So if you go back to the chart that I put up you will see there is some growth going on in British Gas as well because we are reinvesting and so the net number will be smaller than the £300 million because of a combination of inflation and investment in the growth businesses. So that the significant growth businesses here are as we grow the new markets business and as we grow the smart meter activity and the roll out of the smart meter activity, that we will see top line growth for those activities which will more than compensate for any growth in cost. But that is the contra entry there.

Further answer: Phil Bentley
Our operating cost is £1.6m actually so 10% is a little bit more. Our cost of goods is £1.2 billion. So what you have got to remember in the services business is all the labour is part of the cost of goods. So anything we do around pensions and pay and rostering, all plays through in the cost of goods in services and in the new businesses. And that is how we make the numbers work.

Further answer: Sam Laidlaw
But we can unpack that for you afterwards. It is easy to walk you through.

Further answer: Phil Bentley
In terms of parts and efficiency there, we have negotiated vans and boilers and you know we are working hard on our cost base and we are confident about the delivery of those targets.

Q9. Mark Freshney, Credit Suisse
It's Mark Freshney from Credit Suisse. I just have three questions. Firstly on the power generation hedge in the UK. Clearly you have lost or closed a couple of plants, some of the existing nuclear reactors reach 40 years of age in 2016. So your coverage of your peak energy requirement goes down. Does this mean that there is a gap to fill in terms of your electricity hedge in the UK?

Secondly, Nick you mentioned you are now focusing on these RCF to net debt and FSO to net debt numbers, in the presentation. What are the desirable metrics or what is the floor for those metrics that you are looking for?

And my third question is, would it be possible to give some more colour around the impairment of the transportation contracts in Europe? I mean two years ago you impaired the Sean Field which was an oil linked contract. Now you are impairing a transportation contract. How much more potential is there for impairments relating to you know problems with the gas market in Europe?

Answer: Sam Laidlaw
So I think Mark your first question was around the power hedge. And you know if you think of actually closing down old CCGTs, it doesn't really make much difference to the hedge for gas, because gas is the fuel. The question I think is a valid one around nuclear which is clearly more of an issue over time and indeed you know we have a contract with DRAX that will roll off that provides a hedge as well. So replacing that over time to keep to the 50-60% level is something that ideally we would like to do. But we will only do it for good value. And it doesn't mean that necessarily we have to do it all with assets either in the same way we have the DRAX contract, we can do it contractually if we wish to.

Your second question I think was around RCF to debt and where would we like to be ideally.

Answer: Nick Luff
So obviously what matters is what the agencies look for us to be trying to hit. So they typically would want us on FFO to debt to be above 35% which we are quite comfortably as you saw from the numbers. We are a bit tighter on RCF to debt which they would typically look for us to be in the mid 20s. I mean you shouldn't get overly hung up about one individual year of course because you have to look through the cycle etc. But we are a bit tighter against that one than we are about the FFO to debt.

Further answer: Sam Laidlaw
And I think your final question Mark was around impairment of the transportation contracts and is there anything else coming in Europe? And the answer is you know we took this opportunity when we exited Oxxio to actually clean up everything we have in Europe.

Q10. Andrew Mead, Goldman Sachs
It's Andrew Mead from Goldman Sachs. Two questions. One was you have done I think three deals in upstream in as many months, and different sizes. Could you just explain is that just a reflector on new push into that market or is it perhaps market additions whether it be liquidity or prices?

Answer: Sam Laidlaw
I mean actually, two of the three transactions we have been working on for over a year. The Total one was a little quicker, but it was still, it took a number of months. Andwe were able I think to take advantage of slight softening we saw in the autumn to actually manage to come to terms effectively. But they have both been transactions that they happen to coincide, but in announcement, but they had been in discussions for a long time.

I think what we are signalling which is an important point Andrew is we are sort of, we really at the level we are now at of 70 versus the target of 75, we are pretty close to being balanced and therefore, and we need having made these sizeable commitments and acquisitions, you know, I think 2012 will be very focused on closing them and getting a return out of the investment we have made rather than you know seeking to expand that part of the business significantly in 2012.

Further question
And the other one was just on British Gas, the new services, new energy business. Is that going to be big enough to be a separate fourth reporting line next year?

Further Answer: Sam Laidlaw

Not next year, but I would hope that over time it will be, yeah. But as a business that you know, £250million of revenue that is starting to become profitable, it is still too small next year.

Closing Comments: Sir Roger Carr

Finish, excellent. Thank you all very much indeed. Got the team working today as well which means their presence was really worthwhile. Thank you all very much. Thanks.

End of Presentation