



10 December 2004

Centrica 2004 Trading Update & 2005 Outlook

In line with best practice, Centrica will in future issue pre-close trading updates ahead of its preliminary and interim results and today issues its first such statement ahead of entering close period on 31 December 2004. Centrica will host a conference call from 8-9am GMT today.

The company will announce its preliminary results for 2004 on 24 February 2005.

Group results

Overall Centrica's 2004 results are expected to be in line with market expectations. The key operating and strategic themes in the second half have been:

- Challenging conditions in energy markets with further rises in wholesale gas prices
- Strong contribution from gas production and from Centrica Storage
- Improved performance in North America
- Continued investment in upstream energy assets
- Completion of the AA disposal and payment of the special dividend to shareholders
- Early commencement of the £500m share repurchase programme

Despite the significant increase in wholesale gas and electricity prices and the disposal of the AA at the end of September, Centrica expects in 2004 to maintain its record of delivering double digit year on year percentage growth in earnings (including JVs and associates, before goodwill amortisation and exceptional items). Operating profit growth, before exceptionals and goodwill, is also expected to be double digit with improvements in most business divisions.

British Gas

The second half of 2004 has seen further extraordinary rises in wholesale gas and electricity prices (32% and 18% higher respectively than the second half of 2003). In early October gas prices for January 2005 peaked at almost 80p/therm although they have now fallen back to around 40p/therm. Market prices for Q4 2004 are now around 32% higher than Q4 2003; however, Centrica has no remaining exposure to wholesale prices in this period.

The retail price increases announced in August and implemented in September increased turnover in British Gas but also, as expected, led to an increase in customer churn. To date net energy customer losses in the second half of the year are 630,000. The level of churn has fluctuated and is starting to fall as most other suppliers have also now announced similar price increases. British Gas has continued to sign up new gas and electricity customers with sales back to around 80% of the level before the price increases were announced.

In the British Gas transformation programme, rollout of the cross-selling functionality is on track to finish by the end of this year.

Upstream

The level of gas production for the full year is expected to be the same as 2003 due to higher production in the second half to capture the benefits of high gas prices.

Wholesale gas prices have continued to impact Centrica's Industrial & Wholesale business. As predicted, losses on the industrial long-term sales contracts have increased in the second

half due to the continued divergence of sales prices and input costs and second-half Industrial & Wholesale results will be worse than the first half.

Centrica Storage continues to exceed expectations. Due to the wider summer/winter price differentials and termination in April 2004 of all legacy sales at historic prices, full-year profits will be significantly ahead of 2003.

Other downstream businesses

Centrica Business Services (CBS) has focused on maintaining margins against a background of rising wholesale energy costs. CBS has passed price increases through to customers at annual contract renewal and through periodic tariff adjustments. Customer renewal performance has been maintained in the year to date, but is increasingly challenging in the face of volatility and competition in the commercial energy market.

In One.Tel the market remains extremely competitive but the business is now benefiting from the outsourcing of certain operations to India and full-year profits will be higher than expected.

In North America the second half has shown good recovery with top-line growth and a more positive pricing environment. Despite the market reconciliation issue in Texas, which was reported in the first-half results, and the adverse impact of currency movements, operating profit is expected to be slightly ahead of 2003.

The disposal of the AA was completed at the end of the third quarter.

Financial structure

Payment of the special dividend and the accompanying 9 for 10 share consolidation were successfully completed. The share buyback programme commenced ahead of the originally announced timescale and to date Centrica has repurchased 67.4 million shares for cancellation. The weighted average number of shares used to calculate basic EPS for 2004 is estimated to be approximately 4.22 billion.

Centrica has committed to paying a full-year dividend equivalent to a 40% payout ratio in 2004, rising to 50% in 2005 under current UK accounting standards.

Investment progress

Since the announcement of its 2004 interim results, Centrica has made further investments in upstream assets by acquiring a 50% share in the Horne and Wren gas fields in the Southern North Sea and an onshore wind farm project in North East Scotland. It has exercised its option to acquire Wainstones Power Limited giving it the potential to develop a new 1,000MW CCGT power station in South West England. This month it acquired a second power station in Texas, the 447MW CCGT Frontera station. In August Centrica also entered into its first LNG contract with a 15-year supply deal with Petronas for a total of over 45 billion cubic metres of gas.

Recent activity in the upstream gas environment confirms the Group's view that patience, financial discipline and a consistent view of the market fundamentals will continue to be key to success in building both an appropriate gas supply portfolio and shareholder value.

The Group has continued to invest for growth downstream with the acquisition in the UK of DynoRod and Telco Global and, in North America, Residential Services Group and two small energy automation and control companies which enhance the offering to the business sector.

2005 Outlook

Wholesale gas and electricity prices continue to dominate the outlook for 2005. Based on current and projected forecast wholesale gas price levels the Group has decided to balance the level of margin in the short term with the need to maintain a competitive position in order to preserve value in the longer term. It is therefore the Group's intention in 2005 to not pass through to customers immediately the full impact of the forecast increase and to offset a portion by undertaking a programme of cost reductions where these can be achieved without compromising growth or customer service. In the light of this the British Gas profit margin will be similar to 2004 and will increase in 2006 as gross margins improve and the full-year impact of cost reductions takes effect. Centrica continues to believe that 8% is an appropriate and achievable net profit margin target for the British Gas business.

The key focus of the British Gas transformation programme in 2005 is on delivery of the SAP billing system which is now going through test, with the first new-format bills expected in the first half of 2005. The estimated cost of the systems elements of the programme has increased from £400 million to £430 million, including the cost of additional staff back-filling now planned to support rollout of the billing system in the light of experience to date. In addition, implementation of the home services engineer deployment system is progressing to budget (£40m) and is expected to complete by the end of 2005. As previously advised, although the benefits from the Siebel/SAP implementation are delayed, the overall transformation programme in British Gas will deliver the expected level of benefits in 2005.

Gas production in 2005 is now expected to be at least 10% higher than previously indicated. As a result of this and the higher wholesale prices, the effective corporate tax rate for 2005, excluding any changes to the accounting treatment of petroleum revenue tax, is expected to be around 33%.

In the absence of a considerable decline in wholesale prices, losses on the industrial long-term sales contracts will continue to increase and Industrial and Wholesale results will therefore deteriorate further in 2005.

To the end of November, Centrica Storage had sold 84% of all standard bundled units (SBUs) available to non-Centrica Group companies for the 2005/06 storage year. The prices achieved are higher than 2004/05 which will result in a significant year-on-year operating profit increase in 2005.

Operating profit in North America will be further enhanced by improved performance in Texas and business markets underpinned by the value generated from recent acquisitions.

In summary, the key issue facing Centrica in 2005 is the current level of UK wholesale energy prices. As a result operating margins are now expected to be lower than previously anticipated in British Gas, Centrica Business Services and Industrial and Wholesale. A significant proportion of this will be offset by forecast improved results from gas production, Centrica Storage and North America, such that the operating results in aggregate will be in line with the consensus of current market expectations. The change in mix, however, will lead to a higher tax charge which will be reflected at the earnings level.

International Financial Reporting Standards (IFRS)

Centrica's 2004 preliminary results announcement in February 2005 will be on a UK GAAP basis. Clarification is still required on the interpretation of IAS39 (embedded derivatives) and the treatment of petroleum revenue tax. The intention is to restate the 2004 results and hold a briefing for analysts and investors in May 2005 to explain in more detail the key impacts of IFRS on the Group's results.

Trading update conference call details

As this is the first time Centrica has issued a trading update the Company will host a conference call from 8-9am GMT today with Group Finance Director Phil Bentley who will

answer any questions arising from the statement. The telephone number for UK callers is 0845 245 3471. Overseas callers should dial +44 1452 542 300. The password for the call is 2332467. A recording of the call will be available in the Investor Relations section of this website from 2pm GMT today. Listen to the archived conference call.

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