centrica

TRADING UPDATE – 23 November 2017

Summary

The Company continues to make good progress in the implementation of its strategy and portfolio repositioning and remains on track to achieve the 2017 targets set out at its 2016 Preliminary Results in February. However, trading conditions continue to be highly competitive and performance delivery since mid-year within the Centrica Business energy supply businesses has been disappointing.

Iain Conn, Centrica Group Chief Executive, said "Although some aspects of our delivery in the second half of 2017 have been disappointing, I remain encouraged by our progress in implementing our strategy. The balance sheet has been materially strengthened, and we continue to focus on improving our underlying performance. We have also provided a broad and definitive set of proposals this week to improve the UK energy market for customers and look forward to engaging with the Government and regulator in the coming weeks."

In Centrica Consumer, delivery from the Group's efficiency programme is offsetting overall gross margin decline. Energy supply accounts have fallen, but this largely reflects choices we have made to focus on customer value, while in recent weeks account holdings in UK Home Services have stabilised and growth in Connected Home continues. In Centrica Business, we have experienced significant market pressures in our North America Business retail power book, and in UK Business we are not yet seeing improved operational performance flowing through to the bottom line. We are also reflecting a one-off non-cash post-tax charge of £46m in North America Business, relating to a reassessment of the historic recognition of unbilled power revenues. In the asset businesses, the Morecambe field is back on production and Spirit Energy, Centrica's E&P joint venture with Stadtwerke München, is on target to close before the end of the year, subject to regulatory approvals.

Performance and 2017 Group outlook

- We remain on track to achieve our 2017 targets and expect:
- Adjusted operating cash flow to be above £2bn.
- Group capital investment, including any small acquisitions of less than £100m each, to be below the £1bn limit with E&P capex around £500m.
- Incremental revenue investment of around £100m in growth areas.
- 2017 efficiency savings approaching £300m, in excess of the original £250m target, and in addition to 2016 savings of £384m.
- Like-for-like direct headcount reduction of over 1,500.
- Net debt to be within the targeted £2.5-£3.0bn range.

2017 full year adjusted earnings per share are expected to be around 12.5p, including a 0.8p impact from the North America Business one-off non-cash charge. This is lower than market consensus, largely reflecting lower than expected adjusted operating profit in North America Business and UK Business. We are also reflecting the expected impact of warmer than normal weather across October and November. Actual financial performance remains subject to the usual variables of commodity prices, weather and asset performance over the balance of the year.

However, with net debt expected to be within the Group's targeted £2.5-£3.0bn range, the level consistent with our financial framework parameters, and 2017 adjusted operating cash flow expected to be above £2bn, the current level of the full year dividend per share is underpinned. For a period of time, while the Group is implementing its strategy to continue to shift the portfolio towards the customer and diversifying and growing new sources of gross margin, we would be willing to operate with dividend cover from earnings below historic levels.

Divisional Performance

Centrica Consumer

In UK Home, despite the impact of account losses and warmer than normal weather in the year to date, cost efficiency delivery means 2017 full year adjusted operating profit is expected to be broadly in line with 2016. The number of UK energy supply accounts at the end of October had reduced by 823,000 since 30 June 2017, although over 650,000 of these losses relate to collective switch, white-label fixed price and prepayment tariffs, and 150,000 reflect market switching trends and the impact of our price rise in September. UK Home services account holdings are down 39,000 since the half year, having stabilised in recent weeks. Our Ireland business continues to perform well, while in North America Home accounts have fallen slightly, with H2 2017 adjusted operating profit expected to be at a similar level to H1 2017. The cumulative number of Connected Home hubs installed has now reached 750,000, up 223,000 or 42% since the start of the year, and we have now sold over 1.2m connected products in total, up 59% since the start of 2017.

Centrica Business

North America Business is expected to report full year adjusted operating profit of around £80m, with highly competitive market conditions and low price volatility putting significant downwards pressure on realised power margins, and low volatility also reducing opportunities for gas optimisation. In addition energy prices are currently backwardated, meaning the booked profit of fixed price multi-year power contracts will be weighted towards latter years, compressing short term realised margins. As noted above, we expect to recognise a one-off non-cash post-tax charge of £46m (£76m pre-tax) in North America Business relating to a reassessment of the historic recognition of unbilled power revenues. UK Business is also facing competitive pressures and we now expect the business to be broadly break-even in 2017. In Distributed Energy &

Power (DE&P), we continue to see growth with the number of active customer sites up 4% since the half year. Energy Marketing & Trading (EM&T) continues to perform well, and as previously disclosed in the Interim results full year adjusted operating profit is expected to be heavily weighted towards H1 2017.

Asset businesses

In E&P, higher commodity prices have been beneficial for unhedged volumes, although production volumes, and therefore the full year E&P result, will be impacted by the outage at Morecambe until late October related to asset integrity works to improve safety and operational efficiency. We expect H2 2017 E&P adjusted operating profit to be similar to H1 2017. In Centrica Storage, cushion gas production from the Rough asset has been stronger than expected, with up to 25bcf expected to be produced in H2 2017. As a result, the business is now expected to be profitable in H2 2017 and be close to break-even for the full year.

Group net finance charge and tax rate

The 2017 full year net finance charge is expected to be approximately £350m, consistent with the H1 2017 run rate. The 2017 full year effective tax rate is expected to be around 26%, lower than the H1 2017 rate of 29% reflecting changes in operating profit mix and the settlement of provisions. In 2018, we would expect the effective tax rate to return to a higher level.

Strategic progress

As referenced at its Interim results in August, the Group expects to have completed the first phase of its portfolio transformation by the end of 2017, fundamentally repositioning the Group as it continues to shift resources from its asset businesses to its customer-facing activities, and as it pursues long-term shareholder value through returns and growth. The Company has continued to make good strategic progress during H2 2017, developing capabilities and technology in its customer-facing Centrica Consumer and Centrica Business divisions, and reducing scale in and strengthening its asset businesses.

Customer-facing progress

- Continued investment in customer service and digital platforms resulting in a further reduction in energy supply complaints to October across all businesses relative to the same period in 2016.
- Over 500,000 customers now signed up to British Gas Rewards, providing them with personalised offers including those that reward loyalty.
- Acceleration of growth in technology-led 'Local Heroes' on-demand services platform, with around 6,000 tradespeople signed up and over 17,000 jobs now completed.
- Connected Home partnership agreed with Italian energy company Eni gas e luce, enabling 8m energy customers to purchase Hive products and solutions; Hive leak sensor launched.
- Enhanced DE&P capability through €70m acquisition of REstore NV, Europe's leading demand response aggregator.

- Continued development of EM&T route-to-market services, including the signing of a balancing and hedging contract for the 650MW Markbygden wind farm in Sweden.

Asset business progress

- Completion of CCGT and Canadian E&P disposals in H2 2017, taking total proceeds over 2016 and 2017 to £946m, at the upper end of the £0.5-1.0bn targeted range.
- The formation of Spirit Energy, the E&P joint venture between Centrica and Stadtwerke München, is on target to be completed by the end of the year, creating a self-financing, more sustainable, more capable European E&P business.
- Provisional decision from the CMA announced on 15 November to terminate the Rough undertakings and release Centrica Storage from its obligation to offer storage capacity from Rough; publication of final decision expected in December.

UK energy supply market On 11 October, Ofgem announced an extension of the pre-payment tariff cap to a further 1m vulnerable customers, in addition to those already covered by the cap. They also announced they would permit the use of default tariffs other than "evergreen" contracts. Following the Prime Minister's speech at the Conservative Party Conference in early October, the UK Government also published a draft bill on 12 October designed to give Ofgem powers to impose a cap on all default energy tariffs.

On 20 November, we announced a comprehensive package of actions and proposed measures to reform the UK energy market and benefit customers. We have announced seven unilateral steps we will take, including withdrawing the standard variable tariff (SVT) for new customers, and introducing new propositions and a new fixed-term default tariff. We will aim to move all of our SVT customers to other tariffs and to introduce engagement steps to minimise the number of customers ending up on a new default arrangement. We are also proposing a further seven recommended actions for Ofgem and the UK Government designed to improve the market further. These include the phase-out of the SVT and all "evergreen" contracts, a levelling of the playing field regarding supplier obligations, and the move of energy policy costs from energy bills to a less regressive method such as general taxation. We believe our package of proposals will increase customer engagement and choice, give people better deals and make the market fairer and more sustainable. We believe they will be significantly more effective than further Government intervention through temporary price controls.

As the UK's largest energy supplier, we will continue to work constructively with the Government, Ofgem and the industry to ensure we have an energy market that works for everyone. Whichever final path is chosen to improve the energy market for UK customers, we believe we can deliver a sustainable and attractive business in UK energy supply and will update on our progress at our 2017 Preliminary Results in February 2018.

Centrica will be hosting a conference call for institutional investors and analysts at 08:00 GMT on 23 November 2017 to cover the Trading Update and Centrica's proposals for the UK energy market. Please dial in using the following number:

+44 (0) 20 3059 8125

The call title is "Centrica investor and analyst call". A full transcript of the call will be available on www.centrica.com from Monday 27 November 2017.

Centrica is due to release its 2017 Preliminary Results on 22 February 2018.

Enquiries

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