

12 May 2008

# Centrica Interim Management Statement

## Period Review

To date the year has been dominated by high wholesale gas and power prices in the UK driven by record oil prices, rising demand in Asia for the available Liquefied Natural Gas and a lack of imports from continental Europe. On average the month-ahead prices for gas and power were 92% and 100% respectively above those for the same period of the previous year. Against this backdrop all major energy suppliers increased residential energy tariffs during the first quarter of the year. Following our retail price increase in January the wholesale gas price continued to rise, which has caused profit margins in British Gas in the first half of the year to be squeezed to levels below our long run expectations. The quality of our customer service has continued to improve. Complaints to Energywatch fell by 78% from the same period in 2007 and our call answering time has improved by over 60%. However, sales of energy accounts have slowed following the price rise which meant that British Gas ended April with 15.9 million customer accounts on supply.

In Centrica Energy the gas production business has been particularly strong in the year to date with both production volumes and selling prices well ahead of the previous year. This performance was driven by the higher wholesale gas prices, strong reliability at Morecambe Bay and the successful integration of the North Sea assets acquired from Newfield and Sojitz. However the high wholesale gas costs have further impacted the legacy industrial and commercial gas sales contracts. Losses here are currently expected to be materially higher than previous guidance.

Performance across the remainder of the Group has been good. British Gas Business has continued to perform strongly with further growth in its customer base and with its contract book providing substantial protection in the period against rising wholesale prices. British Gas Services has experienced a strong period with the financial results ahead of 2007 coupled with continued good operational performance. In North America during the period we completed two gas acquisition deals and agreed the \$300 million acquisition of Strategic Energy which will double the size of our commercial energy sales business. While the economic downturn in the United States is having an impact, particularly in the Services business, overall performance in the period has been reasonably robust. In the year to date Centrica Storage has benefited from high withdrawal reliability, which ran at over 99%. Profitability in the period has been lower than the prior year due to lower Standard Bundled Unit (SBU) prices. In March we completed the sale of all SBUs for the 2008/2009 storage year at an average price of 38.82 pence, reflecting the narrowing of the summer/winter gas price differentials. The Group net interest charge continued to benefit from the credit for the expected return on the pension scheme assets.

## Outlook

As expected, overall Group operating profit for the first half of the year will be materially lower than the first half of 2007. This is due primarily to the lower profitability in British Gas Residential, which experienced exceptional conditions in the early part of last year.

Looking to the full year, forward wholesale gas and power prices in the UK remain stubbornly high. The wholesale gas price for the second half of this year is double that experienced during the second half of 2007 and for the fourth quarter of this year it is over 80 pence per therm, compared to 44 pence for the same period last year. At current forward wholesale gas prices operating profit in the upstream gas production business will be very strong, although this will be partially offset by the additional losses in the industrial and commercial gas sales contracts. This shift in profit mix will increase the Group effective tax rate, which is currently forecast to be around 55%. While the current outlook for gas prices does create a challenging environment for energy suppliers, we will take the necessary action to deliver reasonable margins in the retail business.

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