

AGM Presentation

Presentation transcript

Roger Carr - Chairman

Good afternoon Ladies and Gentlemen.

It is now 2 o'clock and it gives me great pleasure to welcome you to the twelfth annual general meeting of Centrica plc. I am delighted to welcome so many shareholders here today and we appreciate your interest in the Company and the support that you continue to give us.

One small reminder – please don't forget to switch off your mobile phones.

I am accompanied today by my colleagues on the Board, all of whom will be familiar to you. The seating plan is outlined in the information note you received at registration and our biographies can be found on pages 34 and 35 of the annual report and on pages 20 and 21 of the annual review.

Next, a word or two on procedure. In a moment I shall say a few words on your Company's results and update you on our performance so far in 2008 as Chairman and then Sam Laidlaw will talk about our strategic priorities. After that, we shall move to the formal business, and I shall invite you to put any questions you may have, either on our results or on any other matter relevant to the Company's affairs.

We will then move to the formal business of voting on the resolutions. This year I shall be calling a poll on all resolutions. As you know I have previously expressed a belief in a show of hands but technology and best practice marches on. So, in seeking the best of both worlds the display on the screen will show separately the total votes cast and those cast in the room today. I think this is a good compromise and will enable us to include the votes of those shareholders who were unable to attend this meeting as well as those of you here today.

I will explain the process of voting shortly before we consider each of the resolutions.

All the members of the Board will be joining you for tea and coffee after the meeting and we look forward to talking to you on a more informal basis at that time.

I'd like first to turn to Centrica's performance over the past year. I am pleased to report that your company delivered very strong financial results during 2007, despite an extremely challenging year for us and for the industry generally.

It was a year of exceptional volatility in UK and international gas and power prices. This country's energy markets are now subject to a whole variety of influences across the globe, not least oil prices, but also rising demand for gas from regions such as Asia and the Far East. This year more than a third of the UK's gas will be imported, as we have already consumed much of the available resource from this country's national gas reserves.

These factors, coupled with extremes in weather patterns following the mildest winter on record in 2006-2007, combined to create large swings in wholesale gas prices last year. They sank as low as 13 pence per therm early in 2007, but by the end of the year they had risen by 47 pence, or 260 per cent, to as high as 60 pence.

To manage a business as complex as Centrica in such an environment requires no little skill.

I am pleased to report that our management were up to the task and would thank them and all the Centrica team for their hard work and achievements in challenging times. We restored British Gas to a viable level of profit margin across the year as a whole and also reversed the decline in the size of our customer base. This was achieved through a combination of much more competitive consumer pricing, more innovative product offerings, improvements in customer service and the continued removal of excess costs.

It is crucial that viable margins are achieved within British Gas given the scale of upstream investments we need to make in gas and power assets to supply our customers both in the UK and internationally.

That is why, we had to increase our tariffs in January, after the large increases in wholesale prices squeezed British Gas margins to just one per cent in the second half of 2007.

In this context, we are very mindful that in an era of high energy price volatility, there are many customers who also have difficulty paying their bills. This issue has been compounded by sharp parallel rises in the price of food and other household necessities. As many consumer bodies and commentators have recognised, British Gas has taken a strong leadership position in targeting assistance at those customers in fuel poverty who most need help, and we will continue to do so.

Upstream, we are making progress in terms of increasing the proportion of our gas and power requirements which are sourced from our own assets. This is important to provide a greater financial hedge to protect earnings against volatile wholesale markets. Last year, for example, there was the acquisition in September of the Newfield gas assets in the North Sea for £242 million. And our Langage power station in Devon will be operational by the first quarter of next year.

However, we still need to do more, and Sam and his team are continuing to hold discussions on a variety of fronts, both UK and internationally, in order to achieve that.

While on that subject, I would like to pay tribute to those colleagues who spend more and more time developing sources of gas in some of the less stable regions of the world. To those, and to others who continue to work in demanding conditions on gas platforms, building offshore wind farms and in other locations, I would like to pass on our gratitude.

At board level, Sam has built a strong team which has been working in a very focused way to grow this business and deliver on our strategy. Nick Luff has been with us for over a year now, while Phil has injected a real sense of change and urgency at British Gas.

There is one notable change taking place at board level with the retirement, announced in March, of Jake Ulrich. Jake is therefore resigning from the board with effect from today and will leave Centrica at the end of July after 11 years of invaluable service. We are sorry to see him go. Jake has been the lynchpin of the push to create and build an upstream business for the group. It is a vital role, focused around sourcing, producing and trading the gas and power required for our UK and international customers. Replacing Jake as managing director for Centrica Energy and Europe will be Mark Hanafin, who joins us in July from his current role at Shell. Mark will also have a seat on the board, and we wish him all the best in his new position.

In a moment I will hand over to Sam, who will explain the key performance measures for our last financial year, and also update you on progress with regard to delivering our strategy to build value for you our shareholders.

I thank you for your loyalty and support, and will now hand over to Sam.

Sam Laidlaw - Chief Executive

Thank you Roger and good afternoon ladies and gentlemen.

I am pleased to join you this afternoon for the Centrica AGM, which comes at a challenging time for the industry as well as for your company. We've had a year of good progress and the operational performance of the business has improved significantly. But as Roger has said, it must be remembered that we are now operating in a truly global energy market and the impact of international commodity prices as well as the consequences of climate change are having a big impact on all of us.

Our strategic focus remains to develop our businesses, producing, procuring, storing, trading and supplying energy and providing energy-related services.

The key to delivery of these objectives lie in our four strategic priorities, which remain unchanged. They are to transform British Gas, to sharpen up the organisation and reduce our costs, to reduce risk through increased integration, and to build on our growth platforms.

And as most of you will realise, this work is taking place against the backdrop of a rapidly changing international energy market.

We have seen very sharp increases in wholesale gas and power prices over recent months. Indeed, UK forward gas prices for next winter are now at 85 pence per therm, up by 77% compared with the winter just ended – and these are the highest prices we've ever seen in the run up to a winter period. Meanwhile power prices are now £76 per megawatt hour for next winter, up 50% from last winter.

So why is this happening?

There are clear structural reasons for this which unfortunately won't go away. We need to recognise that in contrast to four or five years ago, the UK is now part of a truly global gas market – production from the North Sea is dwindling rapidly and we are no longer an energy island. Last year around 27 per cent of the gas the UK required was imported, and this will increase steadily to around 75 per cent by 2015.

This increased need to import gas means UK wholesale gas and power prices are now subject to a cocktail of pressures and influences from all corners of the globe. Global oil prices remain at record highs, over \$125 a barrel, and given the strong linkage between gas and oil prices, particularly on the Continent, this has taken gas prices up with it.

In the Far East, demand for liquefied natural gas continues to grow from Japan, South Korea and increasingly, China. The result is that many Liquefied Natural Gas tankers which might otherwise have come to the UK or Europe have been diverted to Asia.

Simply stated, to bring gas to the UK we now have to pay the world price rather than the price to clear the marginal cost in the North Sea.

Meanwhile, power prices have also risen sharply, driven by record gas and coal prices – remember these two fuels between them account for over 75% of UK power generation.

Looking forward, power costs will also inevitably be driven up by the increasing need to reduce carbon emissions and the price put on those emissions. We will need very extensive new investment in cleaner forms of generation if demanding European and UK government targets on emissions reductions and renewable energy generation are to be met.

The impact of this rapidly changing energy marketplace was seen to some degree in our financial performance for 2007. At group level for the year as a whole, we turned in a very strong performance, and although revenue was slightly down, we saw operating profit up 40% and earnings up 60%. Across Centrica as a whole, operating profit was £1.94 billion, up from £1.4 billion in 2006.

It was, however, a year which was characterised by two very distinct halves because of the dramatic volatility that we saw in the wholesale gas and power markets. Market prices fell very sharply at the beginning of 2007 and then rose equally sharply in the final few months.

The consequences of this were particularly marked within British Gas Residential, which made strong margins in the first half after wholesale prices fell. This enabled us to cut customer prices twice last Spring, by a total of 20%. But from then onwards, the rise in market prices reduced British Gas's margins and by the end of the year we were in negative territory, forcing a tariff increase in January of 15%.

In this context, it was crucial that we continued to remove costs from British Gas Residential - £139 million in total last year, or some 15 per cent of the cost base. We're now on track to remove a further £60 million of costs in 2008.

We also improved our service levels – customer complaints to Energywatch fell by 78% from the same period in 2007 and our call answering time improved by over 60%.

British Gas operates in a very tough market, but a key factor in our recovery has been our competitive pricing – our gas is currently the second cheapest for those paying by direct debit and on dual fuel we also remain very competitive.

The result of these pricing and service improvements was that by the end of 2007 we had regained a quarter of a million customers from a trough last spring, leaving our numbers flat year on year.

We also continue to work hard to help those who do have difficulty paying their bills, and as independent commentators have acknowledged, we are contributing almost £70 out of every £100 nationally which goes to help those in fuel poverty – that is more than double our market share. We intend to continue to take a leading position in tackling fuel poverty.

Overall British Gas is in a much stronger, more competitive position than in 2006 in terms of pricing, customer service, our cost base and therefore profitability; and as I mentioned, maintaining this progress is one of our four strategic priorities, along with continuing to reduce our costs across the group and to sharpen up the organisation.

Important as British Gas Residential is, however, it now accounts for less than a third of our overall group operating profit. In 2007 our other businesses also performed well.

In our Upstream business, Centrica Energy production of gas increased by 18% compared to 2006 and our power station output increased by over a third. The excellent group performance was also driven by record profits from our growth businesses, British Gas Services, British Gas Business and Direct Energy in North America, as well as Centrica Storage.

We need to maintain this strong financial performance across all our businesses given the billions of pounds of investment that are needed to secure new gas and power supplies in the UK. We are spending approximately £1 billion a year on new sources of gas and power and we need to continue to do that to secure our energy supplies. As I mentioned earlier, by 2015 around 75% of the UK's gas will be imported and around a quarter of the UK's power stations will be taken out of service under EU environmental rules.

Indeed, another of our strategic priorities is to acquire and build more upstream gas and power assets to increase the proportion of our customers' requirements which comes from our own resources, thus reducing our exposure to buying gas and power on volatile wholesale markets.

In gas, as Roger said, during 2007 we acquired the Newfield assets in the North Sea and we've made three further upstream acquisitions in 2008, one in the North Sea and two in North America.

We also continue to have talks with a wide range of potential partners overseas, including national oil companies in producing countries. We're making some progress here, but such deals typically involve 20 year contracts and do take time to negotiate.

In power, we're continuing to develop our power generation portfolio which will help hedge our gas requirements given the strong linkage between gas and power prices. This power generation will not just be in conventional gas-fired technology, but also in renewables and possibly new nuclear when that programme commences. These technologies cost some three or four times as much to build as gas fired generation, but have an important role to play if we're going to meet the carbon emissions reductions targets set for the UK.

In renewables, in order to meet demanding new EU targets, the Government has set an ambition to build some 33 gigawatts of offshore wind with more onshore wind taking the total to 40 gigawatts. To put this in perspective that's a tenfold increase on current UK renewables capacity.

Centrica has an important role to play here. We already have 180 megawatts of wind in production, and we are currently constructing another 180 megawatts at the Lynn and Inner Dowsing wind farm off the Lincolnshire coast. This is the world's largest offshore wind farm project so far. I am pleased to say first array of turbines started producing power 10 days ago. Overall, provided the economics hold up, we have plans to build a further 1.25 gigawatts of capacity over the next several years.

Finally, as the fourth strategic priority, we are looking to build on the excellent performances delivered by our growth businesses in 2007. There's plenty of scope to do this through organic growth, acquisitions and efficiency improvements, both in the UK and in our Direct Energy business in North America. In March we announced the acquisition of Strategic Energy, which is one of the biggest competitive electricity suppliers to the commercial and industrial market in the United States.

Of the other growth opportunities, we have two businesses in British Gas Services and British Gas New Energy which are uniquely positioned to supply a wide range of energy efficiency products and services, which are increasingly in demand. These will help all of our customers to manage their fuel bills and play their part in reducing global carbon emissions.

In conclusion, given the challenges facing us, and the trend of the commodity markets, together with higher effective tax rate, it is clear that we won't repeat this year the exceptional level of profitability we saw in 2007. However, due to the steps we are taking across the group our relative performance continues to improve. In addition, better performance from the Upstream business will partially compensate for the impact of higher prices on our British Gas residential business.

So I am fully confident that by staying focused on executing our chosen strategy we will continue to deliver value for shareholders and provide competitive, reliable low carbon energy for our customers. We are working hard to make sure this happens.

Thank you.

End of presentation