

AGM Presentation

11 May 2009

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 thirteenth 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 remember to switch off your mobile phones.

I am accompanied today by my colleagues on the Board, most of whom will be familiar to you. Our biographies can be found on pages 36 and 37 of the annual report and on pages 20 and 21 of the annual review.

I would like to welcome Mark Hanafin, Managing Director of Centrica Energy and Europe to his first Centrica AGM having joined the Board last July. And we must say farewell to Paul Walsh, my non-executive colleague - this is his last Centrica AGM as he is today standing down from the Board after six years' service. I would like to thank Paul personally, and on behalf of all of us, for the invaluable advice and guidance he has provided over this time. We are currently in the process of identifying a suitable replacement.

There are also a number of changes within the Executive team that I would like to outline.

In February, Phil Bentley, who previously managed the British Gas energy business, became Managing Director of British Gas – a single customer-facing retail operation which combines British Gas Residential, Business and Services.

I would like to take this opportunity to thank Deryk King, President and Chief Executive of Direct Energy, who has decided to retire. Deryk joined Centrica in 2000 and has built up Direct Energy from scratch into a business with a £6 billion turnover. Our thanks to Deryk for the outstanding contribution he has made and we wish him well for his retirement. Chris Weston, previously Managing Director of British Gas Services, will succeed Deryk King at the helm of our North American business Direct Energy in July. He takes on a large and well established business which has a clear strategy for future growth. In recognition of this, Chris will join the Centrica Board in July.

These changes build on the excellent progress Centrica has made under the leadership of Sam Laidlaw.

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 2009. Sam will then talk about our strategic priorities. After that, we will move to the formal business, and I will invite you to put any questions you may have.

We will then move to the formal business of voting on the resolutions. I shall be calling a poll on all resolutions, and once again we will be using electronic voting handsets which I hope you are now getting used to. The display on the screens will show separately the total votes cast and those cast in the room today. This allows 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. 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.

Before I report on Centrica's performance over the past year I would like to share with you an important announcement we made to the market this morning. We have reached an agreement with EDF to acquire a 20% stake in British Energy, the nuclear generator, together with the sale to EDF of our 51% stake in SPE. The

terms have been revised from those outlined in last year's Memorandum of Understanding between Centrica and EDF, reflecting the changed commodity price environment and the inclusion of SPE. The net consideration of £1.1 billion maintains Centrica's strong funding position in order to capitalise on other future strategic opportunities.

The transactions will deliver significant benefit to Centrica's shareholders, providing the company with both a short-term and long-term hedge against volatile commodity prices and a platform for our involvement in the construction of new nuclear generation capacity.

We will be holding a general meeting in June this year to seek your approval to proceed with this transaction. Sam will go into more detail on this shortly, but I believe it will both strengthen us as a business and provide a growth opportunity in the future.

Turning to Centrica's performance, I am pleased to report that your company delivered strong financial results during 2008, despite an extremely challenging year for us and for the industry generally. We witnessed previously unseen levels of volatility in wholesale energy prices, in the UK and internationally. Oil prices, against which gas prices are benchmarked in many other countries, rose to almost \$150 a barrel last summer before falling back rapidly to below \$50, as the recession impacted demand globally.

This rollercoaster ride was reflected in the wholesale cost of gas, which necessitated two retail price increases for our British Gas customers last year. In February this year, we were the first supplier to cut gas prices and, as I hope you saw in the press, we cut electricity prices last Thursday.

In last year's market environment, profitability at British Gas Residential was inevitably impacted, but nevertheless held up much better than during previous periods of volatility. This reflected the hard work already done to make that business more resilient. And I am pleased to say that British Gas has made a strong start this year.

While it is crucial that we maintain viable margins in our retail business, we are conscious that many of the most vulnerable in society have great difficulty in paying their bills. Our response has been to further extend the industry-leading level of assistance we provide. We increased the number of customers on our social tariff from 340,000 to 530,000, providing them with a typical saving of £202 across their gas and electricity bills over the past winter. And over the three years to 2011, British Gas' total spending on vulnerable customers through obligated and voluntary programmes is expected to have a value in excess of half a billion pounds.

In our upstream business, profits were also strong, and, once again, we saw excellent growth in revenue and operating profit in British Gas Business and British Gas Services.

Moving on to strategy, the volatility that has impacted wholesale energy markets over the past year underlines the importance of one of our key objectives, that of further increasing our vertical integration.

Apart from British Energy, we made further acquisitions of gas reserves in the North Sea and North America last year, and in March this year we took a 23.6 per cent stake in Venture Production, one of the larger gas producers in the North Sea. We are still considering our options in relation to Venture. I should mention that Sam and his management team are continuing discussions on a variety of other options, both in the UK and internationally, to explore further opportunities in gas and power.

Centrica is a complex business operating in a complex environment and our success is very much due to the skills and determination of the management team, and the hard work of many thousands of employees.

Many spend increasing amounts of time in demanding conditions such as developing offshore gas fields in the UK, Norway, operating gas wells in remote areas of Northern Alberta, building and maintaining offshore wind farms in the Wash, and working in Nigeria and other less stable regions.

In February, British Gas was recognised by the Sunday Times as one of the '20 Best Big Companies to Work For', which is a significant achievement. Indeed, I would like to thank all of Centrica's employees for the dedication, loyalty and professionalism which they continue to display.

Earlier today we released our first interim management statement for 2009 to the London Stock Exchange, which makes clear that the outlook for Group earnings for the full year is in line with market expectations. The

reduction in wholesale commodity prices in the UK has moved operating profit from the upstream to the downstream, with the lower overall Group operating profit offset by a lower effective tax rate. There is a link to the announcement on the Company's website and copies are available here today on request. I thank you for your loyalty and support.

I will now hand over to Sam, who will outline developments over the past year and update you on progress with regard to delivering our strategy to build value for you our shareholders.

Sam Laidlaw - Chief Executive

Thank you Roger and good afternoon ladies and gentlemen.

Thank you for joining us at this AGM which comes after the most volatile year we have ever witnessed in international energy markets. We are not immune from the impact of this, but you will be pleased to know that the performance of the business has been good, and we delivered strong operational and financial results in 2008.

We have made good progress against all the strategic priorities I set out last year. I'll talk about these in more detail later but of particular significance was the agreement we signed with EDF to acquire a 20% share in British Energy. We are very pleased to have finalised this agreement, which secures our participation in the UK's nuclear industry going forward. There is a strong short and long term strategic case for doing this. In the short term it gives us 20% of the electricity from British Energy's nuclear fleet. This means that the proportion of our total energy requirements covered by our own generation and production will increase from around 35% now to about 45%. For electricity alone 85% of our power needs will now come from our own generation compared to 58% today. For the longer term, this transaction will also give the opportunity to participate with a 20% interest in four new nuclear power stations that are planned to be built by EDF. This is a very important step forward for your business. It gives us access to a long life, low carbon source of power which is not exposed to volatile wholesale gas prices.

Stepping back, the Energy industry is facing three sizeable challenges - climate change, security of supply and providing customers with affordable energy. In climate change the UK has two tough targets - firstly to source 15% of all UK energy from renewables by 2020, and then to reduce UK greenhouse gas emissions by 80% by 2050.

For the energy sector, which accounts for some 40% of carbon dioxide emissions, the changes required to meet these targets are revolutionary.

Around a quarter of the UK's highest emitting coal-fired power stations will be closed by 2015, creating an opportunity to decarbonise the sector by building clean replacements.

Wind will potentially form a big part of this - indeed the Government estimates that we could see 35% of electricity coming from renewables by 2020, against around only 4.5% now. Progress here depends on investors being able to get an adequate return, and we were encouraged by the Government's announcement in the Budget that they are adjusting the Renewable Obligation for offshore wind.

We will also see the renaissance of another crucially important form of low carbon generation - new nuclear construction. As I have said, Centrica plans to invest in this through British Energy where plans are in place to build four new nuclear reactors.

Achieving these targets will be expensive. The Government has already put a £100 billion price tag on the delivery of its 2020 renewables target alone, and Ernst & Young research suggests that for the energy sector overall, £230 billion will need to be invested by 2025.

Centrica is playing a leading part in delivering the required investment to meet the country's security of supply challenges. We expect to invest at least £15 billion by 2020 - including nuclear, renewables, gas production and gas storage. This, coupled with rising demand for energy efficiency products among our customers, will lead to the creation of around 1,500 new skilled, green-collar jobs in the next year or so.

Despite the cost, longer term these changes should help insulate both investors and customers from volatile global prices for gas and coal and oil, and we will all welcome that.

Which brings me on to our performance in 2008. Overall, we delivered an operating profit in line with expectations, broadly flat at £1.94 billion. However, a significant portion of this, stemming from gas production, was subject to very high tax rates of up to 75%, and as a result, our group overall tax rate exceeded 52% and post-tax earnings per share were impacted, down 20% at 21.5p per share. As commodity prices have come down this year so will our effective tax rate for 2009. Our operating performance continues to improve with better service levels in our downstream operations, better reliability in our power stations and gas fields and a continued strong focus on health and safety.

Good progress was made against our four strategic priorities – to transform British Gas, to sharpen the organisation and reduce costs, to become more integrated by developing and acquiring more gas and power assets and to build on our growth businesses.

I would now like to tell you a little more about how we are moving forward with each priority.

In British Gas, we have already fundamentally changed the performance of the business since 2006. Customer service has improved significantly, particularly call handling and billing, and this has paid off by helping to keep our customer numbers relatively stable.

At the same time, we have kept a tight rein on operating costs, which are down by around £200 million in this business since 2006. This helps us to be much more competitive in the market place and we announced last week a 10% cut in electricity prices, following on from a 10% cut in gas prices in February. This means we have cut gas and power prices by more than anyone else this year, making us the cheapest standard electricity supplier across all regions and payment methods. We are also the cheapest supplier for standard dual fuel customers paying by direct debit, averaged across all regions. Our online tariff, WebSaver, continues to be the cheapest dual fuel offering for those on average consumption. Overall, British Gas is offering great value to our customers. We are beating the competition and now serve over 2 million customer accounts on line. As Roger said earlier, Centrica will continue to play a leadership role in helping vulnerable customers but as the costs rise, there will need to be a more sophisticated fuel poverty strategy that is better targeted at the most vulnerable customers.

In the next phase of British Gas's development, we are now joining up under the leadership of Phil Bentley British Gas Residential, British Gas Services and British Gas Business operations to maximise the opportunities that a single brand and business present.

What is the rationale for this change? Today British Gas serves around 12 million households who hold 24 million products. But of the 12 million homes, only 1.9 million hold both an energy and a services product. Increasing this proportion represents a huge opportunity for us, because customers holding both types of product are not only more likely to stay with us, but the lifetime value of such a customer can also be more than double that of the customer holding a single product only.

We believe that aligning services even more closely to energy will give us the opportunity over time to reduce the cost base by a further £100 million. It will also allow us to position ourselves for a low carbon future and to better target customers with energy efficiency advice and products such as insulation, solar photo voltaic panels and heat pumps as well as enabling the roll out of smart meters in customers' homes.

On our second priority, to sharpen the organisation and reduce costs, in 2008 we continued to make headway. We reduced our Group like-for-like costs by some £40 million, and that's in addition to the £70 million we took out of British Gas. We will continue to focus relentlessly on costs in future.

Our third priority is to reduce risk through increased integration of further gas and power assets. Here, over the last two years, we have acquired additional gas and oil assets with potential reserves of around 800 billion cubic feet equivalent – that accounts for over half of our current UK gas reserves. Overall, we have invested around £1 billion in these acquisitions and developing our North Sea assets. In addition as you will have seen, consistent with this strategy we acquired a 24% interest in an independent North Sea gas producer in March and continue to examine further potential upstream gas opportunities.

In liquefied natural gas, to enhance our diversity of supply we have already brought in 6 LNG cargoes through our import capacity at the Isle of Grain since it was commissioned last November, and we have another 10 contracted for this year and next. We're also continuing to hold active discussions with a variety of National Oil Companies about longer term contracts.

Gas storage also provides a useful hedge against seasonal volatility in prices, and as you may have noticed, we've announced three new storage projects in the past year or so to complement the existing Rough facility. Together these will represent investments of over £1.5 billion.

In Power, clearly the most significant development has been our agreement with EDF to acquire 20% of British Energy for which we raised the proceeds through our Rights Issue last year. As we announced this morning, the terms of the transaction have significantly improved since last year and our investment in a 20% interest together with the sale of our Belgian business will incur a net cash outlay of £1.1 billion rather than £3.1 billion for a 25% interest. I would like to thank all our shareholders who participated in the rights issue as this enables us to move forward and greatly strengthen our business model. We will now have a long life, low carbon source of power which will benefit both our shareholders and our customers, as well as a new platform for growth with new nuclear construction. This is a big step forward for our business.

We will also continue to develop our gas fired power generation fleet and are expecting to fully commission our Langage gas-fired power station in Devon towards the end of the year. In Renewables, our Lynn and Inner Dowsing windfarm is now fully operational and is currently the world's biggest offshore windfarm development. When all these projects are completed, we will generate 85% of the electricity our retail customers require from our own generation fleet.

It is worth mentioning here that Centrica's carbon intensity, which measures the amount of carbon dioxide emitted per kilowatt hour of electricity supplied, is already the lowest of the big six UK energy suppliers – but will fall further still once the stake in British Energy is included.

Finally, as the fourth strategic priority, we have firm plans to ensure our growth businesses continue to perform strongly. British Gas Business, British Gas Services and Direct Energy all grew both revenue and customers, and drove down their costs as a percentage of gross profit margin. The result is that overall we have increased profitability by 50% over two years to a combined £560 million of earnings in these businesses

In North America, we intend to significantly increase integration at Direct Energy taking advantage of current market conditions to add further power and gas assets, and blocks of customers in our target markets.

In Europe, the pace of deregulation, unbundling and liberalisation has been disappointing and returns on invested capital have been low which is why we have taken the decision as part of the British Energy transaction to withdraw from the Belgian marketplace at an attractive price.

In conclusion, we have taken significant strides forward in the past three years to make our businesses more efficient and robust so that it is capable of withstanding shocks from the volatile energy markets.

I believe there is much further to go to unleash the potential of this business. We in the management team are working hard to ensure that we meet the challenges I described and exceed the expectations of you, our investors. We will remain focused on our strategy and the task in hand to continue to deliver value for shareholders.

Thank you.

End of presentation