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Centrica plc 2019 Half-Year Results and Strategic Update Presentation
9.00 am - Tuesday 30 July 2019

Iain Conn, Group Chief Executive
Well good morning ladies and gentlemen and welcome to Centrica's Interim Results Presentation and summary of our Strategic Update which the Board has been conducting over the last six months. But first a word on safety.

[Safety announcement]

Before I continue with the rest of the Presentation, let me comment on the other announcement today that I will step down and retire from the Board next year.

Since 2015 we have been repositioning Centrica towards the customer and from a company ill-equipped to deal with the major changes in the energy landscape to one capable of being in tune with it and the transition to a lower carbon world. The announcements we are making today including exiting oil and gas production and becoming an Energy Services and Solutions company, once materially underway or completed, form the right point for me to hand over to a successor.

I am proud of the efforts of the Centrica team so far. We have made good progress in materially reducing costs and debt while re-equipping ourselves for the future. The Ford deal announced today is an example of that.

The divestments we are announcing or are already underway, mean that the Centrica which I inherited will have changed utterly. It has not been an easy journey, but we are now in a position to begin to restore shareholder value.

I remain fully committed to leading this great company and I am looking forward to executing these next steps and with the Chairman, Charles Berry who is here this morning, to ensure an orderly transition to someone with the skills for the next phase in due course. I also hope, as I said on the radio this morning, that the political backdrop in the UK under this new Conservative Government may be more effective in formulating constructive and progressive pro-market energy policy as we aim to tackle the combined challenges of UK competitiveness and climate change.

In the first part of the Presentation today I will summarise both our current situation and the conclusions of our Strategic Update. This includes the key conclusion that we will become an Energy Services and Solutions Company in tune with the transition to a lower carbon future, exiting Exploration and Production as well as Nuclear, completing the journey back towards the customer which we began in 2015.

Chris will then provide a detailed review of our current performance, first half results and outlook. I will then come back to provide some more detail on key aspects of our strategy going forward and updates on specific businesses.

Let me start with a summary of what we are announcing today.

Firstly, on performance. It is very clear that the circumstances in the first half of 2019 have been extremely challenging. We have had the implementation of the UK default tariff cap including a one-off impact of an additional £70 million which we are challenging in the courts, extremely low UK natural gas prices, outages at two nuclear sites whose restart awaits regulatory inspections and approvals and warmer than normal weather on both sides of the Atlantic.

This is not a positive set of circumstances for Centrica's portfolio today. As a result, despite the hard work of colleagues across the Group, our financial performance in the first half of 2019 was weak. However, there are fundamental drivers of momentum into the second half of 2019 and indeed from there into 2020.

A key indicator of our performance is the number of consumer account relationships we have. I am very aware the loss of customer accounts in the face of intensifying competition has been a major worry for our shareholders and indeed for our colleagues within Centrica. In response to competitive pressures over the last few years we have been driving cost efficiency hard to ensure it is less easy for others to take our customers on price alone and especially when our strong brand is taken into account.

We have also been developing new propositions including the bundling of Energy Services and Solutions. I am pleased to report that through our improved cost base and the efforts of the Centrica team, we have had net consumer account growth in the first half of 2019 for the first time since I have been Chief Executive. We also continue to expect to meet the 2019 Group targets we outlined in February.

Turning to strategy, we have concluded that Centrica has built sufficient capability in the customer-facing businesses for us to now complete the shift towards the customer which we began in 2015 with the decision to exit both Exploration and Production and Nuclear.

Centrica will become an Energy Services and Solutions company. We will focus on our distinctive strengths centred around energy and with a major emphasis on helping our customers' transition to a lower carbon future. The challenge of climate change is affecting all of us, and the energy system must adapt. Centrica is ideally positioned to respond to this challenge with a focus on the demand side of the equation. Centrica has moved from being ill-equipped to deal with the rapid changes in the energy system to being well-positioned for the transition to a lower carbon future.

However, turning to the dividend and our balance sheet, our current circumstances and this shift towards a more pure-play customer facing company will require a change to our capital structure and to our dividend. I deeply regret that we have decided to rebase the dividend for full year 2019 to a cash dividend level of 5 pence per share. As part of this rebasing we will cancel the scrip alternative from the 2019 interim dividend which will be paid in November.

This reduction in the near term annual cash dividend roughly equates to the impacts of our changed circumstances and the reduction in cash flows as a result of the impact of the UK price cap plus the increased pension contributions we will need to make as part of our triennial review which has just concluded.

However, our near-term cash flows were not the only consideration. We have also paid attention to two other factors - the strength of the balance sheet and likely requirement for strong investment grade credit ratings for the future customer-facing company. And the cash restructuring charges we will incur as we complete the transition to becoming a highly competitive, future-facing Energy Services and Solutions company.

I must repeat that I know how material such a rebasing of the dividend is for our shareholders - it represents roughly a halving of the cash dividend and I regret that our current circumstances and the need to complete the competitive repositioning of the company require this intervention. However, I am sure that this is in the long-term interests of all our stakeholders as we respond to the current circumstances and position Centrica to be able to leverage its distinctive skills and capabilities for the benefit of our customers, colleagues within the company, and our shareholders going forward.

There are a number of additional headlines from our Strategic Update which we have conducted over the last five months.

Centrica will continue to focus on the areas of Energy Services and Solutions in which we have distinctive capabilities - namely in energy supply and its optimisation, and in services and solutions centred around energy. Within this there is a growing opportunity in Home Energy Management and the interface with electric vehicles. As evidence of this I am very pleased we have announced today an exclusive deal with Ford for the UK and Ireland relating to electric vehicle charging, EV tariffs and after-market services. We will reposition three key business units, UK Home, Connected Home and North America Business. I will come on to some detail behind these in a moment.

The decision to exit E&P and completely focus on the customer-facing businesses will unlock and accelerate a further £250 million per annum of efficiency delivery. We are targeting being the most competitive provider, consistent with our brands and propositions, which will prevent loss of customers and therefore stabilisation and subsequent growth in both customers and margins per customer.

Financially, dividend policy will be progressive from the rebased level of 5 pence per share, linked to both earnings and cash flow growth and with a targeted range of cover from earnings of 1.5 to 2 times. The rebased dividend will allow organic sources and uses of cash flows before restructuring to be more than balanced. Over 2019 to 2021 in particular, there will be material further opportunity to reduce costs, but with significant restructuring charges.

Divestment proceeds from the sales of Nuclear and Spirit Energy will be first used to fund the restructuring and reduce net debt levels of what will be a pure-play, but less diversified, customer-facing company.

Finally, beyond the period of significant restructuring to the end of 2021 we would expect material growth in net cash flow. Chris will provide further detail on this later.

Now moving onto the current environment and its impact on the first half results. I have already referred to a number of the factors that heavily impacted the first half of 2019. As a result, we reported weak adjusted operating profit, down 49% to £399 million, and adjusted EPS was down 63% to 2.4 pence. Cash flow remained relatively robust. Adjusted EBITDA was down 19% to £1.075 billion and adjusted operating cash flow was down 32% to £744 million.

However, as I have already mentioned. consumer accounts grew. I will provide more detail on this shortly. With the outlook more positive for the second half of the year we continue to expect to meet our full year Group targets with adjusted operating cash flow in the lower half of the £1.8 to 2 billion range and net debt within the £3 to 3.5 billion range.

Moving on now to cover Consumer accounts in a little more detail. I have already mentioned that they grew in the first half of the year by 314,000 in total. We saw growth in energy and services accounts in North America and Ireland. In the UK, total energy and services accounts were down by 38,000 - that excludes Connected Home. Within this, energy accounts were down by 178,000 which includes the impact of a spike in customer churn in March and April, around the time of the significant increase in the default tariff cap. This includes the reduction of 274,000 collective switch and white label accounts while we gained accounts on our British Gas branded tariffs. Notably, overall energy accounts have grown in May and in June.

Services accounts grew by 140,000 and accounts in the UK were up by 124,000 overall when including Connected Home growth. Although this is only one half year, it is encouraging to be able to report account growth for the first time in a number of years.

If we look now at UK Home energy accounts over the last five years, clearly we have moved from 14.7 million accounts to the current position of 12 million. During this period accounts were relatively static in 2014 and 2015 and through the CMA investigation into the UK energy market which ended in June 2016.

However, the increasing number of market participants, some pricing below zero gross margin and taking advantage of the policy-led cost advantages for small suppliers and our own stance in 2016 to focus on margin quality of customers rather than quantity resulted in a step down of about 2 million accounts over 2017 and into the first half of 2018. Since that time, as we have become more cost-competitive and improved both service and customer journeys, we are seeing the decline slow markedly. And this year we have the UK default tariff cap in place.

I promised in February to give an update on dynamics under the cap. This slide shows for both pre-payment and dual fuel SVT customers, the dispersion of market prices before the cap, immediately after the cap, and most recently. What you can see in both cases is that dispersion was reduced significantly on introduction of the cap, and prices bunched underneath it.

An interesting dynamic has developed with the regulated price cap levels increasing in 2019 as a result of lagging formula input costs just as the spot price of wholesale energy has been falling. This has allowed significant dispersion of prices once again in the first half of 2019.

There are three critical takeaways from this. Firstly, despite the expansion of price dispersion, Centrica's energy accounts have only fallen by 178,000 compared to 341,000 in the same period last year or roughly half the rate.

Secondly, within that our ability to discount energy and bundle with services propositions and Connected Home propositions has actually resulted in net account growth despite the increased price dispersion.

Finally, it is likely that the next period of the price cap will be lower by about £80 per dual fuel customer and forward curves suggest wholesale costs will rise. This will compress differentials and put pressure on low cost suppliers who do not hedge. If Centrica has slowed account losses in energy even with the expanded dispersion, the next period should be better and the bundling of energy and services should enable continued account stabilisation and net growth.

I am encouraged by our ability to compete under the new price cap situation although this dynamic between a lagging, static cap and volatile spot wholesale prices will require careful risk management. Let me now turn to earnings momentum.

Touching now upon outlook for the second half of the year and also looking ahead to 2020 there are a number of factors that give us confidence that earnings for the second half of the year will improve compared to the first half. The £70 million one-off impact of the price cap will not be repeated mitigating the normally lower energy profit in the second half relative to the first half. The four reactors offline at the Hunterston B and Dungeness B nuclear power stations are currently due back online between August and October meaning that Nuclear volumes should improve.

As you will hear from Chris shortly, North America Business margin under contract is second half weighted which should result in a much-improved profit in the second half. And cost efficiency delivery is expected to accelerate in the second half of the year including structural changes to cost of goods sold in UK Home services. These factors should also provide benefit into 2020.

In addition, we are seeing gross margin momentum in a number of our customer-facing businesses including reduced cost of goods in UK Home services. We also expect reduced capacity charges in North America Business, reduced losses in Connected Home in part reflecting us refocusing the business on the UK, and improvements in Distributed Energy and Power as gross margin momentum continues.

Now let me return to provide more detail on the key conclusions from the Strategic Update. As already mentioned, we will exit hydrocarbon production creating a leading international Energy Services and Solutions company. We will continue to serve Consumers and Business customers with our geographic focus remaining on the UK, Ireland, North America and Continental Europe.

We will focus our activities around our distinctive strengths. In Centrica Consumer we will focus on the strategic pillars of energy supply, in-home servicing, and home solutions. In Centrica Business we will focus on the strategic pillars of energy supply, energy optimisation, and business services and solutions.

In terms of the timing of completing our portfolio shift, we expect to exit Spirit Energy and Nuclear by the end of 2020 with the exit from Spirit Energy expected to come via a trade sale.

We have already made some specific decisions relating to a number of our business units. I will cover all of these in more detail later in the presentation. However, in summary we will fundamentally rebase UK Home, driving structural changes in customer journeys, internal processes and the cost base; Connected Home will be refocused on the UK and Ireland and around Home Energy Management and will be renamed Centrica Home Solutions; we are making structural interventions in North

America Business to improve returns and lower the volatility of those returns; and we will continue to invest for growth in Distributed Energy and Power with the business renamed Centrica Business Solutions in line with how we go to market today.

Our shift to becoming a wholly customer-facing company will also enable material simplification and greater focus. This will enable us to unlock and accelerate significant further cost efficiency. The 1 billion pounds of savings we have made since 2015 mean that we are now on average placed competitively from a cost perspective.

The next phase of our efficiency programme is designed to position us as the lowest cost provider in all our markets, consistent with our brand positioning and propositions. This will enable delivery of a further 1 billion pounds of efficiencies per annum from 2019 to 2022, which is an increase of £250 million versus the previous target of £750 million we announced in February.

I appreciate this will impact many of our colleagues and I regret that hugely, but it is necessary for us to become fully market-leading and so prevent others taking our customers, certainly on price alone. Delivering this level of efficiency and cost base will require material restructuring charges, most of which will fall over the period 2019 to 2021.

Finally, before handing over to Chris, let me now return to our conclusions on dividend and capital structure.

As I covered at the start of the presentation, we are seeing increased pressure on our cash flows and dividends in the near term. These include our changed circumstances, including the impact of the UK energy supply default tariff cap and higher pension contribution requirements following the conclusion of our triennial review. We are also facing a higher level of cash restructuring costs with very good returns as we drive efficiency and competitiveness. As a wholly customer-facing company we will also require lower levels of net debt to meet likely higher credit rating agency thresholds.

It is these factors which have regrettably resulted in us having to rebase the dividend to 5 pence per share for full year 2019. We will also cancel the dilutive scrip alternative. We will target a progressive dividend from this rebased level linked to growth in earnings and cash flow and dividend cover from earnings of 1.5 to 2 times as I said earlier.

We will continue to target strong investment grade credit ratings to support our commodity hedging risk management activity.

Finally, we will maintain our focus on capital discipline with annual capital investment post the Spirit Energy and Nuclear disposals expected to be around £500 million.

Chris will cover some of these areas in more detail in his section. I will be back in about 25 minutes to cover the key aspects of the strategy going forward and the details of our conclusions regarding specific businesses.

Chris.

Chris O'Shea, Group Chief Financial Officer

Thanks Iain. Good morning everyone.

As usual I will start with the first half results.

Revenue was down 2% to £13.8 billion reflecting lower revenue in North America Business due to fewer optimisation opportunities and the impact of the introduction of the UK default tariff price cap, partially offset by growth in North America Home where we saw strong performance in our Airtron services business and higher energy revenue.

Adjusted operating profit fell by £383 million, with almost half of this reduction due to the impact of the UK price cap. Adjusted earnings fell by 63% to £134 million, reflecting lower profits and the impact of an increase in the Group's effective tax rate in the first half to 47% due to a higher proportion of the profits coming from the more highly taxed E&P segment, partially offset by lower interest charges following the 2018 liability management programme.

As a result, adjusted basic earnings per share reduced from 6.4 pence to 2.4 pence.

The Board has declared an interim dividend per share of 1.5 pence, 30% of the expected full year dividend.

EBITDA fell by 19%, while adjusted operating cash flow reduced 32% to £744 million. However, with operating cash flow expected to be more second half weighted this year, we remain on track to deliver adjusted operating cash flow of between £1.8 to £2 billion for the full year.

Group net investment was 70% lower at £139 million, reflecting the proceeds from a non-core asset disposal programme and a continued focus on capital discipline.

Net debt of £3.4 billion was relatively flat year-on-year after adjusting for the non-cash impact of IFRS 16. With cash flows expected to be more second half weighted, we expect to remain within our £3 to 3.5 billion targeted net debt range for the full year.

Finally, we recognise the statutory basic loss per share of 9.6 pence for the first half after taking into account exceptional items and certain accounting re-measurements and I would like to take some time to cover this before moving on to our divisional performance.

As you know, we separately identify exceptional items and certain re-measurements in the face of the income statement as we feel this makes our results easier to understand. These items fall into three main categories as follows:

Firstly, we separately identify costs associated with major restructuring programmes. In the period these programmes, including the cost of changing UK pension arrangements, amounted to £321 million pre-tax, or £257 million post tax. You can see that with the £205m and the £52m, the first two lines in this slide.

Secondly, we separate out both material profits and losses and disposals of assets together with material asset impairments. During the period we recognise the net pre-tax expense of £25 million comprised of asset impairment charges largely offset by the gain and disposal of our Clockwork business in the US. Post tax the net charge was £3 million, and you can see that from the three line items £29m and £30m offset by the profit of £56m.

Thirdly, as you know, we have substantial risk management activities hedging a large proportion of both the purchases of gas and electricity to meet the future needs of our customers, and the sale of our E&P and power production volumes. Where accounting standard require those hedges to be marked to market, we separately identify those non-cash mark to market movements. During the period this generated a pre-tax mark to market expense of £499 million. Post tax the expense was £424 million.

When the oil, gas and electricity is delivered to our customers the hedges mature and they are recognised in business performance at the same time as the underlying hedged transaction.

The combination of the restructuring costs, asset impairments and non-cash mark to market movements was a loss of 12 pence per share, which more than offset the underlying earnings per share of 2.4 pence.

Turning now to Centrica Consumer, where adjusted operating profit was down 44% to £240 million. As you can see from the chart, this is largely due to the introduction of the UK price cap including the non-recurring one-off £70 million hedging impact which we are currently challenging in the court. The positive effects of our efficiency programme contributed £71 million, broadly offsetting the combined negative impacts of inflation, warmer weather and a decline in underlying margins reflecting the impact of a lower average number of energy accounts in the UK which more than offset strong performance at Bord Gais in Ireland.

Turning now to Centrica Business, where adjusted operating profit fell by 89% to £11 million. Looking first at external factors, the positive impact of higher baseload power prices in Nuclear and the weaker pound were almost entirely offset by inflation and warmer than normal weather.

Unfortunately, the extensions to the regulatory outages at the Dungeness B and Hunterston B nuclear power stations mean neither station has generated any power this year, resulting in lower operating profits. When we take the increased power prices in the first half we would have expected our profits to be £45 million higher had these reactors operated.

As you can see, we benefited from lower losses from the one remaining legacy gas contract in our Energy Marketing and Trading business.

In the first half of 2018 we were able to capture substantial value from abnormally cold weather conditions in the US North-East. This year we have seen far more benign weather conditions which has resulted in lower price volatility and therefore fewer optimisation opportunities.

Underlying performance in the rest of Centrica Business was down in 2018 but this was more than offset by cost efficiencies, with our efficiency programme improving operating profit by £13 million in the first half.

I'll now take a minute to look at Exploration and Production which includes Spirit Energy and Centrica Storage's Rough field. Adjusted operating profit dropped by 42% to £148 million. A little under half of the deduction was due to external factors, most significantly the decline in UK gas prices with 2019 prices having fallen by around 10 pence per therm since the Preliminary Results in February. Spirit Energy production was slightly down on last year although the volumes were moderately ahead of our expectations and we still expect full year production volumes to be broadly in line with 2018. Centrica Storage volumes reduced as expected, reflecting the natural decline of the Rough field.

We also saw increased exploration expenses in Spirit Energy, principally due to writing off the first of our three wells in the Greater Warwick area. You can see that in line with our other divisions we continue to improve our cost performance and it is pleasing to note a further £13 million of efficiencies were delivered in the first half.

Moving now onto cash flow. As indicated in February, tax outflows returned to a more normalised level this year with a net cash payment of £79 million in the first half, the working capital outflow we saw was flat when compared to last year.

There was an underlying increase in working capital in line with normal seasonality in our customer-facing businesses. In addition, Spirit Energy had a stronger end to the first half of 2019 than it did to the second half of 2018 which resulted in a higher working capital outflow. However, we delivered the first £100 million of our structural working capital improvement programme in the first half which offset the underlying increase in the outflow. I will cover working capital in some more detail shortly.

Overall, these factors, combined with £249 million reduction in EBITDA and the fact that we received no Nuclear dividend due to plant outages, resulted in adjusted operating cash flow falling by £357 million or 32%.

Having a look at net cash flow now. You can see clearly here that despite the £357 million fall in adjusted operating cash flow, our continued capital discipline resulted in a reduction in free cash flow being restricted to £78 million. We took steps to reduce our organic capital investment, saving £83 million in the first half of the year and we made no acquisitions in the period resulting in a further reduction of £55 million year-on-year and we realised £260 million from the disposal of our Clockwork Business in the US. Taken together, net investment fell by £324 million.

Restructuring costs increased by 50% as we stepped up the delivery of the second phase of our efficiency programme.

Net interest outflow reduced by almost half to £79 million principally due to the reduction in gross debt coupled with more stable foreign exchange movements. In addition, 2018 saw a £139 million outflow relating to the debt repurchase programme.

Dividends paid to Centrica shareholders of £383 million were lower than last year reflecting a higher scrip take up related to the 2018 final dividend which was paid in June this year. We paid our first dividend to Spirit Energy's minority holders of £124 million relating to 2018.

Pension deficit payments also increased compared to last year and this includes an additional one-off £75 million deficit payment made in January as we agreed with the Pension Trustees as part of the 2015 triennial valuation. We have now concluded the 2018 triennial review and I will take you through this in more detail shortly.

Reflecting on all of these factors, net cash outflow of £305 million was broadly in line with what we saw in the first half of last year.

Moving on now to our efficiency programme which delivered a further £97 million of savings in the first half of 2019 which again, more than offset the impact of inflation and foreign exchange movements.

We made significant further progress in transforming our customer and field operations in the UK and the US, enabled by further digitalisation of customer journeys including continued focus on self-serve and automation. In April, we announced the closure of two of our UK customer operation sites. In June, we announced a further reduction of 700 management and back office roles in the UK and we continue to make progress with reducing the size of our corporate functions.

As Iain mentioned earlier, despite the weak first half performance, the outlook for the second half is more positive and we expect adjusted earnings and operating profit to be sequentially higher due to a number of factors, a crucial part of which is recovery of North America Business and I would like to take a minute to talk about this.

This business made an adjusted operating loss of £14 million in the first half, which is as much of a disappointment to us as I am sure it is to you. The chart on the left shows the gross margin contribution from each part of this business in the first half over the past three years.

In 2018, the big change was a reduction in the power supply business which reflects both the competitive environment and higher capacity charges, partially offset by the material profits made from gas optimisation in January 2018 due to abnormal weather events.

In 2019, whilst we have also seen some improvement in the power supply business, more benign weather conditions resulted in a lack of gas optimisation opportunities. When you look ahead to the second half of 2019, the value of our contracted forward book as at the 1st July is higher than it has been in any of the previous two years. The increase is largely in the power businesses, more specifically in the power supply business, as we see the benefit of reduced capacity charges coming through.

Assuming a normalised level of margin is added in the second half, this, combined with the higher forward look, would indicate an additional 100 million dollars of operating profit in the second half of 2019 compared to the same period last year. When you compare it to the first half of this year the improvement is more significant. Of course this is subject to the usual caveat of normal weather.

The outlook and future for North America Business was one of the topics that Iain touched on earlier and he will cover that shortly in more detail as he looks at the businesses.

I would like to take a couple of minutes to cover the 2019 targets we set out in February before looking at the longer-term outlook for the balance sheet and cash flow.

Despite the weak performance in the first half we remain on track to meet all of our targets. We continue to expect adjusted operated cash flow in the range of £1.8 to £2 billion albeit in the bottom half of this range. This includes around £200 million of structural working capital reductions, half of which was delivered in the first half.

We continue to expect to deliver £250 million of cost efficiencies in the year which will result in-between 1,500 and 2,000 colleagues leaving the Group. We have taken steps to reduce our capital expenditure and this will not exceed £900 million for the full year, below the £1 billion we announced in February. We continue to expect to deliver our £500 million non-core asset divestment programme, with the Clockwork disposal completed in April.

Finally, we continue to expect net debt to remain within our targeted range of £3 to 3.5 billion as the actions we have taken to reduce capital expenditure and release working capital compensate for the weaker performance we see in 2019. In addition, it is worth remembering that normal seasonality in our business results in a net inflow of working capital in the second half of the year.

As you know, running a substantial energy supply business, particularly one which includes fixed or capped prices, requires a material commodity purchase programme and careful risk management. At the end of 2018 we had £27 billion of forward commodity commitments relating to 2019, 2020 and 2021 to hedge our downstream supply commitments not only for the 15.7 million energy customer accounts, but also to the energy supply customers in our business division in the UK and North America. This requires us to be an attractive counterparty with which to trade, hence the requirement for strong investment grade credit ratings.

Following our intended exit from E&P and Nuclear, the Group will have a lower asset intensity, and this is likely to result in higher credit thresholds being applied in order to retain the same credit ratings. As a result, proceeds from the Spirit Energy and Nuclear divestments will be retained on our balance sheet to reduce debt. We will also maintain our focus on capital discipline including structural working capital reductions.

Taking a minute to touch on debt. We have a long-dated bond portfolio with maturities out to 2045 and an average interest rate of 4.9%. Furthermore, in February this year we renewed our 21 banks, £4.2 billion Committed Revolving Credit Facilities. These RCFs have an initial maturity of 2024 with two one-year options. The vast majority of these facilities are currently undrawn.

I mentioned in February that there was more that we could do to structurally reduce the amount of working capital we carry in the business and this has been a focus area over the past few months.

The Group’s trade working capital has normally been in the range of 4 to 4.5% of sales which we believe is too high and we think we could reduce this to 3% over time. This step change would result in the release of approximately £400 million of working capital, both reducing Group net debt, and increasing the Group’s return on capital. We have already delivered close to £100 million of this in the first half and we will look to deliver the same amount again in the second half of this year, with the majority of the remaining £200 million expected to be delivered in 2020.

On pensions, the latest actuarial valuation has now been finalised with our Pension Trustees with a technical provisions deficit of £1.4 billion as at 31 March 2018, up from £1.2 billion at 31 March 2015. As a result of this agreement we have committed to making additional annual cash contributions to fund the deficit with total payments of £223 million this year and £175 million per annum thereafter until the deficit is extinguished.

During the first half we also agreed with those UK-based employees still in defined benefit pension schemes that we would reduce benefit accrual rates and therefore make lower company contributions going forward. We have also started, in conjunction with the Pension Trustees, to de-risk the pension fund asset portfolios by increasing the inflation and interest rate hedges from one-third to two-thirds. This will lead to reduced volatility in the deficit going forward.

In terms of the IAS 19 accounting deficit, the combined net deficit for all of our DB schemes has risen from £79 million at the end of 2018 to £114 million at the end of June 2019.

Moving on now to future capex expectations. Following the disposal of Spirit Energy and Nuclear, and with the continued focus on capital discipline, we will be targeting annual capex of around £500 million per annum.

It is quite important to note that once we have exited E&P our capex programme will largely comprise of relatively small-scale, short lead time projects. This provides us with the flexibility to respond quickly to changing market conditions and flex investment as required. All investments we make will be expected to deliver a minimum IRR of 10% in line with our Group Return on Capital Employed target of at least 10 to 12%.

Our M&A team is rather busy just now and this is going to continue in the coming months as we execute both our £500 million non-core asset divestment programme, commence the process to dispose of Spirit Energy, and complete the sale of our Nuclear stake.

To date, we have delivered just under half of our non-core divestments and we have a number of processes in train at the moment to deliver the remainder over the next six months.

Disposal of our Nuclear stake continued to make good progress. As I have indicated previously, this is a lengthy process and frankly it has not been helped by Brexit nor the operational issues at both Hunterston B and Dungeness B. However, these are good quality assets and we continue to pursue our exit from this business by the end of 2020.

We will kick off the disposal process of Spirit Energy shortly and we are confident we have a good number of interested parties. It is not often the opportunity to purchase a 50 million barrel business presents itself, and especially not one that can stand alone. It is pleasing to be able to confirm that we are fully aligned with our partner SWM.

We will retain our focus on maximising value from the assets held by Centrica Storage Limited at both the Rough field in the Southern North Sea and the Easington terminal in the UK.

Moving now to the cash flow outlook for the next few years.

Throughout the period of restructuring, the majority of which we expect to complete by the end of 2021, the Group is expected to generate positive free cash flow every year including the impact of divestments. Adjusted operating cash flows are expected to fund the rebased dividend, capex, interest expense and pension deficit contributions. The operating cash flows will also partially fund the restructuring costs associated with the delivery of the additional £1 billion pounds of efficiencies from 2019 to 2022.

Like our capital expenditure, the restructuring programme comprises of a substantial number of discrete projects and we can therefore flex the programme up and down as circumstances dictate. We expect restructuring costs to average £300 to £400 million per annum between 2019 and 2021 with the balance of the expected £1.25 billion cost falling due in 2022. Any restructuring costs not funded out of operating cash flows will be met from the proceeds of the Nuclear and Spirit disposals. The balance of the disposal proceeds will be held in the balance sheet to materially reduce net debt.

We indicated in February that our adjusted operating cash flow was under some pressure, and as you can see from the chart, whilst we expect 2019 and 2020 to be lower than in previous years, we continue to expect our businesses to deliver substantial operating cash flow.

There are a couple of points worth noting here. Firstly, these numbers will obviously change once we have disposed of both the Nuclear business and Spirit Energy. Secondly, the cash flow in 2019 and 2020 is underpinned by the structural reductions we are making to working capital.

We have had a consistent financial framework for the past four years and it is appropriate now to update this for the next few years. However, before doing so I wanted to let you know that from the end of 2019, we will report results at a divisional level for three divisions: Centrica Consumer, Centrica Business, and Exploration, Production and Generation. We will provide you with the results at a business unit level for the second half of 2019 to allow a transparent transition to our new reporting segments.

Back to the framework. We will continue to target growth and adjusted operating cash flow over the medium term. The dividend is expected to grow from the rebased 2019 level over the medium term, in line with underlying growth in earnings and cash flow, and dividend cover from earnings is expected to be in the range of 1.5 – 2.0 times over the medium term. We will continue to target increases in operating costs below inflation each year and we intend to deliver a further £1 million of cost efficiencies by the end of 2022.

Following the disposals of Spirit and Nuclear, capex will be around £500 million per annum and we will continue to target strong investment grade credit ratings.

Finally, our Group Return on Capital Employed target remains at least 10 to 12%.

I will now hand you back to Iain to look in more depth at our Strategic Update.

Iain Conn – Group Chief Executive

Thank you Chris. I would now like to cover the key aspects of the strategy going forward and specific outcomes of the Strategic Update in more detail. I will outline the Group's purpose and strategy, the changing energy landscape and Centrica's role in it. I will then cover our performance agenda, cost efficiency and transformation programmes.

A significant part of this is about rebasing UK Home. So I will go through this and our plans to become the lowest cost energy supplier in some detail. I will then move onto the decision we have made to refocus Connected Home, renamed Centrica Home Solutions, before covering the actions we are taking to improve returns in North America Business. Next I will cover our progress in Centrica Business Solutions, describe some of the new capabilities we are building for 2020 and beyond, specifically in the areas of home energy management and electric vehicles, before summarising.

Let me start with purpose and strategy. So what is Centrica here to do? Our purpose, as set out in 2015, has been refreshed, but its essence remains unchanged. We are focused on satisfying the changing needs of our customers but are now increasing the emphasis on enabling the transition to a lower carbon future. Helping our customers run their world in ever more sustainable ways. In that sense we are becoming a 21st century energy services and solutions company and the portfolio changes we are announcing today will complete our shift to this destination and to the customer.

For our other stakeholders our strategy remains to deliver long-term shareholder value through returns and cash flow growth while being a trusted corporate citizen and an employer of choice.

The energy landscape is changing rapidly and I want to describe Centrica's role in it. There are three big points. First the trends that we identified in 2015 continue to play out. Specifically the energy system is becoming more decentralised as advancements in distributed technologies support decarbonisation. Choice, power and influence are moving to the customer and digitalisation is accelerating proposition development, increasing choice and driving efficiency across our sector.

Second, we are now equipped and committed to help our customers' transition to a lower carbon future with capabilities to help them reduce their emissions while we also exit the hydrocarbon production business. We supply natural gas and believe in its near-term role in replacing coal. But we also embrace the ultimate need to decarbonise heating. We have targets to reduce the emissions of our customers, the energy system and our own operations and have made a commitment to have a plan by 2030 to be at net zero by 2050.

Third, we build specific major technology capabilities to offer our customers. In Business Solutions we can now deliver combined heat and power, solar, battery, fuel cell solutions and electric vehicle integration. We can also offer business insight and optimisation solutions including distributed sensing, demand response and route to market services.

In Home Energy Management, we are working on energy control and optimisation, electric vehicle charging and mobility solutions.

Our investments in platforms, including our Integrated Solutions Platform in Centrica Business Solutions, the Honeycomb Connected Home Platform, Greencom networks and Driivz will help us serve our customers future needs and enable growth.

We showed this slide in February. Our strategy is now formulated to contribute to and benefit from the long-term structural changes required to address climate change. In short, we are completing the shift from a company unsuited to where the world of energy is going to one in tune with it. We have made commitments with clear targets in line with the Paris accord built around three pillars. To help our customers reduce their emissions, to enable a decarbonised energy system and to reduce our own emissions. We will report our progress against this framework on an annual basis. We are one of the few companies prepared to commit to improving their scope three emissions, i.e. those associated with their customers.

Let me now turn to what we will offer them. Our overarching purpose is to satisfy our customers changing needs including helping them transition to a lower carbon future. We will offer them more than just energy supply. Energy supply is only one of the services we provide. We will provide services and solutions which customers value and are willing to pay for either separately or as part of bundled propositions. We will focus on those areas in which we have distinctive strengths, specifically, energy supply and its optimisation and services and solutions centres around energy. Our field force is a unique asset and we will expand its tremendous in-home fulfilment capabilities and we will integrate new energy technologies, design customer platforms and leverage data and data analytics to serve our customers better.

Last but not least, we will target being the lowest cost provider consistent with our brand positioning and propositions. This will enable us to price at the most competitive level, slow and then stop customer losses and over time allow us to grow customers and gross margin.

To deliver for our customers the Centrica team must also continue to evolve. We must relentlessly be focused on these five Group priorities. First, customer obsession. Our service to customers has significantly improved but now we must put the customer at the forefront of absolutely everything we do. Second, we need to continue to drive operational excellence to streamline everything and get things right first time. Third, the key financial outcome we will continue to focus on is cash flow growth with which we can fund our needs and underpin our dividend and pension obligations. Fourth, we have to be relentless in our pursuit of becoming the most competitive provider. Finally, in many ways most importantly, some things that we have been doing have been holding our colleagues back and we need to empower them more to allow them to drive the business forward.

So let me turn to the strategic pillars and capabilities of the divisions. We are tightening their focus, built around capabilities where we are advantaged. In Centrica Consumer we will have three strategic pillars, energy supply, in-home servicing and home solutions. These are all activities in which we have distinctive positions, strengths and capabilities. In energy supply we remain the largest supplier in the UK with twice as many customers as the next biggest. We also have top three positions in Ireland and North America.

We have significantly improved customer service levels in all geographies since 2015 while our digital and segmentation capabilities are greatly enhanced. We will drive our cost base to become the most competitive and there is much more potential which I will come onto shortly. And we will offer energy bundled with our own services and solutions, and if we discount anything in the bundle it will be the energy.

This is hard for competitors to imitate. In in-home servicing we are by some distance the largest supplier of contract cover and boiler installations in the UK. We have over 9,000 British Gas service engineers, a position that is almost impossible for competitors to replicate. In the US we have a top 10 and growing position in the provision of protection plans. Our in-home servicing business delivers world-class levels of customer service. Our UK engineer NPS is +65 and increasingly we are upskilling our employees, training them in areas such as smart metering, electric vehicle charging and home energy management solutions.

Our third pillar is Home Solutions which will now be refocused and centred around home energy management. We are the UK's leading smart thermostat provider and have scalable reliable technology platforms. Our in-home servicing channel drives sales and end to end customer service.

Our focus moving forward will be on energy management, including integration of new technologies, such as fuel cells, remote diagnostics and additional growth in electric vehicle related propositions, as demonstrated by our exclusive deal with Ford announced today.

Moving now to Centrica Business. As in Consumer, our strategic pillars reflect where we have distinctive strengths and capabilities. In Energy Supply, Energy Optimisation and Business Services and Solutions. In Energy Supply we are the largest supplier to small and medium enterprises in the UK and the second largest competitive retailer in North America. Our customer service levels have improved materially while our cost base has progressed to competitive levels with potential for further reductions.

In Energy Optimisation, we now have 24,000 MW of contracted route to market capacity globally while we also have 2.5GW of demand response capacity under management. In both areas we have leading software capabilities. In North America we have gas pipeline and storage capacity that provides valuable optionality while we also have strong energy trading capabilities in both North America and across Europe and a growing global LNG position.

In Business Services and Solutions we now serve over 5,500 sites and have over 600MW of energy solutions capacity under management. We are able to offer customers end to end design, installation, maintenance and service solutions for a wide and expanding range of energy technologies. And as in Consumer there is further growth potential from a development of energy management platforms and integration of electric vehicle propositions.

Let me now turn to our near-term performance agenda and progress against it. This is the 2018-20 performance agenda we have shown before. Our first priority is to demonstrate we can grow overall gross margin. We are not yet achieving this which I know is an area of concern, particularly when we lose customer relationships. But we are seeing some signs of progress. As I said earlier we saw net growth in consumer accounts in the first half of the year and there are also further encouraging signs of underlying growth in Centrica Business in particular in Centrica Business Solutions. Delivering cost efficiency, until we can stabilise gross margin remains crucial to earnings and cash flow. I will cover this and our targets to become the most competitive supplier shortly.

Improving organisational effectiveness remains a major focus and is reflected in our current transformation programme. And we need to continue to secure the capabilities we need for 2020 and beyond as the energy system continues to change. I will cover some important developments in home energy management and electric vehicle propositions later in the Presentation.

Finally as you have heard from both Chris and me already, maintaining capital discipline and balance sheet strength remains crucial.

I will now cover our updated cost efficiency ambitions and wider transformation programme. As you already heard, we have delivered over £1 billion of like-for-like efficiencies since 2015. But there is still significant further opportunity and we are targeting a further billion of efficiencies over 2019 to 2022 which is £250 million more than we indicated in February. This additional efficiency is enabled by the conclusions of the strategic update we announced today. This chart has therefore been updated to reflect this increase and now shows the phasing of the projected savings by year. We would expect efficiency delivery to be front end weighted with 85% of the savings planned to be delivered by 2021. Even after inflation we would expect our like-for-like controllable cost base to be £500 million lower in 2022 when compared to 2018.

The restructuring costs to deliver this scale of efficiency will be significantly higher than the cost to deliver the first billion given the fundamental nature and restructuring associated with some of the initiatives, at around £1.25 for each £1 of annual savings. However, with an estimated 15-month payback this is still an extremely good investment with the end result being that by 2022 we would expect to be the lowest cost provider in all of our markets consistent with our chosen brand positioning and propositions.

Let me outline to you the activities underpinning our transformation to reach this level of competitiveness. This slide shows the major projects driving efficiency within our transformation programme. There are a number of ongoing projects that started in 2018, namely the transformation of our customer and field operations in the UK alongside the transformation of UK Business. These will total £450 million of annualised savings by 2022.

Additional projects have been activated and accelerated during the first half of this year as we responded to the current environment including the UK price cap. These are focused on activities within the Group functions, third party spend, the efficiency of core processes and change programmes, transformation of North America Home and overheads reduction in UK Home. These will contribute about £300 million by 2022.

Finally, there are major projects which are consequent on the strategic update conclusions and the move to a simplified and focused customer facing company. They include the fundamental rebasing of UK Home in a price cap environment, the right sizing of management structures across the Group and review of all remaining business unit overheads. We will also be reviewing and consolidating our property footprint. These enable acceleration and delivery of the additional £250 million of efficiencies into the period to 2022.

This is a huge effort and significant degree of change and I'd like to thank Centrica colleagues for delivering it as we also go about serving our customers.

Let me now cover the rebasing of UK Home in more detail. This chart shows the historic and future targeted cost per dual fuel energy account in UK Home in real terms. It excludes costs associated with metering, including smart, as these should normalise over time for all suppliers.

The savings we have delivered since 2015 have kept us moving forward competitively despite battling the loss in energy accounts over the period. So we are now in the bottom half of the range of comparable large and medium suppliers. We are seeing further progress on unit costs in 2019.

Our brand strength and affinity and bundling with other propositions is allowing us to compete effectively this year as demonstrated by the overall increase in energy and services accounts in the first half of this year. However there is much more we can do.

Plans already in action should deliver around £20 per customer of savings in real terms by 2022 taking us to around the level of the projected first quartile performer, the £85 you see on the right. However we are developing plans now to fundamentally rebase the business and take us below this level towards the cost base of the projected lowest cost supplier in the market. Given our scale as the largest supplier in the UK market we believe this is an appropriate target by 2022.

Let me give you a little more detail on the activities underpinning this journey. Here you can see the actions we have already delivered, the plans we already have in place and our future plans. Since 2015 we have significantly improved our competitiveness with cost savings delivered through the removal of process duplication and management layers and increased digital functionality, driving greater self-serve and fewer calls to our contact centres. We have also seen retention benefits from our British Gas rewards programme with 2.3 million of our customers now members and from bundling of propositions.

The plans we are currently enacting involve further improvements to our digital platform, driving digital transactions from 50% today to 70%. We are also upskilling our contact centre teams, reducing costs, the complexity of certain journeys and improving the customer experience through the elimination of call transfers. We will also continue to reduce costs in our back office operations, driving increased automation while we will also reduce the number of non-customer facing roles in the organisation.

These plans will get our costs to first quartile, helping underpin customer stabilisation when combined with our brand. However our future plans will deliver cost leadership and enable us to grow customers and margin. These will entail more fundamental transformation including process reorganisation around customer end-to-end journeys, not traditional industry processes. They will also mean us transforming our IT stack to be more flexible and with lower costs. And we will increasingly embed machine learning into our core operations reducing the number or the amount rather of human contact required.

Moving now onto in-home servicing where our focus is on driving further improvements to competitiveness and service. The chart on the left shows how we have continued to improve the experience for our services customers as measured by the percentage of visits we fulfil on the scheduled day. It is already high and NPS is strong, but we are focused on improving this further still and getting it to as close to 100% as we can.

There are also further efficiency opportunities to reduce our cost per customer visit which will allow us to maximise the growth potential of the business. Although our customer value proposition justifies a price premium and we can see this in our retention statistics, we are focused on becoming more efficient relative to our lowest cost competitor and are targeting a reduction in our cost per customer visit by around 10% over the next three years in addition to further operating cost reductions.

In terms of activities, we have already made good progress on improving our service levels and competitiveness since 2015. We have upgraded our field technology and diagnostics which has improved our first-time fixed rates while the introduction of online appointment booking has reduced the call volumes. Our engineer tracking tool has improved the customer experience and helped reduce the number of missed appointments, while our teams are now organised around the customer which has reduced the number of internal hand-offs.

We have also renegotiated pension terms with our engineers and their unions to make us lower cost in the medium term while still offering a competitive pension offer. And importantly we have seen a return to customer growth over the past two years helped by the launch of new propositions including energy and services bundles.

We have current plans to further improve competitiveness and enable future growth. We are developing a new engineer fulfilment platform which will enable consolidation and reduction of back office costs. We are also upgrading our field and supply chain technology, improving same day parts availability. We are targeting an improvement in our first-time fix rates to 90% from around 80% today. We will also continue to focus on improving the effectiveness of our service engineers, leveraging their skills to capitalise on new market opportunities such as electric vehicle charge point installation and servicing, while also increasing our flexibility to meet our customers' requirements.

Moving now onto the repositioning of Connected Home. We have learnt a lot through Connected Home and developed important skills and capabilities for the future. Geographically you can see from the chart we have been successful in growing Connected Home materially in the UK, in part due to the scale of total UK customer base, sales channel synergies with energy and services and the use of our in-home servicing capabilities to fulfil installation of products and as a sales channel. As a result we have developed a strong position in the UK with leading brand awareness, high levels of customer satisfaction, a reliable and scalable platform and a wide range of products that are synergistic with our energy and services offers and which drive retention. We are seeing a positive impact on our energy and services businesses with the energy NPS for Hive customers 13 points higher than for an energy only customer and the addition of new to Centrica customers providing an additional energy and services sales channel.

However we have not achieved expectations for growth in other geographies despite our Direct Energy customer base and partnership with ENI in Italy, due to the absence of a number of these factors. Therefore having reviewed the key success factors for growth we have concluded that we cannot justify expansion into other geographies and Connected Home will now be focused on the UK and Ireland, with the business unit more appropriately renamed Centrica Home Solutions. It's about much more than connecting the home and it should also be very closely tied to our core skills in energy management and in-home servicing. We will continue to leverage our distinctive field force for new propositions which will be focused around home energy management and home remote diagnostics and monitoring.

Given these changes and reduced resource allocation as a result, we are now targeting revenue of £150-200 million by 2022 compared to £67 million in 2018. And with lower costs and reduced investment requirements we are targeting EBITDA breakeven for Centrica Home Solutions by 2021. We will also continue to evaluate joint ventures and partnerships in home solutions, if they unlock further value from the platform and capabilities we have created to date and I will outline an example in a moment.

Moving now onto Centrica Business and first North America Business. North America Business is a unit of significant scale but as you know we have had issues recently with margins and returns.

We make money through supplying gas and power to around 250,000 customers and through the optimisation of pipeline and storage capacity that our retail activity enables and through providing route to market services for power generators. North America Business also provides risk management support for North America Home's procurement activities. North America Business has a number of sources of competitive advantage: Its scale as the second largest competitive retailer, the range of its product offering to customers, its risk management and optimisation capabilities and high levels of customer service. Its large customer base is also a source of competitive advantage for Centrica Business Solutions.

However recent performance has not been acceptable due to a combination of both structural and internal factors. Customer usage is declining with energy efficiency measures taking effect. And we are seeing increased levels of competitive intensity.

Of a more temporary nature the shape of the commodity curve and the phasing of capacity charges has created an additional headwind since 2017. There are internal factors that have impacted performance including poor visibility and forecasting of gross margin components and we have taken actions to address these. We have already intervened to improve performance and initiated some further actions. We are making improvements in the quality of underlying gross margin through focusing on higher value customer segments and changing our core retail offer to reduce risk and volatility. We will continue to optimise our customer mix and increasingly leverage our business solutions technologies and propositions to help improve retention rates further.

We have also delivered $25 million of cost efficiencies since 2015 and there are further actions in place to deliver an additional $25 million over the next two years. We have successfully reduced the capital employed in the business by $1.2 billion since 2015 without degrading the underlying margin quality of the customer book. Further working capital and margin cash initiatives mean we are targeting a further $100 million reduction in capital employed over the next two years.

So what does all this mean for returns going forward? Our focus will remain on business energy supply and optimisation where we have distinctive positions and capabilities and on enabling growth of Centrica Business Solutions.

The actions we have already taken combined with the reversal of the commodity curve shaping effect and capacity charges are expected to lead to economic returns in excess of cost of capital in 2019. And the further actions we are taking are expected to lead to average post tax economic returns on capital employed of at least 10-12% and no worse than 8% at the bottom of the cycle.

If we can deliver such returns through the cycle, limiting the downside, while enabling Centrica Business Solutions growth, then North America Business will deliver lasting value to our shareholders and will be core to Centrica's portfolio. We are determined to deliver these outcomes on a sustainable basis. If we cannot deliver improved returns relative to cost of capital and therefore through cycle shareholder value, then clearly it would bring into question the role North America Business plays in our portfolio. We will only invest for growth in North America Business once materially improved returns have been demonstrated.

So moving now to cover Centrica Business Solutions. Centrica Business Solutions is highly aligned to the energy trends I referenced earlier and the associated changes in customer demand for new propositions. We are focused on delivering energy optimisation and solutions propositions for customers and now have a wide range of technologies to underpin our solutions offering as well as advanced software to underpin our optimisation propositions.

We have developed distinctive capabilities and an integrated approach to customer solutions through our integrated solutions platform. We have been successful in developing an international business model with operations in 11 countries and 64% of the order book is now outside the UK. And as you can see from the chart on the left, growth rates for order intake and order book have been accelerating. Centrica Business Solutions is becoming material and we hope to achieve revenues of over £300 million this year. We will continue to invest internationally in Business Solutions with our focus on the UK, Ireland, North America and Continental Europe.

Importantly, our growing installed base provides a platform for recurring revenues from operations and maintenance, optimisation activity and finance solutions. On the left you can see that more than half of our order book is recurring in nature and made up of a variety of technology solutions and optimisation services. We are going to look to deliver further growth through leveraging our existing customer relationships as well as expanding our range of technologies to meet customer needs.

With continued resource allocation to this growing and attractive business we continue to target £1 billion of revenue by 2022. With unit gross margins expected to be around 20% we are targeting Centrica Business Solutions to break even at an EBITDA level by 2021. This combination of skills and capabilities we have built within Centrica Business Solutions makes Centrica an international market leader in this area.

Finally, let me briefly cover a couple of specific areas where we have been developing additional capabilities to meet some emerging future needs of our customers.

Consumers and businesses are approaching us to help them with energy management and mobility solutions around electric vehicles and we are developing propositions and technologies for inclusion of electric vehicles for both consumers and business customers, integrated into their energy management systems. In electric vehicle solutions the focus has been on energy system requirements for EV integration, EV energy tariffs, electric vehicle optimisation software and after-market services.

I am delighted we have announced this morning an exclusive partnership with Ford as they prepare to launch their latest electric car to the European market. Under the five-year partnership, Ford customers will be offered a dedicated home charging installation and EV tariff from British Gas, while we will also install charging points at up to 1,200 Ford dealerships across the UK and Ireland. We will also explore demand side response services including the potential technologies of vehicle-to-home-to-grid and home energy management solutions with Ford. Integration of EVs into the home and control of all energy management requirements of the home will be an important growth node. We are working on a potential platform to enable this for customers.

We already have ownership interests in individual technology platforms that will enable us to achieve this. We own the platform for home heating control, automation and diagnostics. It is called Honeycomb which supports Hive today.

We also have an 18.7% interest in Greencom Networks, an energy management information and brokerage platform for the home, and a 17.2% interest in Driivz, who have developed an EV charging network control platform which supports some of the leading EV networks in the United States and in the Netherlands.

And at the bottom of the chart, the acquisition of REstore in 2017 also provided us with leading demand response capabilities which we can increasingly leverage for consumers as well as businesses. We intend to work on the integration of these platforms and the development of a customer interface which will allow consumers to control and optimise the energy of their homes, electric vehicles and the relationship to the grid. This is an important future market and the technology positions we have developed when combined with our other skills and in-home servicing capabilities leave us well positioned to benefit as evidenced by the Ford deal announced today. And we are also talking to a number of OEMs about similar relationships.

I hope these more detailed summaries of some of the key conclusions from our Strategic Update have helped to position Centrica today, our determination to drive efficiency and competitiveness and the leading capabilities we have been building and their relevance for the future.

Let me now summarise with what you can expect from Centrica moving forward. Our direction of travel towards the customer has been reconfirmed in the Strategic Update. We will complete this shift with the exit from E&P and Nuclear with Centrica becoming a leading international energy services and solutions provider.

As I hope I have demonstrated, Centrica is increasingly well positioned for the future energy transition as the world of energy decentralises, rent moves towards the customer and we harness the power of digitalisation. We will focus on our strengths of energy supply and its optimisation and on services and solutions centred around energy, with an emphasis on helping our customers' transition to a lower carbon future.

While we build these propositions, we must also drive to being more competitive. We will deliver further material cost efficiency out to 2022 as we target becoming the lowest cost provider in all of our markets consistent with our chosen brand positioning and propositions. This will be a key enabler for us to deliver stabilisation and growth in customer accounts, when combined with new propositions, the expansion of net margin per customer. We will continue our strong focus on capital discipline and on maintaining a strong balance sheet. And we will aim to pay a progressive dividend linked to earnings and cash flow growth from the rebased level of 5 pence per share we have announced today.

Thank you for listening. I'd now like to invite Sarwjit and Richard onto the stage for Q&A, thank you.

Questions and Answers

Q1. Jenny Ping, Citi

Hi, it's Jenny Ping from Citi. Two questions please. Firstly, Chris I'd like to understand a bit more about the conversations you have had with rating agencies in terms of what is the scale of the uplift on the ratios that they are looking for, for the new Centrica, and what sort of conversations you have had with them?

And then secondly, just going back to the cost savings element, you talk about wanting to become the lowest cost supplier; I presume that is amongst the big six. How do you then sort of square the circle in terms of the 20+ independents that are still biting at your heels for market share? Thanks.

Answer: Iain Conn
Thank you, Jenny. Let me answer the second and then pass over to Chris on the rating agencies. Firstly, we are not talking about relative to the big six, we are talking about relative to anyone. And I did say consistent with our brand and propositions. So, in energy supply in the UK we are targeting being the lowest cost provider, full stop. That will require some radical changes to our IT architecture, our end-to-end customer journeys and our internal processes, and that is what the next phase is about. It has not been possible up to now to get to that place, but we have got to being very competitive with the large suppliers, just not with the leaders in terms of cost alone.

In servicing we do not necessarily have to be the cheapest. In fact, our customers would say we don't want you to be the cheapest, we are willing to pay for what British Gas offers and the assurance that the service that we offer provides. So, one has to be very careful about unit KPIs dependent on what you offer. Because clearly if customers are willing to pay a premium for a premium product then you can charge more.

But in the case of energy, the evidence suggests that we have to compete head on with the cheapest and that is the goal. And it is not just about the UK, it is in all of the markets in which we operate internationally and all of the business units. Chris, credit rating agency conversations?

Answer: Chris O'Shea
We have had some quite some detailed discussions Jenny as you would expect. Unfortunately, I am not allowed to disclose what they have told us. But in the discussions, normally if you go through a process like this you would present an actual transaction with the agencies, you'd go through the RAS RES process and they'd tell you what your ratings would be. We don't have an actual transaction to present just now.

So, we have had some theoretical conversations and they have given us some indications which I think lead us to believe we can do what we want to do and still maintain strong investment grade credit ratings. I think that the conversations are reasonable, I would obviously suggest that they are maybe a bit conservative on the ratings, but they do expect an increase as the asset intensity goes down. But they would charge me a huge amount of money if I was to disclose what the numbers are so it has got to remain private at the moment, but it is entirely in line with what we are planning to do.

Q2. John Musk, RBC

Good morning everyone, John Musk from RBC. Apologies for the first question Iain, but in terms of your decision to retire and the timing of that, what led you to decide that May next year is the right time and is there a risk that your successor comes in, has another look at the strategy and we are all sat here in 12 months time with yet another refresh of what Centrica is planning to do?

And then secondly, on the new dividend baseline and rebasing that to 5 pence, can we talk a little bit about the dilution impact from these disposals? My own numbers would suggest somewhere around about 2p, maybe 2.5p, of dilution and given the new 1.5 to 2 times earnings coverage are we able to see a progressive dividend into 2020, or is that going to be quite tough?

Answer: Iain Conn
Okay, so first of all on the decision to step down and retire from the Board next year, first thing, this is completely in line with my original timeline when discussed with the Board back in 2014, first point. Secondly, it is not just my decision. I have been in discussion about this with the Chairman who is sitting in the front here for months actually, and we were deliberating whether this was the right time or the wrong time. The view that we reached together was that at this moment, when we are making the final decisions on the final portfolio repositioning of the company, it was the right time for me to indicate that once those are largely done it would be time, with a small and more focused customer facing company, for me to pass on to somebody else who would take it forward. I mean, I have nearly done 5 years already and I believe it is the right time to start working on the succession. But I have also absolutely undertook that I will work with Charles and the Board to make sure the succession is orderly. Hence, it is next year and we anticipate I will still be here, I am sorry to say, at least at the time of the AGM next year.

Now to your important question about strategy. So, we have a new Board, or at least a newish Board. We have three new Executive Directors, a new Chairman and two relatively new non-Exec Directors. So, rightly so Charles said, 'can we just have a look at the strategy and let's kick it about, especially given where we are'. And you have heard the results of it. What it isn't is a change in direction. And one of the conclusions we reached is there isn't a particularly different direction that this company should go in and in fact the skills and capabilities we have got says there is only one direction. Now, when a successor comes in I am sure they will make adjustments, or could make adjustments, but I would encourage you to recognise that once we have sold E&P and Nuclear we are a customer facing company in entirety in energy services and solutions. And I don't really easily see how the direction would be dramatically different to what it is today. That is the only thing I can say to you John.

And on the dividend, I am going to pass to Chris. But I just want to say that we are absolutely committed to and convinced we can deliver a progressive dividend from here and we did indicate why we believe the second half of this year, and into 2020, has reasons for momentum and Chris can talk about, and if he doesn't I will come back and add to it, our future cash flows and how they relate to the dividend, why it is sustainable and why you might see increasing net cash flow into the future. Chris.

Answer: Chris O'Shea
On your first part John, it depends the period in which you look as to what the contribution to the Group's earnings are from Nuclear and from Spirit. You can see that of the £140 million of earnings in the first half, £9 million has been non-controlling interests so you can back over and see roughly what relates to Spirit. Bear in mind that we have a different hedging approach to our partner in some of these volumes. Nuclear delivered no profit at all. I think the 2 to 2.5 pence is high, it is probably I would say 1 to 1.5 pence on average and E&P is very highly taxed, particularly in Norway where it is 78%. So, the bottom line contribution is not as high as you would otherwise think.

In terms of can you expect a progressive dividend into 2020? I think it is too early for us to say. We do see momentum in earnings and in cash flow going into 2020. We won't see the recurrence of the UK one-off price cut of the £70 million. We expect to deliver further substantial cost efficiencies so we say it is a billion pounds over 2019 to 2022, £250 million this year. We expect the majority to be delivered by the end of 2021. So, we should actually see a step up from £250 million moderately into 2020 as you see that coming through. We expect improved profitability in North America business as Iain touched on and we also expect the Nuclear Power Stations, until we dispose of them, to come back on stream.

All of those things together should give us higher earnings. But it is worth noting, we want to grow the dividend in line with growth in earnings and in cash flow and we want to have a cover of between 1.5 and 2.0 times over the medium term. So, it would be unusual on the day that we cut the dividend to announce it was going to rise next year, but it is certainly not our aim to keep the dividend at 5 pence as we go forward. We would like to grow the business, we would like to grow the dividend, but we have to be disciplined and we have to look not only at the current year performance, but also the future prospects of the Group and investment requirements.

Answer: Iain Conn
And if I can just add on cash flow, Chris covered earnings. If you think about, and Chris showed a pretty important chart. I know some people have been writing about us saying, 'what has happened to the £2.1 to £2.3 billion on average that came under pressure, because of the fall in commodity prices and the price cap?'.

If you look at what we are indicating for this year, we are now saying in the bottom half of the £1.8-£2 billion range. So, without giving you a precise prediction, let's just call it £1.85 billion. If you add that to what we delivered last year which was £2.25 billion, you end up with just over £2 billion on average for these two years.

Chris indicated in line with what he just said, with our like-for-like portfolio we would expect higher, all other things being equal, adjusted operating cash flow in 2020, albeit with some continued reduction in structural working capital which can't go on at these rates for ever. But we have always been doing some of that. When you add all that together you can easily get to the maths which is around, give or take, around £2 billion on average over the three years. Now that is clearly below £2.1-£2.3 billion, but it is not dramatically below.

And if I then just turn, because I suspect there will be a question on how does it work for the new company going forward? If you take £1.9 billion in round numbers and you then say two-thirds of that is currently coming from the customer-facing businesses, about a third from Nuclear and E&P, that is about just over one and a quarter billion pounds.

Where are we going to spend that money? We have indicated around £500 million on capital. You can do the math on the dividend, but it is a little bit below £300 million. Pensions have gone up and there will be - we can disclose that? £175 million, I can't remember what was on your slide, and then interest of you know £220 million or something. What does that get you to? £1.2 billion. So, it means the operating flows of the company in this environment, albeit with a small amount of help from structural working capital, will cover the organic needs and contribute to restructuring costs. What we will need to do though is use the divestment proceeds in order to drive and fund the rest of the restructuring and reduce net debt so that the company has the right sustainable position by 2022.

Q3. Martin Brough, Macquarie

Hi, it's Martin Brough from Macquarie. Just following up on the dividend. You have got £2.1 billion of shareholders' equity at the end of the first half in the balance sheet. Obviously there is a lot of further exceptionals to come through. I think you are still carrying about £1.8 billion of book value for the Nuclear stake if I am right. So I would imagine the possibility of some sort of write-down there?

Iain there is quite a lot of out of the money debt. I mean you have got over £4 billion of book value debt and obviously it is as you say 4.9% coupon. So if you start sort of buying that back over time that will be more than the current book value. So are you confident that you are going to get through all this restructuring with a positive net book value? I know that is only an accounting issue, but are you confident the Board is actually going to be willing to sign off on the cash dividends if you end up with negative net book value?

Iain Conn
This must be one for you?

Answer: Chris O'Shea
There are a number of questions in there. So, we have no plans to buy back debt at the moment, so we have some minor refinancing coming up in 2020. The major thing is in 2021 with one of the hybrid bonds, the first call option on the hybrid bond comes up. There are no plans just now to buy back debt.

In terms of the ability to pay dividends with what you look at there is the overall Group number, there are lots of consolidation adjustments. We have over £2 billion of retained earnings in Centrica plc so there is no question at all about having an issue on paying dividends.

In terms of what the Board will sign off on, my job along with Iain, Sarwjit and Richard is to recommend things to the Board and have a conversation, and the Board have shown in my time here a willingness to sign off on things that make perfect sense. So, we do have a lot of restructuring expenditure to undertake.

Bear in mind it is small projects, we can flex it up and down depending on the cash requirements that we have in the business, the business environment that we see and the proceeds we get for the assets. As Iain said it is a 15 month payback. I'd love if we had the investment opportunities, I mean it is the best investment we have in the Group and I would challenge you to see any other investment in other companies with a 15-month payback. So, we do have to balance and naturally I would like to do it all yesterday, but we have to sequence it properly in order to have a strong balance sheet and to get the highest impact restructuring done first. So I don't have any worries about our ability to fund the restructuring, to fund the ongoing capex of the Group, to fund the dividend or to fund the pension payments. I think that is all part of the balance financial framework that we have got.

Q4. Martin Young, Investec

Thanks, it is Martin Young from Investec. I have two questions if I can please? The first gets back to the strategic review that you undertook. To what extend was your continued involvement in the US market put as a question in that strategic review? And if it was can you share some of the reasons why you decided that staying in the US is the best course of action?

And then secondly on the UK supply market. You said a lot about seeking to reduce your cost base. Maybe you could share with us some of your thinking about how the landscape of market participants might evolve, whether you see consolidation and further exit of some distressed small suppliers, increased role for intermediaries, price comparison sites etc? Thank you.

Answer: Iain Conn
Well the second one is clearly for Sarwjit. Let me just address the US question. Firstly, we have got two principle energy businesses in the US: North America Home and North America Business. North America Home has been growing operating profit at over 10% per annum for the last 3-4 years. It is under new leadership and we are seeing quite a lot of momentum. It has been growing customer accounts in both service propositions, i.e. protection plans, as well as energy, and I think that is quite encouraging. It has got good market shares in Texas, in the North East States where it operates and in Alberta.

So, I just want to make sure that when we talk about the US we are not just labelling the whole thing as one homogeneous thing, and it is not only the US, it is also Canada. And I suspect the big question is about North America Business and I tried to go through that in some detail, as did Chris.

Our ownership question in North America Business was clearly part of the strategic update and one of the big questions was if we didn't own a leading market position in North America would we want one? And the answer is yes, for the largest energy market in the world and the largest market for distributed energy technologies in the world. But it can't be unconditional, and the thing that has been plaguing us has been, in the last two years for sure, the return on capital employed in North America Business.

Hence, you see what I described earlier which is the interventions we need to make in order to improve North America Business's returns. If we can get to 10-12% returns through the cycle and limit the downside to cost of capital and we can continue to upsell distributed energy propositions, then it is obviously in the shareholders' interests to keep it. But if not, we will have to ask the question again.

I might ask Richard briefly just to add if there is anything else you want to add Richard about that and then pass to Sarwjit on the UK market structure?

Answer: Richard Hookway, Chief Executive, Centrica Business
No, I mean as Iain said, we did have the conversation. We had a plan in place to address the issues that we have seen over the last couple of years. The team and I are absolutely determined to see those through. It is a combination of actions to reduce the denominator, the capital employed. We have got actions underway to address the numerator as well. More costs can be taken out of the business. We are addressing gross margin and some of the issues we have had there in terms of the shortfall. And if you put all of those things together, we are confident that we will get to those low double digit returns through the cycle.

One other element you have to remember on the gross margin is that average contracts are around 2-3 years, so it takes a little while for some of those issues to work their way through the system. We are starting to see that in the forward book for the second half of 2019. That is why I have confidence the second half will be better than the first half by some considerable margin and that 2020 will be better than 2019, and 2021 will be better than 2020.

Answer: Sarwjit Sambhi, Chief Executive, Centrica Consumer
So in terms of the question, you know, how do we see the supply market shakeout over the next few years? I think our view is that there is going to be consolidation, but you are going to have, potentially, the share of the big six reduce, particularly those that don't address their lack of cost competitiveness and their customer service.

On the smaller suppliers, we have already seen in 2019 three exits and the three exits have either been because they have hit a liquidity crunch or their service is poor. But I think in terms of, there are some small suppliers out there that will be successful and will grow - their limitation will be what do they do beyond energy? And, you know, that is where our kind of strengths play into winning. When we address our cost competitiveness, when we improve service levels even further so that we can expand into not just energy but do more of what we are doing today, which is to bundle energy with other services.

We have already shown in the first half that we have reduced, over the last two months, losses in energy and grown services because of the bundles which are attractive mainly to new-to-brand customers. So, the new-to-brand share is about 70%.

So as the market unfolds we get more cost competitive and it is not just about taking out costs using current industry processes. One important bullet point on Iain's chart on the actions was saying we have got to move to end-to-end journeys for customers and not create our business around industry processes. That is where some of the smaller suppliers, not many, but some of them are being really successful. Not only does that create a great customer experience, but they can do it at a much lower cost.

So how is it going to shake out? I don't think all of the new entrants will survive. I think there will be consolidation, but there are a few that will be successful.

Q5. Iain Turner, Exane.

Hi, it's Iain Turner from Exane. Can I ask about the disposal of Spirit and the SWM statement? To what extent that complicates, do they have pre-emption rights or tag along rights?

Answer: Iain Conn.
So Stadtwerke München, first of all naturally I alerted them to our likely decision. They are aligned with us in entering a process. They do have rights to stay in and we can't drag them into it, but they can tag along with us. So, it is very early days. As a company they are owned by the City of Munich. They are going to need to go through a process, but we have got a very constructive relationship and excellent conversations on it. And I think they understand the value trade off potentially if they stay in and the uncertainty around having a different shareholder partner. But at the same time, they want to see how the process of also. We are going to be going ahead on the process with them.

Q6. Chris Laybutt, JP Morgan.

Chris Laybutt, JP Morgan, good morning everyone. Two questions from me. First of all, your investment requirements for new Centrica. You are talking about a figure of £500 million. Could you provide a rough breakdown of that? What do you intend to spend that on going forward?

And then in terms of the deficit repair, would you give us an idea for your sense of how long that will continue, some clarity there?

And if I can throw in a third one, a very brief one? In terms of politics any views on the new Tory Government and - I guess I will leave it at that.

Answer: Iain Conn
I'm glad you didn't finish beyond the 'and'. So very briefly on the first and last, I will leave the deficit repair to Chris. £500 million very roughly is about £100 million of ongoing capital requirements just to continue with replenishing the existing capital base. About £200 million of IT, this business is increasingly becoming digital technology heavy and less physical capital heavy obviously. And the other £200 million is for proposition development and for deployment into distributed technologies with our customers and potentially small capacity building acquisitions, but obviously we will only do that if we are able to afford to do so.

And on the politics, look, I said this morning on the radio, I am hopeful. I think the last Tory Government got itself a bit tangled up in interventions in free competitive markets and unfortunately our market was the one they chose to target first. I think it had shockwaves across many markets and a lot of people wondered about investing in the UK on the back of it. I get the impression that despite some flowery language about business in the past that the new Prime Minister actually is quite keen on competitive markets and understands what is at stake if we exit the European one way or another. So I am hopeful, but politicians are a whole other breed of people and I will wait and see I suppose is the best answer. Chris?

Answer: Chris O'Shea
So the pension deficit recovery period is under 8 years. Obviously, we do a valuation every three years though. And one of the reasons we are derisking the portfolio in conjunction with the trustees is to reduce the value at risk and therefore reduce the chance that you will see huge spikes in the volatility. So less than 8 years, 223 this year followed by 175 per annum to extinguish a £1.4 billion liability.

Q7. Fraser McLaren, Bank of America Merrill Lynch.

Good morning, it is Fraser McLaren from the Bank of America Merrill Lynch. Three very brief questions please. First of all, what happens if you can't sell Nuclear in 2020 because, for example, Hunterston remains an issue or if E&P fetches a lower than expected price? Would either of those be enough to actually derail the plan?

Could you also clarify please where we are with the Hurricane JV exploration, how many wells are left and when are the results due?

And then finally just a point of clarification on energy accounts. I think Iain you mentioned that churn rates have halved in the period, is that right? And could you also speak please about the margins that are available on the new accounts that you are gaining? Thanks.

Answer: Iain Conn
I am going to leave the last one for Sarwjit in terms of margins, but what I did say was that the 178,000 energy losses in the first half this year was approximately half the 341,000 in the first half of last year. So that is roughly half.

What happens if we can't sell? Well firstly, we are pretty confident we can sell. I mean both E&P and Nuclear. There is a very free market for exploration and production assets. There is a lot of consolidation going on. We see absolutely no reason why we can't sell in a trade sale.

On the Nuclear, there are obviously complications with Hunterston and Dungeness, but right now I mean the last delay was two weeks as opposed to three months. And as long as these come back up in the second half, just given the constructive nature of the conversations we are having with two groups, I believe - I have got confidence - we can execute certainly the first tranche of this if not, you know, if not all of it by the end of 2020. And I personally don't believe this will derail. I mean clearly if we couldn't, I have just explained that the organic cash flows would be enough for the future organic activity. And the operating cash flows of Nuclear and E&P can fund their capital requirements. So, what it would prevent us doing in an extreme case is driving the restructuring as fast as we would like. But capital expenditure as I just indicated and restructuring expenditure are both variable. But we see no reason why we can't make this portfolio change and obviously the main decision with the Board was, is this the right thing to do? And the answer is, Centrica is strategically not sufficiently coherent in its current form, therefore we have to make these sales.

Hurricane very briefly, the second well is being drilled at the moment. The first well did encounter hydrocarbons just at disappointing rates to the surface. And we will know more in the next couple of months about that second well I suspect and then we have the third well to drill in the back half of the year. So, we will know an awful lot more in the rest of the year.

Sarwjit, accounts?

Answer: Sarwjit Sambhi
Yeah so two parts of the question. On churn, Iain has clarified the kind of statement of halving. But I think it is important to also note that if you compare H1 '18 with H1 '19, the market overall has seen switching increase by about 17% and if you put aside acquisitions, we have seen the churn in our book actually reduce by almost a percentage point.

So, there are two things, one is we are able to kind of sell into a market and acquire new-to-brand customers, and we are demonstrating that all the activities that we have been undertaking to retain customers, such as rewards, is working.

In terms of what we are selling to new-to-brand customers and also existing customers who may switch a tariff, it is a mix. You have got some fixed term contracts, which are British Gas branded, which are priced pretty close to SVT. You have some online only offers that are lower in price than SVT, but have a similar margin because of the online nature of the product. And then in terms of the lowest margin, the bundles for the energy leg in terms of margin are very low. But, in terms of overall customer lifetime value they are positive and they are also kind of positive from day one from the services point of view because they have a very low marginal cost.

Q8. Ahmed Farman, Jefferies

Ahmed Farman, Jefferies. I just want to start with your comments about the disposal programme. I just want to understand a little bit better how that ties in with the growth aspect of the dividend policy, because you talked about that being a critical part of bringing down the debt and funding the restructuring costs. So I just want to understand that a little bit better?

Chris you earlier mentioned the EPS dilution, can you give us an indication on the EPS dilution from the disposal? Could you give a bit of a sense of the free cash flow disposal dilution from Nuclear and E&P?

And just finally could you give us an update on where you are in the Nuclear disposal process? Thank you.

Answer: Iain Conn
So on the growth of the dividend, I think we indicated that from 2022 we should see significant expansion of net cash flow and that is the thing that I believe you all need to hold on to. And, we have the potential of the organic business to deliver more operating cash flow than is needed for all of its needs and make a contribution to the restructuring in the meantime. But we will want to use the divestment proceeds for the rest of the restructuring requirements and of course to pay down net debt. But by 2022, and potentially earlier, there should be expanding net cash flow, but as Chris said that is a question for the Board later on.

What was your third point?

Ahmed Farman
Nuclear.

Iain Conn
On Nuclear. I mean obviously we can't talk about divestment conversations in detail, but as I said earlier we are in conversations with, advanced conversations with, a couple of groups about taking the Nuclear stake and it is going very encouragingly. But I don't want to say anymore because these things can trip us up. Chris, EPS dilution?

Answer: Chris O'Shea
Yes, so on the free cash flow dilution, an essential where we get our money in Nuclear is from the dividend so you can see that quite clearly. You can also see in the Release today, you can see our adjusted operating cash flow from E&P is £433 million, so £157 million of tangible capex, there is £74 million of intangible. So there is about £200 million of free cash flow in there from the E&P business. Now that goes up and down depending on the capital investment. That is £230 million of capital investment which is probably a bit on the low side for Spirit. So you are probably looking at a few hundred million pounds, but it really does depend. I mean if you think about for example in a Hurricane success scenario, Spirit is going to substantially free cash flow negative probably because it has been a big success and that will be very expensive to develop it. So it really depends on what the prospects for the business are.

Q9. Elchin Mammadov, Bloomberg

I have two questions. The first one is on E&P. When you presented your strategy in 2015, it was still maybe not the central part, but one of the core areas, what has changed between 2015 and now that you want to sell that business?

The second question is on the Connected Home business. You said that you struggled to grow outside UK and Ireland. Can you talk a bit more about why? Yeah and that's all.

Answer: Iain Conn
I'll let Sarwjit do the second one. I did try and outline the differences geographically.

But on E&P actually in many ways nothing has changed. We indicated in 2015 that we were going to de-emphasise E&P and we indicated that we would retain a limited scale E&P business for reasons of cash flow diversification and balance sheet strength. The judgement we have had to make now is do we have sufficient capability, albeit with a rebased dividend, in this current environment to actually separate from E&P and get to where we need to get to as a customer-facing business? I don't think we could have easily done that in 2015. So nothing has changed, but we have now crystallised the decision.

And to your point about current prices, most people value E&P assets on through cycle commodity prices. And so, people will look through the front end, especially when you look at the commodity curve in the liquid period, it is rapidly accelerating even to this winter. So I am not too worried about that. Sarwjit, Connected Home?

Answer: Sarwjit Sambhi
Yeah so in terms of why we have made the decision to focus just on UK and Ireland and withdrawal from outside of the UK and Ireland. If we look at the UK, the reasons we have been successful is largely because of our routes to market and there are two aspects to that. We have millions of customers that we can market the product to and we have an advantaged channel that does two things. One is our engineers are great ambassadors for Connected Home products. Two, they install them and that is something that, all of that we can't easily replicate in other geographies. So the review said, look we have tried in North America but when we look at what has truly made it work in the UK, you know we can't find a way of easily doing all of that in another geography. So I think the strategy is, let's refocus back on home turf and focus on a narrower product set, home energy management remote diagnostics and monitoring. And also have a quicker path to profitability.

Q10. Dominic Nash, Barclays.

Hi it's Dominic Nash, Barclays. Two questions please. Firstly, on the pension deficit. Could you just tell us the quick difference between the IAS19 and the £1.4 billion, what are the main differences there?

And is there any risk that the Trustees will ask for some of the proceeds of your asset divestments to repair the pension deficit?

And secondly, on capacity payments. Could you just summarise how you have treated that in these half year numbers both on the accrual for the generation but also the cash that you have taken on on your retail side as well please?

Iain Conn
Chris, both for you.

Answer: Chris O'Shea
So the capacity market challenge is, we have been consistent with what we did in the second half of 2018, which is we have assumed that the capacity market is reinstated. So we collected the money from our customers, we have kept that money, we haven't paid it over to anyone yet. But we haven't recognised that profit in the downstream business, so in the supply business. We have assumed that that will be paid off. And we have also assumed that the generation businesses will receive that

income. So essentially we have recovered more cash than we otherwise should have by about £40 million. We carry a provision on the balance sheet for that. We expect to pay that to someone, we just don't have anyone to pay it to at the moment, but it is fully consistent with the second half of last year.

On the pension, the big difference between the accounting deficit and the technical provisions deficit is the discount rate at which you discount the future liabilities. So for the technical provisions deficit you take Government bonds, make some adjustments there for the accounting deficit, you take, you are supposed to take good quality corporate credit which is, the proxy for that is AA rated bonds. So AA rated it shows in the UK and that is the main difference to the £1.2 billion there.

The risk of the Pension Trustees. So hopefully, we signed the agreement last night, so I am hopeful and they know what we are going to announce, so I am hopeful that they are not going to be on the phone at the moment. But I mean the discussions we have had is they look at the strength of the company and if we have assets of X billion today and tomorrow we liquidate some of those assets and keep the cash in the balance sheet, then the strength of the company is exactly the same tomorrow as it is today. The question is what you then do with that money? So the act of selling an asset shouldn't trigger, and actually doesn't trigger, a contribution into the pension scheme. But if we're ultimately to sell and simply sit on lots of cash and see a business that doesn't grow in any way then the Trustees would clearly come and talk to us. We have constant dialogue with them, we have the triennial valuation every three years. Yesterday when we shook hands on it last night, that is 19 months since the last one, so we will start again in a couple of months in the run up to the next valuation. So it is an ongoing conversation, they are an important stakeholder, but as long as we use that money wisely I don't expect the need to put any of that into the pension scheme and that is the basis of the discussions I have had with the Trustees.

Q11. Mark Freshney, Credit Suisse

Hi, it's Mark Freshney from Credit Suisse. The question or two questions for Sarwjit. On price caps, I mean you have got an important change coming through and the CMA are looking to roll over the pre-payment cap into the default tariff cap, we should expect some adjustments for the metering costs? Given how sensitive your margins are to small changes and policy as we saw with the £70 million, how confident are you that the price caps when we see them next week will be fair?

And further to that, I mean the writing is on the wall, the cap is likely to be extended past 2020 certainly for pre-payment meters probably for default tariffs as well, you know what is your view on the long term? I accept it is early stages with the current Government, but do you think it is plausible, I mean would a base case be that that cap should be on forever?

And then I guess finally, long run profitability in British Gas residential, I mean we have seen the cost cutting that you have got on the cost to serve, but where do you think margins could be in 2022?

Iain Conn
There is a lot in there, Sarwjit.

Answer: Sarwjit Sambhi
So I mean the first one is factual. We will find out on 7 August from Ofgem as to whether they make the adjustments that they have consulted on, or that the CMA has consulted on, for the pre-payment cap. Our expectation is that they will and therefore we will see the new pre-payment price cap reflects that and I think there is nothing more today on that apart from waiting until the 7th.

On the price cap removal, I mean you have said it yourselves, it is very uncertain given the current environment. It is not necessarily top of the political agenda. But what I can say is that you know Ofgem are asking the question, what would be the conditions for the removal of a price cap and that is a kind of a very complex question because it plays into demonstrating that the market is competitive, demonstrating that there is engagement in the market. And I think there is a third big one that is pretty high up on the agenda: making sure that customers in the market who are vulnerable or can't participate in the market aren't treated unfairly. So I think that will be an important factor into any discussion around conditions for removal of the price cap.

On the third question of where do we expect margins to go? What we have said today on energy supply and saying we want to be the most competitive you know is really important because as Iain described, it is not just about becoming, as you know, the best of the big six or the eight largest suppliers, it is truly about becoming as cost competitive as anyone in the market. And that requires us to do two things: changing the way that we do business, moving away from the industry processes and designing your business around following a meter read to actually designing your business around the customer, and making your IT stack that you run your energy business on more flexible and lower cost. If we do that and we get to the cost levels that Iain described, with our scale, that is hard to replicate. So you know in terms of your question, the strategy is actually we want to make sure that we can be the most competitive and beat average industry margins. We already know that, in terms of the current price cap, that if you set the average of what is currently the EBIT factored into the price cap, you are just under 3%. So if we become as cost competitive as we can be, you know that is the target to beat.

Answer: Iain Conn
Mark, just on your Ofgem point, I mean in my discussions with them there is a recognition that the price cap needs to be temporary. So I have the opposite impression. But the difficulty as Sarwjit said is the conditions precedent for lifting it and how do you operationalise that.

Q12. Deepa Venkateswaran, Bernstein.

This is Deepa from Bernstein. Sarwjit you have mentioned a lot about this fundamental reset to UK energy costs, so I just wanted to understand restructuring costs, because I don't see those costs captured in the ongoing capex of £500 million. So should we understand that there is restructuring of I don't know £1.3 billion that captures everything you need, whether that is the IT stack, changing the ways of working, is that all-inclusive or is there anything more to come?

And then I guess another question to Iain is really when you are looking at the E&P sale you do need to retain the cash in the balance sheet so that is not ideal. So did you look at anything more dramatic as sale of the entire company where shareholders could realise more value? Because here, although you would sell E&P, for shareholders that is going to be a line in cash not earning too much. So was there another way where you could have sold everything but preserve more value, or indeed generated more value?

Answer: Iain Conn
Firstly, on your first question, and I actually think it is a Group level question, which is the £1.3 billion isn't all down to, it is not just in UK Home, although a lot of it is. And so just on the Group question, I mean clearly we are not expecting to fund all the restructuring from within our organic flows. Although that little maths thing I did earlier demonstrates that the new company should be able to contribute to the restructuring, what we don't know is how much it can contribute. And I indicated it will be able to contribute some. And as I tried to indicate as well, there are choices about the phasing of restructuring. Sarwjit, anything you want to add to that in terms of from a consumer perspective?

Answer: Sarwjit Sambhi
Yeah I think in terms of some of the investment required, for example in technology, part of that, not all of it, we expect to be self-funding as well as we prioritise not investing say in the current stack to take funds away from that to invest in new technology. That is another lever that we can pull as well.

Answer: Chris O'Shea
To be clear with your question, is there more cost over and above the £1.3 billion and the £500 million capex to rebase? And the answer is no. So within the capex envelope and the £1.3 billion, that covers everything we want to do with the Group. There is no additional cost to fundamentally rebase UK Home.

Answer: Iain Conn
And on your bigger question, look, clearly the Board, we have considered everything in the interest of our shareholders. We believe the right answer just like the question on North America is as we have laid out. We think it will ultimately maximise shareholder value and that we can grow the company from the rebased place. But it is a very, very difficult set of circumstances that we are in and as I said at the beginning, the energy transition and the dramatic changes in a regulatory and commodity price sense clearly are not what this portfolio as it currently stands is ideally suited to. And we know that we are chasing a moving target around competitiveness and actually we have made a lot of progress on it and we have been able to underpin all the degradation in underlying margin, but we can't deal with things like this price cap at this level overnight. So my answer to you is, yes of course, it is a strategic update. We have considered all the options that the company has at its disposal. We believe as a Board this is the right course of action and I think I can speak for the Board, Charles, that it is as simple as that.

Ladies and gentlemen, I don't see any other hands and – oh, there is one more and this has to be really short.

Q13. Sam Arie, UBS.

Hi, Sam Arie from UBS. I thought I would just jump in because I had a follow-up question that was connected to Deepa's actually, I think.

And you are saying that you have looked at all the options earlier in the presentation, you said you felt there was only one strategy for a future management team to follow. I suppose in the mix between what you are proposing doing and what Deepa is asking about in the whole company, there is another option which would be to start divesting what has always been considered the core business of Centrica, which is British Gas. And if I think about the sort of 20-year strategy, history of British Gas, of Centrica, as I have always understood it you are building these other businesses around British Gas to provide the financial strength and support, the credit metrics and the hedging requirements of that business.

What you are explaining today is that becomes increasingly difficult to do as you have to divest the sort of flank of businesses. So is there an option did you look at where you would actually move on from British Gas? That British Gas be owned by a larger company perhaps without the same credit rating challenges and strip Centrica down to something much smaller, more geared to the climate change trends that you are talking about with much higher potential growth rate?

Answer: Iain Conn
What we have done clearly is look at what we think is right for value creation for our shareholders and that is what this Strategic Update represents. No one can ever rule out industry consolidation. It is not something that we are currently pursuing. No one can ever rule that out and no one can rule out that portfolio questions such as the one raised in North America might not come back if we don't get the returns up.

But we have been really clear after six months of very intense work that clearly I have not been trying to push that there is only one answer. The Board has concluded this is the right answer. But it is not an easy path, it clearly isn't. There is more restructuring to do because the world of energy and services is changing really dramatically, and we have to move there.

The good news is that if you look at the cost efficiency we have delivered already and the restructuring we have delivered, by the end of this year it will be £1.2 billion out of the £2 billion. The people I care about the most are Centrica's employees and colleagues who are having to go through hell and back to deliver all of this. But you have my commitment as long as I am here, and I am not planning on walking out the door tomorrow, that we are going to deliver on this. And actually, irrespective of the other options that you and Deepa are saying, why haven't you considered these? Everything we are talking about today is good for all seasons. And so we need to get after it.

Last question and then I am going to summarise.

Q14. Siddarth Sukumar, JO Hambro

Siddarth from JO Hambro. I am just trying to understand the role of your energy trading business going forward and particularly the contracts that you have signed in terms of Mozambique and Cheniere. I notice that the spreads since the date they were signed have narrowed. So how do you view this in terms of the value that it brings to your organisation?

Iain Conn
Richard, brief answer on that one.

Answer: Richard Hookway
Yeah let me address the LNG portfolio. I mean clearly you are right in that gas prices have become depressed over the last period and hence spreads are compressed. But as I said back at the time of the Preliminaries in February, we have pretty much tied down 2019 and 2020, we have got about 9 cargoes this year and we have got about 29 next year. Almost all of them are contracted away. Some have got options as to what we do with them. And almost all of the numbers, again something I said back in February, almost all of the numbers I have written in black rather than in red, so that is looking good.

As for general markets, they wax and wane. The gas price is low at the moment but won't be low forever. The fundamentals behind LNG demand, in Asia for example, supply nodes out of the US and particularly Mozambique which geographically is extraordinarily well positioned, will come into their own. There will be profitable arbitrage opportunities, which when they occur will lock them in.

Your broader question about the role of trading is of course both to support the downstream businesses with their hedging, their risk management activities, but also to add value through optimisation on the back of those positions that are created and providing additional services to customer like the 24GW route to market services that Iain mentioned during the Presentation.

Closing Remarks

Iain Conn
Thank you Richard. Ladies and gentlemen, it has been a long 2 hours and 15 minutes. I appreciate you participating and listening. Just a couple of points in closing. This is an exceptionally challenging set of circumstances for this company and I regret that hugely. I and many others tried very hard to stave off this price cap in the UK which has clearly done in one step a very significant amount of damage to our gross margin which we then need to take some further steps to try and underpin through cost efficiency.

And I also regret the fact that the commodity prices are behaving in a very strange way where we have now got natural gas prices below our lowest case we imagined in 2015 and crude oil back at 63 dollars a barrel. And then you have got all the other issues we talked about earlier. It is an extremely difficult set of circumstances.

Second thing is I regret deeply the dividend cut. We know how material it is and you know I have defended the dividend for as long as I could. But in this set of circumstances with the pressure on our cash flows, we just cannot. And it is absolutely the right thing by the Board to rebase the dividend to a place which we think is sustainable in the long-term even in very challenging circumstances. And we have gone through why we think it is sustainable and also why we think we can expand cash flows and earnings to make it progressive.

Thirdly, I believe the steps that we are taking are the right ones and they are the final stages in turning Centrica into a coherent energy services and solutions company and that is what we envisaged back in 2015. And you have my commitment, obviously, to finish the job.

And then lastly, the Board does believe this is the right direction. It plays to Centrica's skills and it is in tune with where the world of energy and the energy transition to a lower carbon future is going.

Thank you very much indeed for spending the time and look forward to interacting with a number of you over the next week or so. Thank you.

End