Sainsbury's Supermarkets Ltd
Second Quarter Trading Statement - Transcript
08.30am, Wednesday 28 September 2016

Mike Coupe
Chief Executive
Good morning everyone and welcome to the Quarter 2 Sainsbury's Trading Update Call. I am joined by Ed Barker, our Interim CFO. As you are aware John Rogers has moved to a new role of CEO of Sainsbury's Argos. Ed will run through the highlights and then I will hand over the call for the Q&A. Ed.

Ed Barker
Interim Chief Financial Officer
Thanks Mike, morning everyone. I will take you through the financial highlights for the Second Quarter. We have made continued good progress against the strategy we set out in November 2014. Total ex-fuel sales were down 0.4% in the Quarter. Like-for-like ex-fuel sales were down 1.1%, reflecting of course food price deflation which we are measuring at around -1% in the Quarter. And we achieved again like-for-like transaction growth across all of our channels so that is supermarkets, convenience and online. And total volumes across the business are also up year-on-year.

We have also made targeted further price investment in everyday low prices with another round of price cuts at the end of August, focusing on those products that matter most to our customers. We continue to invest in the quality of our products and earlier this month we launched our new On the Go range of sandwiches, salads, sushi, snacks and drinks.

General merchandise has grown over 4% and the Bank continues to deliver a good performance.

Convenience and online both performed well, convenience growing nearly 7% and online growing 8% with orders growing close to 12%.

And of course we completed the acquisition of the Home Retail Group on 2nd September. Although Sainsbury's did not own the business, we are announcing today the Argos Second Quarter performance for the thirteen weeks to the 27th August. Total sales growth of 3% and like-for-like growth of 2.3%, both of those of course ex-vat numbers.

As you can appreciate, we have only owned the business for just over three weeks now and the period we are referring to there is a period before we took ownership of the business and with time we will give you more detail on our thoughts and plans for Argos and the wider GM business, but we are not going to say anything more on the performance today. We will have 30 Argos digital stores within Sainsbury's stores by Christmas. We will also have 200 digital store collection points, Click and Collect points within our supermarkets by Christmas and we will have five mini-Habitats in our supermarkets probably by year end rather than this Christmas.

Finally, but importantly, our in-store operational metrics continues to improve and we were recognised by winning the Grocer 33 Service and Availability Awards for the 4th consecutive year.

So overall a solid performance for the first half, continued execution of our strategy. And with that, I will hand over now to questions.

Q&A Session

<u>Question 1</u>

Bruno Monteyne, Sanford Bernstein
Two questions for me so there is fall in growth in the UK market, I guess most talks of about 1-3% and we have not that much space coming in. You are having a small nugget of volume like-for-likes. So my first question really is, where are those, why are those volumes below the market and who are people switching to if that is the case? If you compare that performance versus Morrison's and Tesco?

My second question is around your different approach to promotions, I mean it has been quite radical and persistent for the last year, less promotional, simpler, clearer pricing, no more multi-buys. But is there a risk that the consumer got used to that about you guys leading the market instead of losing out on potential volume and trade? Thank you.

Answer: Mike Coupe
Hi Bruno. Yeah on the market performance we would stand by what we said previously. If you look at our market share over let's say the last year, we are the only one of the big grocers broadly speaking to have maintained market share so we are pretty pleased with that performance. Of course there are ups and downs in any given quarter and that has always been the case. And we have also highlighted the fact again, as you have pointed out, that we have seen volume growth during the quarter. We have also seen transaction growth. So these things bounce around as they always do. People tend to fixate on the quarters, but we stand by our track record of outperforming the market consistently, not just in the last year, but actually over the last 4,5,6,7 years.

As far as promotions are concerned, we have seen promotional participation in the Quarter around 25%. It is a little bit higher than the previous quarter, but if you look at the sort of previous years trends, you can see a step up in most numbers of that promotional performance and we again will stand by what we have said we will do, which is continue to invest in everyday low prices. We think that is an important part of our long-term strategy. And that is something we have done consistently now for probably what three years. Of course all the time we are asking the question that you have asked, which is, where is the boundary and clearly it has different impacts on different categories. We have also taken a lot of the promotional noise out of our business. So again if you look over the last year, reduced the number of Nectar points, taking out Brand Match, reducing the number of multi-buys. All of those things to your point are quite radical moves. But we think it is right to move the business towards a longer-term more sustainable price position and in particular to close the price gap relative to the discounters. And that is what we are focused on doing.

Further question
Coming back to that first point, indeed I understand the longer-term picture, Sainsbury's has done fantastically well. And so the last quarter of data does not unduly worry you is basically as a message that it has to be seen in the broader perspective? Is that the right way of summarising your view on that?

Answer: Mike Coupe
That is the right way of summarising, but even in the last quarter, you take the last twelve weeks, Tesco have done a little bit better than we have done, but actually we have been second in terms of overall market share position. So these things do bounce around. Other businesses in various particular cycles of recovery, but actually if you go back to the underlying point which is this isn't a sprint, it is a marathon. It is a long-term game, we stand by our track record over many years. Of course in any given quarter there will be ups and downs.

Further answer: Ed Barker
Yes Bruno also useful probably just to break out a little bit more our Q2 numbers, so the Q2 like-for-like at -1.1 versus the 0.8 in Q1, so slightly down but food price deflation, we are still measuring at around 1% as part of that. Probably slightly higher in Q2 than in Q1 and non food of course a little bit slower in the Quarter given the impact on clothing, particularly that we are reporting today. So from this you should be able to work out that our like-for-like volume performance overall and for food specifically was probably slightly better in Q2 than in Q1, but still very slightly negative.

Bruno Monteyne
Thanks.

<u>Question 2</u>

Niamh McSherry, Deutsche Bank
Hi, I just had a very easy one on contribution from space which at 0.7 was below kind of your full year guidance and below last quarter. So is the guidance of about 1% for the year still in place? Should we expect the contribution from the space to accelerate next year?

Answer: Ed Barker
We will update more fully at the Interims Niamh but you have to remember we are a little uncertain on the timing of selling our Pharmacy Business and of course the Pharmacy Business sale has come out, that happened about 3-4 weeks before the year end. That will have an adverse effect on that new space number, but we will update you at the Interims of our outlook for the full year.

Niamh McSherry
Okay, thanks.

<u>Question 3</u>

Andrew Gwyn, Exane
Hi, I will ask about consensus. So consensus for the full year and consensus in the first half, I wonder if you had any views or loosely where people are or where we should be?

Answer: Mike Coupe
You know that this is a Quarter Two Trading Update. You know that we have got our Interims in 5-6 weeks and we are fully aware of any responsibilities we have. So we can go no further than that and would go no further than that on a Trading Call.

Answer: Ed Barker

Yeah I think the only thing we would add is you know the consensus on our website was code compliant up until the transaction date so it is very up to date. The only other thing to point out is that consensus is a Sainsbury's only consensus.

Further question
And that says 517?

Answer: Ed Barker
That is what the average of the range is currently, yes up on the website, quite a wide range around that.

Further question
Just on a broader question then, I mean market conditions you have obviously mentioned a little bit of your own price investment at the end of August, is there anything exciting going on in the market at the moment? Obviously we have had some noise from Asda but not really much action as far as we can see certainly. I just wondered what your take on the market is at present?

Answer: Mike Coupe
I think it is a continuation of the trends that we have seen, not just in the last year, but probably the last 2-3 years now. You know the market continues to be in a deflationary cycle. The volumes have already been observed have come back to the market in terms of a little bit of volume growth. But that is the critical dynamic that has driven the underlying challenges of the industry. But it does not feel like things have radically changed from where we were in the last quarter, certainly nothing that we have seen that would indicate that there is a radical shift in strategy of any of our major competitors.

Further question
Okay, that is clear. And finally on Argos, when are you going to be in a position to communicate more. You said you would, I am just wondering if you could give a time scale or should we wait to the full year results or are you going to say more at the Half Year?

Answer: Mike Coupe
No you understand, we are three and a half weeks in to owning the Business, so very early days. We have actually given quite a lot of detail if you go through all the prospectuses around some of our intentions. So we would refer you back to some of the documentation that is already out there. But we will give a much more detailed overview of our intentions when we get to our Interims in November. So five or six weeks down the track, that is all you have to wait. And as you can understand, as I say we are only three weeks into owning the business so very early days.

Andrew Gwyn
Okay, no time at all, thank you very much,

<u>Question 4</u>

David McCarthy, HSBC
Morning. Just a couple of things. One is you say you are uncertain on the impact of sterling. Can you explain where your uncertainty lies? Is it around the extent of the increase in costs that it is going to bring? Is it around your ability to pass it on? And are you more uncertain around the supermarkets than around Argos?

And then a second question, can you give us any update on the operating costs inflation situation? You know is that the same as you have guided previously and are we going to be living with adverse differential inflation going forward throughout the rest of this year?

Answer: Mike Coupe
I'll have a go at the first bit and Ed can have a go at the second bit. I guess without being glib Dave, all of the above in terms of your list. First of all, clearly currency movements have an influence on input prices, but equally you can see that there is some commodity market shifts as well. So if you take fuel as a good example, a real example. Although there was a devaluation of the pound, you also saw oil prices fall and therefore the kind of subsequent increase, slight increase in fuel prices was nowhere near as high as you might have expected on the basis of the devaluation of the pound. You have seen this year the harvests look like they are going to be pretty good, so it looks like there is a downward pressure on commodities like wheat. So again not necessarily offsetting completely the deflationary effects, sorry the inflationary effects of the pound/dollar exchange rate. But nevertheless having some mitigation. I read in the newspapers this morning that the price of coffee is going to go up. So the other way there is going to be pressures on the upside. And of course to your point, any pressures either way it is difficult to tell until it happens as and when these things will get passed on to consumers. As I say, whether it is on the downside or the upside. So I think it is uncertain. I don't think any of us could put our hands on our hearts and give you any sense of predicting what may or may not happen over the next period of time. But I don't think it is purely about, or it isn't purely about the effect of exchange rates, there are other factors, not least the movement of commodity prices which will have an influence.

Further question
So what about the impact on Argos then because presumably that is going to be you know a little bit more certain in that you have not got the vagaries of the commodity prices and harvest?

Further answer: Mike Coupe
Well I think I would refer you back to the Statement that was made by their business at the time. So if you want to look up what John Walden and Richard Ashton said about their position on hedging, I think they were pretty clear. And of course whatever applies to Argos also applies to the rest of the marketplace. So the idea that Argos is somehow different to any of its competitors in terms of the impact that any form of currency movements may have just isn't true, I mean it isn't factually right. So I would say, point you to the Statement made by Argos themselves pre the transaction and firstly and secondly, whatever pressures there are and whichever direction, aren't just exclusive to Argos, they will also apply to other players in the marketplace. And as we have said already, we will give you more colour when we get to the Interims. So we will be in a position, hopefully to give you a bit more explanation beyond what we have put in the prospectus about our intentions and how we intend to execute and how that will play out over the next period of time.

David McCarthy
Okay thanks.

Further answer: Ed Barker
In relation to your second question, Dave, we are not going to be updating guidance or commenting on profitability, this is a Trading Statement only today. We will update on that at Interims and therefore refer you back to the guidance that we gave at Prelims where cost inflation was expected to be at the lower end of our 2-3% range.

Further question
So you do anticipate adverse differential inflation continuing therefore?

Answer: Ed Barker
Well until we update at the Interims for any further information, we will stick to the cost inflation, yes we will have a cost inflation coming through at the bottom end of that 2-3% range.

David McCarthy
Okay, terrific, thanks.

<u>Question 5</u>

Edouard Aubin, Morgan Stanley
Good morning guys. Just two questions for me. First of all on Convenience. I think Mike in the first quarter you mentioned that like-for-like turned slightly negative for the first time in a while. Was that the case as well in Q2 are they negative as well?

And my second question, I know you don't want to talk about Argos, but just a technical question. Have you changed the way you calculate your like-for-like sales there? I ask the question because the net new space boosted sales by around 2.8% on average over the past few quarters as Argos rolled out concessions. In this quarter it looks like the benefit was only 0.7%. So is that due to closure of concession at Homebase or is that due to change in that ability?

Answer: Mike Coupe
Well I will answer the first and Ed can answer the second. So Convenience like-for-likes were positive in Quarter Two, up 0.6% against down 0.7% in Quarter One, so relatively speaking the Convenience business is better than it had in the first quarter.

Answer: Ed Barker
Yeah and in relation to your second question, no change in calculations as part of that and again we are not going to comment on the Argos performance, but I would just refer you back to their Q2 last year. You will see that there was a really big space put down in their Q2 last year in terms of the number of instore concessions that were opened and that will probably have the major effect on what you are seeing as the switch between new space.

Edouard Aubin
Okay, thank you.

<u>Question 6</u>

Rob Joyce, Goldman Sachs
Good morning guys. I have got sort of three areas from me, should be brief. Inflation wise, are you seeing on the food side any cost price inflation or deflation? And does that mean if so your higher level of deflation in this period means you are investing a bit more in price?

Answer: Mike Coupe
We don't again break out the specifics of our price investment and I will refer you back to what I said earlier. I mean there are movements in both directions on commodity prices and clearly exchange rates have an influence on that and we will see how that plays out over the next period of time, both in terms of cost price

pressures either way and subsequent retail movements on the back of them. So you can see from what we have said that broadly speaking the business is tracking where it was in Quarter One. I don't think there are any significant movements that I would point at. And I certainly would not take it that we have invested above and beyond our normal rate of investment on price.

Further question
Okay, fair enough. And then other two quick ones. In online have you seen any kind of discernible impact from Amazon?

And then on Argos for the Quarter, are you able to break out the price volume in that 2.3 like-for-like? Thanks very much.

Answer: Mike Coupe
Well I will do the online piece and will probably give you the same answer we have given already on Argos which is, we have been very kind that we have actually given you the Quarter Trading Update, but we are only three weeks in. We will give more colour when we get to our Interims in 5-6 weeks time. So I beg your indulgence, please be patient with us, we can't talk about it in any more detail.

As far as online is concerned, 8% headline sales growth, 12% volume growth, nothing that we can see in the numbers that has impacted us as far as the Amazon position is concerned. We are continuing to execute what we said we will execute before. We now have same day delivery in eight shops. We are rolling out Click and Collect in 200 shops. That is the most significant news for us in the Quarter is that we have successfully opened out Bromley By Bow online picking centre which will enable us to increase capacity in London and that ensures that we can get growth in what is now probably now the most highly penetrated online grocery market well certainly in the UK, if not the world. So that gives us capacity for the future which is a very important part of our growth aspirations for that business. But nothing, the direct answer to your question is we can't see anything in our numbers which would lead us to think that in any way, shape or form, has Amazon impacted us.

Rob Joyce
Okay, thanks very much.

<u>Question 7</u>

Stewart McQuire, Credit Suisse
Morning Mike, morning Ed. One follow-up and a couple of questions from me. I am struggling a little bit with the Convenience. It grew 7% you said. You opened 9 stores out of 783, but like-for-likes were only up 0.6%. Can you tell me how you calculate that 7% growth? That is question number one.

Question number two, on online, 8% sales growth, 12% order growth, can you give us an indication on size of the online basket? Obviously it is trading down, where are you?

And then finally on your multi-buy strategy. You said that you wanted to end them entirely by August, but now you have had the vast majority of multi-buys removed. Do you still expect to remove all of them or is there back tracking there? Thanks, that's it.

Answer: Mike Coupe

Yeah, I am trying to work out which order. I mean the Convenience numbers are as they are, I am not sure there is a lot more I can say. It is 7% growth. We have not changed in any way, shape or form the way that we report things and I would suspect that is a reflection of the number of stores that we opened quarter on quarter. So I will ask the guys to update you on the specifics. But clearly last year we opened in total 69 during the course of the year, this year we will open less and therefore I suspect the savings difference that you are talking about is a reflection of the timing of openings. But there is nothing sinister in the way that we reported it. It is identical to the way we have always reported it. So I am sure that after the call we can give you a bit more colour in exactly how that number is calculated.

The second point, yeah I mean basket size in online continue to drop by implication, they are dropping by about 4% given the difference between the online order growth and the actual online revenue growth. And that is a function of the fact that delivery pass penetration continues to rise. It is a great thing from a customer point of view, but of course it means that they can shop more frequently, effectively for free, so that is what they choose to do. And clearly things like Click and Collect also have some influence on market size. So we have seen a slight slowing down of the reduction in trend or reducing trend. I suspect over time that will begin to flatten out, but I think that will probably still be the case for let's say the next 12-18 months.

As far as multi-buys are concerned, we just have to be slightly careful that we aren't called to task for running things like buy 6 on alcohol. So when we do a wine promotion buy 6, save 25%, that is technically a multi-buy. So there are a few of those types of things that we caveat what we said by. But what we are talking about is the sort of in terms of our general day to day trading. We have eliminated all of the multi-buys in our business. So it is purely around giving ourselves a little bit of wriggle room to make sure that we don't end up with a headline that we are running multi-buys in some categories at some periods of time. We just want to make sure that we don't make ourselves a hostage to fortune.

Further question
Thanks Mike, just one quick follow-up. On the delivery pass. Can you give us an idea of what percentage of customers have delivery passes and also give us your average basket size for online?

Answer: Mike Coupe
I don't think we quote the average basket size. I am now looking around the room. We will get back to you on that second or the first question, I don't have the number. I used to know what it was, but I don't have the number off the top of my head. I know the penetration has increased. So I apologise, but if we can give you the number we will.

Stewart McQuire
Thank you.

<u>Question 8</u>

Sreedhar Mahamkali, MacQuarie
Good morning. So a couple of questions from me please. I think again, harking back to the first question where we started the promotional strategy. Can you actually say whether that change in strategy, which has been gradual, but I think certainly you have stepped up over the past few quarters. Has that actually impacted volumes negatively? And how do you, give a sense into how you will deal with that impact? Is that something you would annualise in a year and move on? Should that negative

volume continue to persist, would you need to revisit that balance in terms of multi-buy versus everyday low prices? Just talk us through that balance please, first one?

And second one, you talk about outperformance, continuing to outperform the major peers is what your strategy is enabling you to do. Just clarify that outperformance? Is that based on total sales rather than like-for-like? Just help us understand that comment, outperformance please?

Answer: Mike Coupe
Yeah I mean on the first, actually we have seen volume growth in the quarter, we actually saw a slight volume decline in the previous quarter. So our analysis would suggest that what we have done on not just removing multi-buys, but also of course investing in underlying base prices, has not had a material impact on overall volume. Clearly it has an impact on a category by category basis and that is part of a kind of learning process that you go through. I think again we have said publically that we won't be hide bound by a particular number that we aiming for. What we will do is continue to look to refine on a holistic basis, but also on a category by category basis, a combination of where we choose to promote and where we choose to price invest. And we know and we learn continually about the best kind of price investments for our business and how we hone that overall balance. You know it is fair to say, if you look at what we have done in the last year, we have made some quite radical changes. So whether it is reducing Nectar points, whether it is taking out Brand Match, whether it is reducing multi-buys, an investing, reinvesting that back into underlying price, we will continue to move in that general direction, whilst being mindful of that balance that you have already highlighted that you need to strike between maintaining volume growth and getting to a sustainable and competitive platform for the medium to long-term. So the promotional participation in the Quarter is around 25%. It was 23% in the previous Quarter, but actually if you look historically it does step up a bit in the summer so that is more a reflection of seasonal trends, rather than something that has changed about our underlying strategy.

Further question
What was it in Q2 last year Mike? Do you have that number to hand in terms of promotional participation, the 25%?

Answer: Mike Coupe
It was 31% last year.

Further question
And the outperformance comment?

Answer: Mike Coupe
Sorry on outperformance, I am looking at the market share data. If you look at our market share over the last year and remember this is a marathon and not a sprint, we have broadly speaking maintained our market share and certainly all of our mainstream competitors, the big three others, have all lost various levels of market share. And even on a 12 week basis, the sort of latest Quarter, broadly speaking we are second, Tesco have done a little bit better. But I would refer to what I said earlier, in the end we are in this for the long-term and we stand by our track record of outperforming the market year on year for probably now the last 6,7,8 years. So that is the measure that we would look at. And of course I would point at the fact that we have been pretty consistent in our performance and perhaps some of our competitors have been less consistent and therefore might be starting from a slightly different start point.

Further question
Just to pick your brains, do you think the like-for-like outperformance is more important or overall total sales and total market share is more important?

Answer: Mike Coupe
Well we could have a very long debate about this. So you guys put particular stool on like-for-like performance and I would argue that as we look forward, that particular measure becomes increasingly meaningless in the sense that I suspect even today, people may choose to report it and probably do choose to report it in different ways. But of course in the world that we are describing where you have got Click and Collect, you have got online deliveries to home. You have got an increasing penetration of various delivery mechanics and of course in our business with the overlay of Argos, half of Argos's business is bought online and half of that is Click and Collected in stores. Now is that online growth? Is it like-for-like growth? How do we treat an Argos concession in a Sainsbury's store? All of these issues are issues that we will need to articulate more clearly to you when we get to our Presentation in November at our Interims. So I would suggest that increasingly headline sales growth is the measure that you guys need to look at and certainly I would point at as being the measure, an ultimate measure of our performance. Because you can see it in some of our competitors. Where there has been massive space closures, clearly that has a level of consolidation which leads to effectively boosting the like-for-likes. These are the kind of issues which get foggy when you start getting into just obsessing about like-for-like sales. So I would suggest that over time I would point at headline sales growth, the total sales growth as being the most meaningful measure.

Sreedhar Mahamkali
Thank you.

<u>Question 9</u>

Kiranjot Grewal, Bank of America, Merrill Lynch
Morning, you made some comments on the price gap having never been smaller across the big four. Could you give us some details on where you sit versus the others?

And also, following on, where is the price gap today versus the discounters? Thanks.

Answer: Mike Coupe
Yeah we haven't again talked specifically about the numbers, but I stand by what we said today and what we said previously. First of all our price position has never been sharper and that has consistently been the case during this Quarter and during this financial year. And secondly the corridor, if that is the way of putting it between the big four Grocers has never been tighter. And you can see it is not necessarily the most scientific price survey, but we did actually win the Grocer 33 Price Survey this week and that has not happened for a while, but perhaps that is a reflection of the fact that we are pretty comfortable with our price position relative to our mainstream competitors.

We have talked on this call previously, that if you kind of go back a few years, you would articulate the price gap between ourselves and the discounters and let's say for the sake of this conversation, around 25%. We would say that that gap is now in the order of 15%, but of course you could put together a basket at one extreme that would show us being cheaper than the discounters if you looked at our basics range and equally we know it was publically reported that the discounters themselves chose a different basket which would show the gap to be wider. So all of these things are open to some form of interpretation, but the way we would measure it, we would say that our price position, relative to discounters has closed reasonably significantly over the last couple of years. And that is a reflection of the targeted price investments that we have made.

Female
Perfect, thank you.

Question 10

James Tracey, Redburn
Morning Mike and Ed. Two questions from me. The first one is for Mike. You mentioned the importance of looking at the headline sales instead of like-for-like. I have done some approximations and if you look at the core business, this is about online and Convenience, total sales in the Quarter declined by 1.8 and have been falling for about 2.5 years or so. So do you see an end to that trend in grocery in online and Convenience for the clients in the core?

And the second question is around the pension deficit. Discount rates appear to have come around 100 basis points which would imply a £1.7 billion increase in the liabilities, is that a reasonable estimation? Thank you.

Answer: Mike Coupe
Well I will go on the first and then pass to my colleague on my right for the second. Again we have been pretty up front when we laid out our strategy in November 2014, we were very clear that over time we would expect that supermarket volumes would decline, that online would increase, convenience would increase and indeed that the market share of the discounts would increase to round about 15% share over 5 or 6 years. There is nothing in our current analysis that would change from that point of view. In fact I would suggest that what we said in November 2014 is playing out to be remarkably accurate plus or minus maybe one or two percent in either direction. So it is absolutely true and we are planning on the basis that our underlying core supermarket volumes and sales will decline over a period of time. Of course all of the things that we are putting in place, improving our price competitiveness, making sure we improve the quality of the products, that we focus on areas where we can differentiate particularly around our service, product availability, instore standards, we will continue to do so to mitigate that loss. And as I have already suggested, if you take the last year broadly speaking we have maintained our market share. So on the face of it, we seem to be doing a reasonable job of that whilst accepting that the market is changing and therefore we need to adapt to changing customer behaviour and habits. And that is why same day delivery, rolling out Click and Collect online, the acquisition of Argos and the Home Retail Group, play into the future of this business. And that is the balancing act that we are always treading. But your underlying analysis, I have not actually back solved the arithmetic, but you won't be far out in terms of the analysis that you have made. I will hand you over to Ed to talk about pensions.

Answer: Ed Barker
Lovely, thank you. So I think first point to distinguish James is there are two things going on. We have an actuarial valuation which is our triennial valuation, takes place every three years. And that really derives the cash that we are going to be paying into the pension scheme. Our triennial strike date was March 2015 and we hope to be able to announce the results of that come our Interims. But that drives the cash that funds the pension scheme.

I think what you are referring to is probably the accounting deficit. The accounting deficit is updated every reporting date so we will have a next strike date of 24 September for that. And that will take into account a movement in both assets and in liabilities. We put some sensitivities around that which I am sure you are referring to within our year end accounts. It is difficult to judge what the movement in assets and liabilities has been. They have moved in different directions, but again we will be reporting on that come the Interims once we have gone through the full valuation process.

James Tracey
Right, thanks a lot guys.

Question 11 [No question]

David McCarthy, HSBC

Mike Coupe
Are you cheating Dave, that is the second time? He is cheating, he has obviously pushed the off button. Can we move on, I think Dave has disappeared.

Question 12

Darren Shirley, Shore Capital
Hi, it is the short fat one, it's Clive, morning gentlemen and Darren is here too. Just in terms of sort of more subjective questions gentlemen. Firstly just on the differential in price versus the discounters, Mike do you have an aspiration in that respect given the magnitude of the progress you have made over the last year?

The second question was what you felt about the cost of servicing online orders, given what you said about delivery pass as a free shopping issue for shoppers? Because I sense the industry was trying to introduce more rationality in terms of the cost of fulfilment and maybe that is going back a step again. Is that a big issue down the line how you break that?

And then thirdly, what your customers view, what feedback do you get directly from your customers of the step down in promotional activity? What are they actually saying to you in terms of how the stores look, the theatre, the colour, the offers versus more mainstream, but that times can be more dull, EDLP please?

Answer: Mike Coupe
Yeah, I will have a go at all of them, I am sure Ed will chip in if there is anything he can add. I think without getting into too much detail, if you look at other developed markets where you have seen a kind of stemming of discounter growth, you probably need to see a price gap of somewhere between 5-10% of that order of magnitude. So you know you have made the observation, not just us, but our mainstream competitors are all kind of tackling that particular issue in a slightly different way. I think that in and of itself creates an interesting dynamic in the market and perhaps a slightly more challenging environment as we can see from the discounters themselves. So I would suggest that you need to get to that kind of position over time. It is not something you can do overnight for obvious reasons, but we will continue down the road of targeted price investment, of looking for the opportunities as and when they arise. And clearly you can see in some categories, and nappies would be a good example recently. There is a bit of a turf war going on where people understand the sensitivity of very specific lines.

In terms of the online business, I guess there are two things you could observe in the market place. One you have already referred to. There is a degree of rationality around slot pricing. And you could argue that there have been a few moves by some of the players in the marketplace to perhaps bring a slightly more, how should I put it, sensible approach to slot pricing, which clearly improves, if that is the right word, putting the underlying profitability of the business. But secondly there is an element of self-help. So if you take us as a specific. We have invested quite a lot of money in an online picking system in the last year and indeed in online routing systems, which means there is quite a lot of self help going on. And if we look at our online picking efficiency in our shops and our delivery and drop densities, actually there is a slight advantage for a specialist picking centre, but not much. So there is, you could argue both sides of the equation of gradually working their way to a sensible and rational position.

As far as customer measures are concerned, one of the things which is particularly encouraging from where we stand is we have seen our customer satisfaction index, which is an independently monitored customer measure, actually improve, not just overall, but on underlying pricing. So certainly the measures we would look at within our business, the external measures would suggest that our customers like what we are doing. They like the simplicity. You know we have made the commentary before around the fact that our customers will say to us that they don't want a Maths Degree in order to be able to do their shopping. And in that sense, simplified pricing works, But you are right, there is the other part of the equation that we have to be mindful of is that it does create a buzz in the stores and so all the time we are trying to find the sweet spot as we discussed earlier between underlying EDLP and making sure there is some excitement in the overall mix and overall offer and will continue to do that whilst accepting the general direction of travel will be to invest in underlying pricing, particularly in lines which are discounter facing.

Further question
Thank you for that and just to come back on one point, on the pricing differentials again. To the extent that you have made structural progress in more so in the pence rather than percentage differential on fresh food, that almost won't be. There will be no going back in that respect. I mean fresh produce, fresh meat that sort of thing, versus the discounters?

Answer: Mike Coupe
Yeah again we talked around targeted price investments and clearly if you look at some of the things we pointed at today, investments in underlying protein meat, beef, chicken, fruit and veg, have been pretty significant over the last period of time and that has been one of the areas where we have invested reasonable amounts of money and have seen volume reactions on the back of that. So these things are dynamic. You can choose a particular week when a particular product is in the firing line. As I say the most recent spats have been on nappies, it was ever thus. But the general direction of travel is to make sure that we are addressing the price gaps that our customers would see as being most important to them. Primary protein would be a good example of that. And we know that where we see volume increases in primary protein, we don't just see it in the products themselves, we also see it in the associated items that customers use to make the particular dish they are making. So mince and spaghetti Bolognese would be an example. You sell more spaghetti, you sell more tomatoes, you sell more onions. So that is the sort of learning that we get as we go through this process.

Clive Black [Not Darren]
Thank you very much Mike.

Question 13

Nick Coulter, Citi
Hi good morning, just a couple of very quick follow-ups if I may. Firstly on the discounters, are you saying we are broadly half way through a five year industry journey to address the discounters? And presumably you will need to see more in the way of like-for-like volumes from your grocery business across that period? That is the first one.

Answer: Mike Coupe
Well it would be nice to think we are half way through a five year journey, but I suspect it was ever thus. I have worked in this industry for 30 years and there is always rising and falling tides. But the underlying issue, dynamic between the supermarkets and the discounters is playing out broadly speaking the way that we articulated in November 2015, sorry 2014. We would expect the discounters to increase their market share, they have done. We would expect them to get to around 15% of the market over the next five or six years and clearly that has a consequential impact on all of the markets, not just the big four grocers. So we are planning the business on that basis. We have said that consistently. Whether we are half way down the journey or the journey will continue beyond that, I suspect we are going to be having the same conversation in 5,6,7 years time. So this market is constantly evolving, constantly changing. What we are doing is setting up our business for that evolving and changing future. So there are many other dynamics that will play out over the next period of time, not least the rise of online shopping, not just in groceries, but also in non food. So it was ever thus. To articulate a sort of five year journey that we are half way through is probably a little bit short-sighted in the sense I suspect it is just part of the cut and thrust of operating in a grocery market.

Further question
But then you are clearly expecting in a short-term sense there will continue to be a volume headwind. Your like-for-like volumes in grocery are weaker over a shorter period of time. Presumably to make your P&L work, that needs to tick back up again, and that is something you will be targeting to do?

Answer: Mike Coupe
Yeah, again we have articulated at a headline level, we would expect over time that the relative proportion of our business in supermarkets will fall. However we can do lots of things to mitigate that and we have talked again extensively about what we intend to do. Whether it is improving the quality of the products that we sell, targeted price investments focused on particularly the discounter facing lines. But also investing in areas of growth like Convenience, like online and of course we have not talked about it much today, but we now own the largest non food business in the UK and given its relative lack of consolidation, we think there are opportunities for us to get potential growth out of that part of the industry. So when we look at it in the round, we think we are pretty well set up to deal with the headwinds as you described them within the grocery sector and we think there are opportunities for growth, not just within our underlying food business but within our non food business. And we haven’t even talked about the Bank, but we also own a Bank which has lots of upside potential as we look forward and the process we are going through in terms of re-platforming that. The Argos book coming over to the Bank are all part of that underlying strategy. So we think there are opportunities in this business in the future.

Further question

Thanks and then one very quick follow-up on the Convenience business. There is a notable delta in like-for-like performance between Q1 to Q2 versus the performance of the underlying supermarket business. What has driven that delta? Is it comp based or have you changed something in the offer? Thank you.

Answer: Mike Coupe
Well we continue always to strive to improve all aspects of our business. If you look at something like the launch of On the Go and our Food to Go business, then as you can imagine that would have a disproportionate impact on as disproportional improvement in some aspects of our Convenience business. You know it tends to be products that are more convenient and therefore more important to the convenience business. If you are standing back and looking at the market conditions you could argue relatively speaking it has been a slightly nicer summer. It was an awkward summer in terms of some aspects of the seasonal business because it was a little bit wetter and colder in the first part and a bit warmer and drier in the second part. That has probably been helpful to the Convenience business. So where there is a delta to the supermarket business, it is probably driven as much by the weather in August and the early part of September as anything else. But clearly some of the areas that we have been investing in product development, On the Go, Ready Meals, some aspects of our fresh food offer, have a disproportionate benefit to our Convenience business as well.

Nick Coulter
That's helpful, many thanks.

Closing remarks

Mike Coupe
I think that is it unfortunately. So hopefully we will get to talk to you at some point between now and our Interims and if we don't we will see you all at our Presentation in the early part of November. Thank you very much.

End