

J Sainsbury plc
Q3 Trading Statement Analyst Q&A Call
Friday, 10 January 2025 – 9.15 am

Presentation

Operator

Hello, and welcome to the Sainsbury's 2024-25 Q3 Trading Statement Analyst Q&A call. On the call this morning is Simon Roberts, Chief Executive and Bláthnaid Bergin, Chief Financial Officer. I will now hand you over to Simon Roberts for the presentation.

Simon Roberts
CEO

Well, thank you and good morning, everyone. Welcome to our quarter three trading statement covering the 16 weeks to 4 January. I'm going to talk briefly about our trading performance, and then of course, Bláthnaid and I will be happy to take all your questions.

So first and foremost, I want to say that we're really pleased with our grocery performance. As you know, we were up against some tough comparatives, particularly at Christmas, and we knew we would need to be our best operationally, and make the right balanced and targeted investment choices to deliver the growth that we planned, particularly in fresh food, with customers shopping later than ever.

Specifically, we invested in service, availability and value. Our value index against our biggest competitors is as strong as ever, and customers recognised this with our best ever Christmas availability and our highest ever customer satisfaction scores, both in stores and online.

So I'd really like to thank all of our colleagues for what was an outstanding effort across stores, depots, and our support centres, and of course, everyone out on the road in vans and lorries. A big thanks too to our suppliers for their fantastic support in delivering that best ever availability.

We've continued to be super sharp on value, and customers love the value they get through Nectar Prices. We've rolled out across more of the range, and it's a key driver of the continuing strong improvement in our value perception. At the same time, we've continued to drive innovation, adding more than 300 new Taste the Difference products this Christmas, driving growth ahead of all our key competitors.

Argos sales were strong over the key Black Friday and Christmas periods, reflecting improvements to the customer proposition. But as you'll have seen from some of the macro data published this week, it was a tough backdrop for general merchandise spending outside of those key weeks, and this impacted both sales and margins.

Against particularly tough volume and inflation comps from last year, we grew grocery sales by around 4% over the quarter and the key Christmas weeks, with volume growth the main contributor. General merchandise sales within Sainsbury's largely reflected the decisions we've made on product categories and space allocation, offset by strong sales and market share gains in our Clothing business, with sales up 2% over the quarter and double-digit sales growth in Clothing at Christmas.

At Argos, sales were down slightly year-on-year over the quarter, reflecting weak consumer spending in discretionary categories, but they were stronger over the Christmas period.

Now, the strength of our grocery performance against that tough comp is clearer here, with our two-year grocery volume growth continuing to accelerate, up nearly 6% in the third quarter and ahead of the market and key competitors over the four key Christmas weeks. We've started to see some modest benefit from space reallocation to food, with an addition of around 1% by the end of the quarter.

Now, this benefit will build substantially over the course of this year as the program builds and as the former Homebase stores come online. Regionally, this will also put us in a stronger position to pick up a bigger portion of trade outside of our traditional southern stronghold.

The consistency of our delivery on value, innovation, and service really shows through here, where we've won market share at Christmas every year for the last five years, with more and more customers choosing Sainsbury's for their big basket shop, and nearly 20% of new big basket customers entirely new to Sainsbury's.

This slide we've updated from our Interims shows again our winning combination across quality, service and value. In our supermarkets, we saw higher year-on-year customer satisfaction across all the key measures on value, quality, and availability. In online grocery, we delivered record customer satisfaction, driven by improvements in availability, and order completeness, probably the most important metrics for customers doing their big Christmas shop online.

Sainsbury's reputation for quality and the innovation we're delivering really shines through, I think, here. Taste the Difference already has the biggest premium own label participation of any grocer in the market, and we've built even further on that, with sales up 16% in the key Christmas weeks, nearly 20% in key fresh food categories, and Taste the Difference products in more than half of big Christmas shops.

Now these charts give a bit of context to the Argos sales numbers. Not the top-line growth that we'd hoped to deliver in Q3, but clearly a much better trend over the last two quarters, reflecting improved online traffic. As you can see from both of the top two charts, we're now heading into softer comparatives over the next two quarters.

The bottom chart shows that customers responded well to our Big Red promotional event, the key Black Friday weeks, and the immediate run into Christmas. But outside these periods, sales were subdued across the whole market, particularly in the period between Black Friday, and as you can see, Christmas. This impacted sales, but also margins with a high level of promotional activity in the market.

So we're now nine months into the Next Level Sainsbury's plan that we outlined last February. Looking at the key outcomes we detailed, we're really pleased with the continued momentum at Sainsbury's, with two-year volume growth continuing to accelerate as more and more customers choose Sainsbury's for their big shop and we add more food space.

Nectar is more relevant and more rewarding for customers, and Nectar 360 is a significant contributor to profit growth. We're making progress at Argos, with a stronger digital proposition and improved online traffic trends, driving good conversion with customers spending over the key trading periods.

We're making good progress across our savings programs and capital investments that deliver efficiency gains, and we continue to make balanced choices. These are ever more important as we head into a year of particularly high operating cost inflation.

We've guided today that we expect full-year underlying retail profits to be in line with consensus, up around 7% year-on-year, with very strong profit leverage at Sainsbury's, particularly strong in the second half, good cost saving progress and a growing profit contribution from Nectar offsetting profit pressure at Argos.

Looking to the year ahead, our Next Level plan, our scale and the positive momentum we have across our grocery business in Nectar and in our cost saving program put us in a really strong position to navigate a tough cost environment, and we'll come back and talk to you more about that in April with our full-year results. So now let's open up the call for Bláthnaid and I to take all your questions. Thank you.

Question and Answer Session

Operator

We'll now go to the Q&A. If you would like to ask a question, please use the raise hand feature at the bottom of your screen. Alternatively, if you have dialled in, please press star 9 on your handset now. To keep things as fair as possible, please only ask one question per person. If we get additional time, please re-join the queue by re raising your hand or pressing star nine, and we'll try to get back to you.

We will pause for a moment to allow questioners to enter the queue. The first question is from Rob Joyce at Exane BNP Paribas. Please unmute yourself and begin with your question.

Simon Roberts

Hello, Rob. Good morning.

Rob Joyce, Exane BNP Paribas

Thank you very much. Morning. Happy New Year and thanks very much for taking the questions. So look, firstly just on grocery. As you alluded to there, the profit drop-through has stepped up materially in the second half while Tesco yesterday suggested limited drop-through on profits.

Could you elaborate a bit more on what's driving that improvement for you versus the first half, and just give us some confidence that there hasn't been any diving for the line to offset some of Argos's weak performance there?

Then the second one is really just on Argos. Another year where the market's been very promotional. Profits look like they're down there despite strong execution and a softer comp. Is there more you can do at Argos than you currently are or do we just look at this as a market with overcapacity and probably structurally declining profits? Thank you.

Simon Roberts

Rob, thank you. Okay, let's take those in turn, starting with your question on grocery. So look, first thing to say, we're really delighted with our grocery performance and I think we've delivered exactly what we set out to do. We made targeted investments this Christmas, and you can see that really playing through in value, in availability and service. I have to say, I've

seen 30 plus years Christmas in retail. I have never seen the intensity that came through in those last two or three days, and our team really stepped up.

Our plan was ready, we were ready for it. Customers shopped very late, and we saw real delivery come through when it mattered. What that's meant is that this story continues to be a volume-led story for us. We're growing our volume. You can see our two-year volume up 6%. You can see what's happening is we're being very intentional about the target investments we're making in the offer. We've been at our best position on value, and we exit the quarter at actually the strongest value position of the year against our major competitors.

You've seen what we've done on availability, leading availability; we've never delivered that level. Our customer service metrics right across the board, we invested for that outcome and it came through. So I think the volume-led delivery in grocery we're really encouraged by, and as you know, we've been building this picture now over seven consecutive quarters of growth ahead of the market, and five Christmases in a row we've delivered that.

What's powering that performance is the big shift in the big trolley shop back in Sainsbury's. That big trolley shop through all of the build of '24 came through at Christmas even more strongly. So to your question, we are very focused on delivering the best customer offer, and customers are really responding to that. But exactly as we expected, we're driving a higher profit leverage is that volume-led story in grocery really plays through.

Bláthnaid Bergin

But one small build on that, Simon, if I may. The other thing, Rob, to think about is a lot of our cost saving program was second half delivering. So that was really important. So you've got some of that coming more in the second half. One of the things that we're particularly proud of is Smart Shop that we had a 30% participation over Christmas. That's a big cost saving for us as well. So it's exactly as we planned it, and it's dropping through that way.

Rob Joyce, Exane BNP Paribas

Then the old diving for the line we used to talk about, none of that in there?

Simon Roberts

Far from it. What you can see is the performance building, and look, you'd expect me to say this, but when you look at the strength of our volume comparative in the year before and how we've built on that this year and you look at the strength in areas right across the fresh food and Taste the Difference offer, the year-on-year improvement in our volume given the strength of last year is very substantial.

When I look across areas like produce, fresh food, party food, getting close to double-digit increases in some of these big areas which show there's just the strength of the fresh food offer but also point to the job of work of getting all that volume through the system.

To be able to plan for that intensity, prepare for it, make sure we deliver the best ever availability and the customer satisfaction to Bláthnaid's point. We took a lot of cost out the front end and our customer satisfaction improved year over year in the peak week. That demonstrates, I think, this balanced set of choices between taking cost and efficiency, and improving the customer offer at the same time.

Bláthnaid Bergin

Just, Rob, on your point of diving further down, look, we have absolutely protected our value position. So as we exit Q3, we're in one of the strongest positions we've been in ever, I think. So we have absolutely protected the value position as well. We'll continue to do that and remain competitive.

Simon Roberts

So turning to your question on Argos, I think the first thing to say – we said to you in November that we expected to improve on our performance in quarter 1 and quarter 2 and what you can clearly see in the sales trend at the top line is to what extent that's happened. So as we've come through this period, we delivered clearly negative 1.4 for the quarter overall, but positive 1 for the last six weeks.

That really was a feature of the fact that when customers really came shopping in the market on Black Friday and on the Christmas weekend, we saw Argos being a real target destination for them. What happened? Well, one in four of the UK population visited the Argos website over the Black Friday weekend.

Traffic has moved up, as you've seen, online traffic's moved up. That's really a key underpin of the fact that, as you know, there's a lot of work we're focused on in Argos. The team are focused on those four elements I described in November, which is we're looking hard at our assortment and we're constantly improving.

It's worth knowing that against that objective of improving our range, in fact in the third quarter alone we added around 3,000 stockless SKUs to our offer. We'll have about the same in quarter four. We saw substantial improvements in our availability in immediacy, which has really helped customers fulfil. We've extended our range of payment options in the last quarter, so Klarna, Google Pay, now fully live on our platform.

We've seen customer improvements in areas like quality and inspiration jump already from the work we're doing. So just remembering back, Rob, we said we'd improve our range and that was a key way of driving more conversion on the Argos platform. We'd improve our customer experience online. We're starting to make progress there. We'd take costs out of the operation to become more efficient, and we would continually look to improve our stockholding position to become more efficient with cash.

All of those programs are well underway, and in fact a lot underway in quarter three, against a backdrop that clearly was a tough one in general merchandise. Customer behaviours were subdued, they only shopped at the big peaks, which is why we need to keep driving that program through in the way that we are.

Rob Joyce at Exane BNP Paribas

Okay. I'm guessing you're going to a potentially tougher backdrop next year.

Simon Roberts

Yeah, I think the backdrop in general merchandise continues to be tough. That's the reason we're taking the actions we are to make sure we've got a really clear plan in Argos. I would just finish the point by saying we talked to you about the profit leverage in Sainsbury's that we delivered in the first half. You can see the progress that's continuing in the second half and you can see we're doing that whilst delivering for customers a really compelling offer.

At the end of those two components, we've confirmed our guidance today at the midpoint of the range, which demonstrates, despite the softness in the GM market, the strength of the

Sainsbury's performance driven by both the grocery volume and the cost savings that Bláthnaid spoke about, and the net delivery gives us confidence we will deliver against the midpoint of our range this year.

Rob Joyce at Exane BNP Paribas

Thank you.

Operator

The next question is from Sreedhar Mahamkali at UBS. Please unmute yourself and begin with your question.

Simon Roberts

Hello, Sreedhar.

Bláthnaid Bergin

Good morning.

Sreedhar Mahamkali, UBS

Thank you. Good morning. So listen, I think a couple of questions, maybe just to follow up on Rob's probing on Argos, and clearly that's one we get quite a lot here from investors. I guess, Simon, you've already alluded to probably another tough year coming up in terms of consumer backdrop, particularly discretionary general merchandise area.

Is your view that the strategy is beginning to have some impact on Argos' performance and it should continue to build into next year, or should you be pushing harder in one of these areas and changing strategy a little bit as you head into what might be a tougher context? I guess we really want to see when you think Argos will be pulling its own weight in terms of profit contribution as we head into next year. Your thoughts there.

Secondly, I think some of the points you've made, what we are seeing in the industry in terms of inflation, if you could talk a little bit about what your view is. Clearly, Kantar comes up with some numbers that I think seem quite a bit far from reality, but if you could talk about inflation that you see and how you feel about your own volume performance, potentially in that maybe rising inflationary environment. Thank you.

Simon Roberts

Thank you, Sreedhar. Okay, well, let's talk on Argos first. I think the important point to make here is we can all see the context of the general merchandise market, really challenged market, subdued customer. Customers have come to the market to spend at the key moments, Black Friday and Christmas. More subdued in the weeks outside of that, higher propensity towards technology spend, lower margin categories, lower propensity for all the obvious reasons to big ticket items.

So what are we doing? We're really focused on that four-part plan that we've shared and I've just been talking with Rob about. I think it's important to say, as we think about this year, Argos will be usefully profitable in the second half of the year. Clearly we'll make a profit for the full year. We're very focused on delivering our plan in Argos, the team. We've got very, very clear execution plans against the More Argos, More Often plan.

Already, as I've just described, elements of that plan are already landing and making a difference, but against a backdrop that will continue to be challenging for the reasons that you say, Sreedhar. So when we stand back and look at our performance, very strong grocery business performance, driven by volume, improving level of profit leverage as we make more progress into our Next Level plan, powered by that volume and our cost saving plan, and getting things right ultimately for customers. More big trolley shoppers coming into Sainsbury's - that's been really evident this Christmas - to make sure that we mitigate any risk on the Argos side.

Whilst - and this is important to say - we've said this since way back in 2020 - we won't compromise the performance of our food business for underperformance as a result of the broader general merchandise market. That's what you can see exactly that we're doing. In terms of the question on inflation, I think you've indicated by your question, it's very clear that inflation at Sainsbury's through the third quarter was substantially below the numbers we've seen reported on the market data this week. In all reality, quarter three's data was a bit up on quarter one and quarter two, but nothing like what we've seen being reported.

So inflation between 1% and 2% for the third quarter, a bit higher in fresh food, growing more quickly in fresh food, and no surprise we'd expect to see in areas like meat, fish and poultry, produce and dairy, that inflation would rise more quickly given the labour component that's more significant in those categories. I think in terms of where we are, we're delighted with our volume performance. We had a very strong comp that we were going against this year on volume and we've improved on it. When you look at our two-year number, you can see the strength of our performance compared to the market and compared to others.

It was absolutely delivered by a very clear plan that was focused on bringing more customers to do their big trolley shop into Sainsbury's and it really worked for us. Our value position was the strongest we've had through this period, powered by Nectar Prices. Over 9,000 products in the offer on Nectar Prices this Christmas and so when customers were choosing where to do their big trolley shop, that was a key driver of decision. Innovation - I've talked lots about that before, our team did a fantastic job building on last year's already strong TTD performance, where we delivered 16% growth in TTD in the key Christmas period.

That was powered by over 300 new products and I'm sure, Sreedhar, you were in store along with everyone else seeing all those products and hopefully buying one or two of them, but they really delighted customers. I think that combination of value and innovation is really working for us in Sainsbury's being more of a destination for treat and trade up than others. As a result of that we're seeing that combination come through.

I just want to then just finish that by just as I've already said, the strength of the operation and our service delivery stood us apart this Christmas. We were really busy, and we planned for this. We put more fresh food through our network than we've ever done before and we did that whilst delivering a leading level of availability. So all those things together give us a lot of confidence about the strength of the food volume and one clue that we intend to continue to drive forward. Thanks, Sreedhar.

Operator

The next question is from Freddie Wild at Jefferies International. Please unmute yourself and begin with your question.

Simon Roberts

Hello, Freddie.

Freddie Wild, Jefferies International

Good morning Simon and Bláthnaid. It's not too late to say Happy New Year.

Bláthnaid Bergin

Happy New Year.

Simon Roberts

Happy New Year, Freddie.

Freddie Wild, Jefferies International

So two questions from me, if that's okay. First, on the cost savings which clearly are, you're saying, more of a help in half two than half one. Could you help us quantify the level of help in half two versus half one and how much that will expand or contract into next year as well? Then second, are you seeing any improvement in labour availability behind that 5% increase in pay you've announced today?

Simon Roberts

Thank you, Freddie. Bláthnaid, do you want to speak to cost and then I'll talk about pay?

Bláthnaid Bergin

Yeah. So Freddie, we laid out a cost savings program last year, £1 billion over three years. We haven't given the H1, H2 splits, given it comes down to the phasing of different execution and decisions we make along the way. So, we're not going to break out the H1, H2 cost saving. Assume in your models, a billion is pretty even over the three years.

Freddie Wild, Jefferies International

Thank you.

Simon Roberts

Thanks, Bláthnaid. Then on the pay rise, just to give you a bit of colour on this, Freddie. So first thing to say is we always announce our colleague pay rise at this time of year. The reason for that is we begin our new financial year at the beginning of March. So, of course, it's right to share with our colleagues just before we go live with that what our plans are. So that's consistent with our usual order of business.

In terms of the way we've thought about this, of course we plan for our annual pay rise up to 12 months in advance. It's one of the things we have to think about given the size of the number of people we employ and our responsibility to make sure we deliver the right benefits and rewards for all of our team.

So the way we've thought about this this year clearly is that given the wider challenges on cost coming at the industry to take a balanced approach in our thinking on pay, which is the reason why this year, quite different to previous years, we've split our pay award into two separate increases, one in March and one in August. So in March, we'll move in the UK outside London from £12 to £12.45, and in August from £12.45 to £12.60.

Worth saying in context, clearly the national living wage is going up 6.7%. Our pay increase is weighted over the year at 4.5%, total 5% by August, but clearly, we're doing the second part a bit later in the year, so 4.5% over the year. That I think just reflects the fact that we of course want to lead the industry with a strong pay increase for our brilliant team, recognising the strength of our service and our productivity as Bláthnaid has just spoken to. Also setting that against an affordability lens which given all the costs coming at the industry, we thought it was appropriate and prudent to do that in two stages this year.

So that's the backdrop to our pay increase in terms of the way that we've thought about it. In terms of why is it important, it's important because one of our four key outcomes is save and invest to win. In order to do those things we've got to have the right capabilities and the right skills in our Company. One of the things I think is becoming increasingly clear is our service performance is really standing us apart.

You can see that again this Christmas. We had our best ever customer satisfaction measures in our supermarkets than at any point we've had before on value, on availability, on how we served our customers and that's one of the reasons why in this balanced choice we make, we want to reward our colleagues with the right level of pay, albeit we've done it in two phases this year to manage the obvious impacts of all the costs coming at us.

Freddie Wild, Jefferies International

That's super helpful. Thank you so much.

Simon Roberts

Thanks, Freddie.

Operator

The next question is from Monique Pollard at Citi. Please unmute yourself and begin with your question.

Simon Roberts

Good morning, Monique.

Monique Pollard, Citi

Morning. Thank you very much for taking my questions. Just two hopefully quick ones. The first one was on Argos. Obviously, you mentioned that sales were strongest in tech, toys, and big-ticket items were weaker. I just wondered if you could give us any sense as to whether the gross margins across those categories are materially different or whether some of those categories – I would imagine things like tech – might lend themselves more to higher promotional activity than others.

Then the second question was just one on the customer sentiment. Obviously, you mentioned in the release a couple of times that customers shopped later than ever. I'm just wondering if you think that the shopping later than ever was to do with Christmas timing, it being on a Wednesday this year versus a Monday the year before, or do you think it is a sign of increased customer hesitancy?

Simon Roberts

Monique, thank you. So, Bláthnaid, shall I maybe take the customer behaviour and maybe on the Argos categories that performs? You take that one?

Bláthnaid Bergin:

Yes.

Simon Roberts

So, let me take the second question first and then we'll do your first question. So, look, I think in customer behaviour, Monique, as you described, there's no doubt that customers shopped later than ever for food. I'm pretty sure we say that every year, customers shop later this year than the year before. But I think this year, to your point, because of the midweek Christmas, that amplified that effect even more. So, the biggest day was Monday the 23rd, we had the biggest Christmas Eve as well.

I think that just really played to this point that customers waited to do their big shop until then. I think it's also a feature of the fact that as we've come through the pandemic three or four years on, customers now feel really assured they can get everything they want closer to Christmas.

So, that availability that I spoke of, we had our best availability when it really mattered. In terms of the other features around customer behaviour in food, look, I think we saw customers clearly looking for the best value. They were promotionally driven, no surprise there, given all the pressures on households. So, I think for us, because we had such a strong value offer, it really connected with customers. I talked about 9,000 plus products on Nectar Prices.

So, we were able to win that big trolley shop because of the strength of the offer. I talked about trade-up as well. It's been a theme we've talked about all year, which is that customers both want to get the best value, but they also want to treat family and have special occasions, not least at Christmas for all the obvious reasons.

That 16% growth in our Taste the Difference ranges over the key Christmas period really shows the strength of the offer and the extent to which customers traded up in those big weeks. I think to your point on changes in how customers are shopping and maybe moving to GM a wee bit, obviously, more subdued in GM for all the reasons that you've said. Definitely, we saw customers shopping much more on the Black Friday weekend. We had a strong level of traffic through Black Friday, strong performance on share.

Of course, there was lots of deal chasing going on through that period of time, looking for the best deal in the market. I think without any doubt, we showed up to be ready for that. There's also, I think, clear evidence that customers are shopping closer to payday for all the obvious reasons.

So, the fact that Black Friday coincided with the last payday before Christmas this year changed shopping patterns, whereas in the previous year, Black Friday came the week before the payday, and that undoubtedly changed how customers shop. So, maybe the headlines on how we think about customer behaviour. Bláthnaid?

Bláthnaid Bergin:

Yes, on Argos, look, it's a great question. What we saw there was a growth in technology, particularly in mobiles and tablet sales, and also growth in the celebration categories. But what we saw was some weakness in the household electricals, consumer electricals, toys,

home and furniture, and they tend to be a little bit higher margin. So, you've got some of those mix issues flowing in there as well. But overall, look, we were happy year on year. I think one important thing to say here is we are pleased with how we exited stock at the end of the period.

So, while we've got some isolated pockets that we'll deal with between here and year end, we're pretty pleased we've got a clear stock position and we're on target for those working capital targets we set in Argos. We won't be over-summering anything. Thank you, Monique.

Monique Pollard, Citi

Thank you very much.

Simon Roberts:

Thank you.

Operator:

Just a reminder, if you would like to ask a question, please use the raise hand feature at the bottom of your screen. Alternatively, if you have dialled in, please press star 9 on your handset now. The next question is from James Anstead at Barclays. Please unmute yourself and begin with your question.

Simon Roberts

Hello, James. Good morning.

James Anstead, Barclays

Good morning. Good morning. Good morning, Simon, Bláthnaid. Two questions, if that's okay. So, firstly, Simon, you boldly predicted that Argos would have positive sales in the third quarter, and it didn't quite pan out. You obviously had better sales trends at the end of the third quarter and I think the comps for the fourth quarter are actually relatively easy. So, I just wonder if you're optimistic that the fourth quarter could be the period when Argos sales do turn positive, except I think it's an eight-week period, so making predictions over short periods of time is quite difficult.

The second one, perhaps for Bláthnaid. You've now set out your pay increases for the year ahead. I just wonder if that enables you to comment even more precisely about the overall payroll headwind you're facing next year versus the year just finishing. Thank you.

Simon Roberts

Thank you, James. Super clear. So, let's take the questions in the order you've asked them. So, look, absolutely, as you said, when we talked in November and we looked at the plan for Argos through the quarter, we were clear based on the trends at that time that we were building well towards our plan for Black Friday. I think I said pretty clearly it all depends on how Black Friday played through. In the end, what we saw happen was a softer period between Black Friday and Christmas. That's where our trajectory to the quarter came off a little bit.

So, as we came out of Black Friday and the days afterwards, we were well on track to be up on the year for the quarter overall. But in the couple of weeks between Black Friday and Christmas, it softened more than we expected, and that's what brought that little further

downside than we expected. I think, as you say, overall, in the six weeks to Christmas, we were encouraged by the top line trend.

I would just make the point again that the changes that the team are leading in improving our range, 3,000 new SKUs stockless onto the offer through quarter 3, improvements in the online journey so that we saw more online traffic, the work we're doing to improve the way we're encouraging customers over £100 on free delivery, what we're doing on our cost base, all that activity played through our Christmas offer, albeit the weeks outside the peaks were softer than we expected.

To your point, the comps are softer as we look out over the period ahead. So, look, as I've said, the customer is very subdued in this space. You know that. We can see that in all the market data. What I think we're really clear on is that we're getting more and more progress under our belts on the transformational initiatives that we're making. So, against the context of that tough market, we're positioning ourselves in the best place that we can be to make sure that we capture the customer conversion online. Good to see that online traffic picking up in the way I've described.

As I said to the earlier question, we expect whilst the headwinds are significant, whilst the categories that did stronger were lower margin that we expect to usefully make a stronger contribution in the second half, and obviously see a profit overall for the year. Bláthnaid.

Bláthnaid Bergin:

Great. So, look, we've well trailed this before. The NICS will cost us about £140 million. The rest of the industry is facing that same challenge. The 4.5% increase will cost us about £90 million as well. That was well planned. As we think about our cost savings program, we would have embedded expectations of pay increases. Great, thank you.

James Anstead, Barclays

The £90 million, just to be 100% clear, that's the gross cost of the pay increase that you'd be hoping to make some cost savings to offset that?

Bláthnaid Bergin:

That's the gross cost, and we'd have cost savings already built into the plan, yes.

James Anstead, Barclays

Yes, perfect. Thank you very much.

Simon Roberts

Thanks, James.

Operator:

The next question is from Manjari Dhar at RBC Capital Markets. Please unmute yourself and begin with your question.

Simon Roberts

Hello, Manjari, hi.

Manjari Dhar, RBC Capital Markets

Morning, Simon, Bláthnaid. I just had two questions, if I may. The first is also on Argos. I don't know if you could give any colour in terms of Argos' dollar sourcing exposure now and how you're thinking about potentially managing that for the future. Then secondly, on the food side, I wondered if you could give any colour or any sort of KPIs that you're tracking for the improvement in convenience after you've rolled out the Aldi price match there, and any further opportunities you see to improve the convenience offer. Thank you.

Simon Roberts

Bláthnaid, do you want to speak to that?

Bláthnaid Bergin:

I'll quickly take – so, we hedge everything pretty far ahead. So, when you think about a general merchandise buy, you tend to do that kind of nine to 12 months out. So, we have a rolling hedging policy. So, as you think about some of what's happening on the gilt markets, we're pretty well covered at the moment with our hedging. Simon.

Simon Roberts

Thanks, Bláthnaid. Thanks for raising convenience and really, really good to be able to speak about our convenience offer, because as you say, we had a lot of significant improvements for customers through the third quarter. So, just a quick recap, we substantially improved our ranges in convenience stores. Most stores saw hundreds of lines improvement in their offer, and customers have responded really positively to that change. So, it's a big change we made in October, a huge amount of workload actually in our stores, and our team did a brilliant job landing that change in advance of Christmas.

At the same time, you'll remember we rolled out Aldi Price Match in our convenience stores as well. Again, we've seen customers respond really positively to that. Not different to our supermarkets, we had our biggest ever days in convenience on the run into Christmas. We saw a very strong performance in what we call between the eves. So, obviously, as customers shop more locally between Christmas and New Year, that was particularly strong in convenience as we really focused our offer and our operation to be ready for that.

So, look, we look at our convenience estates, we're really pleased with the progress of the improvements in the offer, most notably, because customers are responding so positively. As you know, we continue to see opportunities to grow our convenience estate. We'll open around 25 new convenience stores next year as we embed those improvements to ranges and with Aldi Price Match. Of course, we intend to make the offer more compelling in more locations. Thank you.

Operator:

The next question is from Clive Black at Shore Capital. Please unmute yourself and begin with your question.

Simon Roberts

Hello, Clive.

Bláthnaid Bergin:

Hi.

Clive Black, Shore Capital

Morning, team. Thank you for the time. Just a couple from me. You've talked about labour as a headwind for the whole industry in the year ahead. Maybe touch on where you see other cost pressures though coming through, because it's easy, I think, to believe that labour is the challenge. Then this time last year, or nearly this time last year, your Capital Markets Day, you talked about the repurposing of space out of non-food into grocery.

Just wondered if you could give us an update as to progress to date, particularly how you're seeing those stores performing, those reconfigured stores, and also just what degree of disruption takes place. I presume the disruption is front-end loaded until you start to actually build momentum in that program. That would be really appreciated. Thank you.

Simon Roberts

Thank you, Clive. Yes, let's take what are the various dimensions of the cost coming at the industry. Let me start on this one. I'm sure Bláthnaid will want to come in as well. Look, I think, as has been well documented, we face an unprecedented environment in terms of the impacts, certainly of the national insurance change on top of any wage increases that we were already planning.

So, as I made the point earlier, we've really thought about our approach to our wage inflation this year, given the added impact of NI. I won't speak about that too much because we're all very familiar with that and it's going to happen in the early part of April. I think, clearly, in addition to that, two things that are worth adding. The first clearly is there are regulatory taxes coming at the food industry by way of EPR.

As other industry colleagues have done, we continue to lobby really strongly that we as far as possible should look to phase the introduction of those costs, given all of the costs coming through NI, that would be an important area to keep really focused on and we're working hard to, as others are, to engage with government to encourage on that.

Similarly on business rates, I think we were and should continue to expect that there is a need for fundamental reform to business rates. As I've said before, as others have said, it's really important that the threshold between large and small stores reflects the fact that actually every retail store faces this punitive tax and we are working with government and will continue to as an industry to ensure that the reform when it comes, creates a fairer situation across the field. That's the second.

There was a risk at the moment obviously of business rates applying a different threshold for smaller stores versus larger ones and that's clearly not something we would in any way think is a solution. Then beyond that, I think really clear regulatory taxes, business rates and then the NI. So, hence the reason, Clive, at the heart of your question, why our Save and Invest to Win program is so important and maybe just hand it back to Bláthnaid on the way we're thinking about the billion cost saving and how we're working it through.

Bláthnaid Bergin:

So, look, Simon's spot on on that. The billion cost saving would fall over the three years, as I've said, Clive. A lot of it, we had anticipated what inflation we'd see in our cost base and built our cost saving program around that. Some of these new costs are unanticipated, so

we'll do everything we can to mitigate it. We have got really tight cost control in this business, and we'll continue just that discipline that we have today.

Simon Roberts

Thanks, Bláthnaid. Then to the question on space.

Clive Black, Shore Capital

Sorry, Simon. Can I just come back on that? Does that unanticipated cost base, particularly NI, actually change some of the parameters around Save to Invest to the extent that labour is becoming so priced? You look at Save to Invest in a different way than you talked about last February.

Simon Roberts

Thanks, Clive. Helpful question. So, look, I think, however important it was to have an ambitious and focused cost program last February for all the obvious reasons, I'm glad we're not trying to think about what that looks like now. We have a well-developed approach to cost saving in this business. We began that in 2020. You'll remember when we did the original work on Food First and delivered £1.3 billion of savings, doubling our run rate in the first three years of our Food First program.

As you say, the billion that we announced in February on top of that to continue that work. So, two points I would make. First of all, we're making really good progress with the plans that we're delivering, and you can already see them landing in the business. We spoke to it earlier on a couple of examples. We've transformed the front end of our supermarkets in a way where we've taken a lot of costs out of how we run the front end. I'm talking about the checkout operations in our stores.

But we've done that whilst delivering for our customers improved satisfaction this Christmas. That's something that's challenging to do for all the obvious reasons. We've grown smart shop participation to 30%. We've encouraged more customers to self-checkout. We've still given every customer the choice to use a traditional checkout. We've made big savings as a result of doing that, and we've improved our customer satisfaction.

Our depot work rate. I talked about the volume of fresh food that flows through our network this Christmas. Our logistics colleagues did an outstanding job moving the level of volume through the network whilst delivering record levels of productivity in our depots. We've completely transformed our fresh food and ambient food forecasting capabilities. As you've heard us talk about that before.

We completed the rollout through the fresh food categories last year and the supply chain team have led and delivered that really quite a complex thing to do in the industry. Make sure you deliver availability and put a completely different platform in. Now with Blue Yonder in place across the whole business, we delivered record availability.

So, the point I make here is not just the cost saving, it's the improvement in the customer offer at a lower cost. So much of what we're doing in our Save and Invest to Win program is about that. To your point, the added cost pressures coming at the industry make that program even more important, which is why it was part of confirming our guidance for this year, it's important we can confirm that we're on track with our cost programs and they're delivering as we expect them to.

Clive Black, Shore Capital

Thank you. Very clear.

Simon Roberts

Shall I just do a minute or two on your question on space, because on the other side of the equation, just to reiterate the point we've said before, given the strength of where our food business is now, I can't think of a better time to be adding more space. We've got the best volume performance we've seen. We delivered nearly 6% volume growth over two years.

You can see the way in which big trolley shops are coming back into Sainsbury's, powered by value, powered by the strength of our innovation and by the service that our team are delivering. That's just across the whole of the operation now. So, as we said before, given the strength of the offer, there are so many parts of the UK where customers can't easily access a Sainsbury's supermarket, which is the reason why over the next 12 to 15 months, we're doing two things.

First of all, as you indicated in your question, we're rotating space out of general merchandise into food which means in many more of our supermarkets, we'll be carrying our full food range. Just reminding us back in February when we announced this, that only 15% of supermarkets like Sainsbury's carried the full food range at that point. We've made about a 1% shift in space since that. That program really accelerates over the course of the next year. So, that's the space rotation in store and then it's the 20 – around 20 new supermarkets will open over the next 12 to 15 months.

Again, the property team working with all of the retail teams are well on with planning that program of opening. A significant piece of work for us, first doors opening in the first quarter of the next financial year. When I look at the map of the UK and those new supermarkets opening, they're in all the locations where, for example, this Christmas, we wouldn't have been able to target customers who want to shop with Sainsbury's, but those stores will be largely in place by next Christmas.

So, an exciting time as we rotate space into food, get more food range in more supermarkets and open those new stores. Of course, all these new stores are away from our southern heartland, which is an important part of growing our map here. Thanks, Clive.

Operator

Our final question is from Izabel Dobрева at Morgan Stanley. Please unmute yourself and begin with your question.

Simon Roberts

Hello, Izabel, good morning.

Izabel Dobрева, Morgan Stanley

Hello, good morning and Happy New Year. I had a couple of questions. My first question is to do with the acceleration of profit drop-through in the second half. I know that there were savings to consider, but I'm wondering why did you not accelerate price investments in grocery, considering that we might be heading into a more value conscious consumer environment?

Also, if I look at the Kantar market share gains, those are actually slowing on the latest readings versus what they used to be on a one year ago basis. What led to the decision to

not step up price investments in order to really build that volume momentum for the year ahead?

My other question is just your outlook for margin for next year. I think going back to the CMD, there was an expectation that there would be margin expansion because of the efficiency program and volume leverage. Since then, the cost environment has clearly changed. I'm wondering, do you think now it's more likely margin will be flat because of all of the different factors?

More in general, how do you think about the ability to pass on pricing in general merch versus grocery? My real question is, is there a danger that next year your grocery pricing will end up subsidising the general merch weakness?

Simon Roberts

Thank you. Well, why don't I take your question first of all on where we are on grocery value and within that, just the decisions we continue to make to be Food First. Then maybe Bláthnaid, just talk a little bit about how we'll talk to you about next year, is probably the best way of expressing it.

I think to be absolutely clear, we couldn't be more encouraged with the strength of our momentum right now, and that's powered by the strength of our value position. If you look at the data this Christmas, the most important message that we see from our customers is they're really buying into the strength of our value offer, our quality, and our service. As I've said before on the call, we exited Quarter three with the strongest value index against our major competitors we've seen for a long while. Our value position is where it's at and it's winning new customers.

As you know, we had a very strong comp last year and we knew that going into this Christmas, so we planned for that. I think we took rational and balanced decisions. It's not volume at any cost, it's the right volume for where we think the business needs to be based on the strength of the comp last year.

As you can see, the reason we can talk about profit leverage from the grocery business is the strength of that volume drop-through in the way we're delivering our year end. All of the work we've done on food to put food first back at the heart of Sainsbury's has been about making sure we make decisions to drive our food business above all else. That's exactly what you can see us continuing to do.

To the last part of your question, we won't make compromises because of weakness somewhere else that would compromise our food business and the strength of what we're doing in food. You can see it clearly in the numbers, you can see it in the strength of the two-year volume. Most importantly, you can see it in the customer satisfaction performance this Christmas, where we delivered our best satisfaction we ever have because we made those targeted investments. Bláthnaid?

Bláthnaid Bergin

Izabel, we're guided today to the middle of the range, in at least 500 million retail free cash flow. As you'd expect, let's close out this year and publish our results, and then we'll guide on next year when we come to the market in April.

The other thing I would really like to point out is the strength of the operating leverage in H2 in Sainsbury's. We achieved this, just to build on what Simon said, whilst achieving our best ever value position. We're really proud of the quality of delivery here as well.

Simon Roberts

Thanks, Izabel, thanks for the question. Just to check, are there any final questions?

Operator

We have one final question from Paul Rossington at HSBC. Please unmute yourself and begin with your question.

Simon Roberts

Hello, Paul. Good morning.

Paul Rossington, HSBC

Good morning, well done on the numbers. Just one quick one from me, could you give your views on what you think the outlook is for promotional activity and levels at wider industry into the next financial year? Thank you very much. That's it.

Simon Roberts

Thanks Paul. As Bláthnaid's just said, I think we should look April onwards, in April when we give our guidance for next year. I think the macro position, to your question, is, there's no doubt as I said in my comments, to how customers behave but value is no less important than it's ever been for all the obvious reasons.

We've seen a higher propensity towards promotions, and clearly, the loyalty programs such as what we're doing with Nectar have been a fundamental reason why so many customers have shopped with us this Christmas, and in fact through as our performance has continued to improve through 2024.

I think of course promotions are going to continue to be important, of course, we are going to make sure we stay super sharp on value. You can see that we are doing that as we've exited '24 and come into '25. As we look over the year ahead, as you just heard from Bláthnaid, we're really clear that our food business continues to grow because of the targeted and balanced investment choices we've been making to deliver for customers and to deliver for shareholders, and of course we're going to continue to do that as we look further out. Thank you.

Hopefully we've got to everyone's questions. Just a big thank you again for your time this morning. I'm very conscious it's been a very busy week for reporting in the sector, so thank you for giving us your time and all the questions this morning. I'm obviously looking forward to catch up again soon. We're very well set for the balance of this quarter.

As you've heard, we've confirmed our guidance for the year end; 7% growth year on year, very focused across the team as we've come into January, reset out of Christmas and good to go, and giving our customers the best offer that we can. Thank you for your time. See you soon, everyone.

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