Mitchells & Butlers 2015 Half-year Results Announcement
Thursday 14 May 2015

Tim Jones
Finance Director

Good morning, slightly later start for us than normal because we tried to sequence this to help you with other companies' announcements this morning. So I will crack straight on with the slides.

I am going to take you through the trading performance for the half year and then I will hand over to Alistair who will give you a little bit more in-depth commentary on our perspective on our markets - both how they have been and where they are going. And particularly what we are doing within those markets and the transformation plan we are taking this business through over the next few years.

But let me start with the P&L or the income statement. Total sales in the half year just over £1.1 billion, so that is 10% up on last year, both developing new sites and Orchid of course played a large role in that, but also like-for-like growth from our existing estate. And operating profit up to £153 million so that is up just over 4%. Slightly lower rate so there is a weaker margin there. Our margin of 13.7% is 80 basis points weaker than the first half of last year. Two real drivers behind that. Firstly we have got the impact of Orchid coming in. So until we realise the full value of the synergies on the Orchid estate, that is going to be a slight drag on the Group margin and I will come on and talk about that a little bit in more depth later. But also the fact that at the moment and for the last year the thrust of our sales growth has been coming from volume rather than price which of course is not as rich as it flows through the P&L.

At the bottom EPS up 6%, so still a strong EPS performance. I would point out to you that many of you will be aware last year we took the non-cash pensions interest charge that we used to report in exceptional, we now report that within underlying PBT. That actually increased by £3 million in the half year. So if I strip the impact of that out and look at EPS on the old basis or on a pure trading basis, then EPS would have been up just over 9% half on half.

Now let me take you through the various drivers and levers of the P&L, starting at the top of course with sales. Sales performance averaged out at 1.7% in the half year so stronger than we have been for the past couple of years. As you can see that was very much driven by strong food sales and a slightly weaker drink performance. The first half I have to say is slightly flattered by Easter which was in the second half of last year, it was in our first half of this year. So I will give you the week 1 to 32 which takes us to last weekend and if you like that is a measure that is clean of all bank holidays or one-offs and that is probably the best measure of a run-rate you have got for our first six months of the year.

I'd like to delve down into sales a little bit more as we always do and look at the two main products we have, food and drink, and what are the key drivers beneath those. And if I start with food, you have been aware for a couple of years now we have been looking to moderate spend and price increases to drive volume back into the business after a period in FY ‘12 and ’13 where we had quite steep negative volume. As you can see we have continued on that journey in the first half, price very moderately increased, a very strong increase in volumes and that has really been coming from a greater use of time slots across the day, trading in our sites and breakfast is a particular feature of that.

Drink, we have continued to take some price, although slightly less than we have in previous years. A small increase in the decline of drink volumes, not something we would see as significant in this period and it is probably as much related to the fact that where we have driven food occasions, they have been occasions that have been less associated with drinks than the other ones.

Looking at the operating profit or EBIT movement as a whole, again breaking that down. Last year £147 million in the first half. We have got a £6 million impact coming in from Orchid. We bought Orchid on 15 June last year so it is not in the comparator first half at all. Costs have been fairly benign in total, particularly energy and food have been in deflation for us in the first half so overall a benign cost environment. But of course the costs that we have the biggest exposure to is wages and national minimum wage is the key driver behind that. That went up 3% this year, it is going to go up by 3% another year. So actually that accounted for more than all of that £5m, and for about a £7 million headwind in the first half. And it is only deflation on the other items that has taken us down to £5 million.

Now we have got growth in the like-for-like estate. We have got the beneficial impact coming through from new sites that we opened last year, at the annualisation of our trading and then we got the slight diluted impact from pre-opening costs on sites that we are opening this year although they will start to contribute going forward. Our cash flow has been strong. We are making high contributions to our pension fund as you are all aware. And capex has been slightly higher in the first half than it was last year and I will come on and look at that a little bit later. But overall a strong cash performance and we generated, importantly, positive cash after funding our bond amortisation, that is £17m you can see at the bottom of that slide there. And that is the criteria and the profile that we need to see in place to start paying a dividend as a Group. So that is a decision that we as a Board will review at the end of the year and if we can see that profile in place then for us that is surplus cash that can be distributed.

Where the cash flow performance leaves us is net debt of just under £2 billion, so that is 4.4 times EBITDA. A slight decrease from the beginning of the year, but still an increase on pre the purchase of Orchid nearly a year ago now.

Capital expenditure increased slightly to £94 million, that increase coming through from maintenance capex where we have now substantially completed a lot of the infrastructure investments that we have been doing for the past two and a half years, in particular we have new tills, new EPOS systems rolled out across the whole of the M&B Estate and the new incoming Orchid Estate. We have also substantially completed our finance system and HR system replacements as well. We have also continued to invest a slightly increased amount actually in remodels in the period. In terms of expansionary capex, we have invested in 32 sites, 9 of those have been new sites and 23 have been conversions. We would expect that to be about 65 for the full year for about double what we did in the first half. Our returns as is set out on this slide as well, looking slightly stronger than they have been in previous periods.

Of course our largest element of capex if you like over the last couple of years is the purchase of Orchid, so a few words on that. We are very pleased with the acquisition of Orchid, we are very pleased with the trading that has come out of Orchid since we have acquired it and our integration plans are absolutely on track. We closed the Head Office exactly on plan at the beginning of the second half. That is now allowing us to realise £6 million of annualised savings. And the conversion progress plan is well underway. At the half year we have converted 14 Orchid sites to M&B brands. In the 4 weeks subsequently we have done another 7, so we have now converted 21 sites. We expect to do 40 or slightly more than 40 by the end of the year with the balance coming in FY16. I think crucially the initial returns that are coming out of those sites are in line with our expectations and are very strong. So we are very pleased with their progress. There will be of course a cohort of sites that we don't convert or at least don't immediately convert to M&B brands and they will be subsumed within our Heartland Estate and that is a process that will take place over the second half.

So just maybe wrapping up on the key messages there. We are continuing to see signs of the work on our business transformation come through particularly in strength and food volumes, albeit that is coming at a slightly short term dilutive impact to margins, exacerbated by the purchase of Orchid. But we are knocking off the milestones that we have been talking to you about for a year and particularly the infrastructure and investment now being substantially complete across the whole of the estate which gives us a great platform to deliver our improved service and initiatives.

And last, but not least, we have done that while increasing EPS by 6% or say 9% on a trading basis across the whole of the estate.

So with that I would like to hand over to Alistair to take you through our markets and our strategy.

Alistair Darby
Chief Executive
Well very good morning to everyone. I hope you have not been tempted to broach the can of beer you have been given by Marston's. I have tried to line up some eggs Benedict for afterwards, but Andrew Andrea advised me not to.

So very good morning to you. Thank you to Tim. What I want to do is I want to talk you through the progress we have made since we presented in November. We laid out a plan for how we were going to drive the business on and I really want to comment on the range of things we have done over the last six months.

Now back in November I talked about how could we fairly say we had returned this company from being a good company to being a great company. And I laid out five kind of hardnosed metrics that to me were the measure of the progress we are making. Now how have we done against those? Well I think we have made encouraging progress on like-for-like sales growth and clearly we have been aiming to get ahead of the market and the reason that is so important is that because over the last previous two years when we took a bit too much price, we lost volume and therefore market share. So we have been keen to win back market share. I think we are making encouraging progress. I am going to show you a slide a bit later about how we are doing against the market. So more to do but encouraging.

Tim has explained what has happened with margins. As expected margins have declined in the first half, principally because of Orchid and us continuing to drive volume. Clearly we want to drive the integration of Orchid and to improve margins going forward. So there is more to do on that front.

We are certainly starting to get better returns in freehold and I am really pleased with that. There is more work to do when it comes to the returns we are getting on leaseholds, working very hard on that. But I am pleased to say, when it comes to net debt and EBITDA, we have dropped debt and we have raised EBITDA so we are deleveraging this business which we think is an important feature of our story. And Tim has explained where we are regarding dividend. We are not there yet and we are keeping a very careful eye on our ability to resume that at a time that is appropriate and obviously by agreement with the Board.

So have we got to being a great company yet? No because we haven't ticked all of those boxes. Are we making good progress? Yes, I think we are and I am pleased with what we have achieved in the first half.

Before I go on specifically to what has been going on in the business, I would like to just make a few comments on the markets and what our views are in the market in which we operate.

The first thing to say is undoubtedly consumers are better off at long last, there is more cash in pocket, wages are increasing and with that consumer confidence is growing, this is good news. Clearly lower petrol prices and lower food prices is helping. But I think the consumer outlook is as good as it has been for some time and we are very encouraged by that. And I think that gives us encouragement for what lies ahead.

That then begs the question of course though, why is it that the market in which we operate has been a bit soft or softer over the last four months? And in this chart I show the Peach Tracker which is a tracker of like-for-likes in our sector. We are a contributor as are Spirit and Marston's and so on. And what is interesting is the rate of growth in the market has slowed in between, since the beginning of this calendar year. Importantly the market is still growing. It is not growing quite at the rate it was and that kind of begs some questions. Within that also restaurants have outperformed pubs and pub restaurants. After quite a long period of them lagging, pubs and pub restaurants, there is some interesting stuff going on in there. How might we explain this? Well I think we shouldn't lose sight of the fact that consumers are still carrying a very significant amount of personal debt and this is going to cause consumers to continue to be cautious and careful about what they do. There is some evidence that maybe ahead of the Election consumers saved a bit more just in case. Obviously there is a bit more certainty about where we stand now.

But one of the others theories is around, and I think it is quite robust, is that there has been a catch-up of previously delayed large purchase items, replacing carpets, replacing cars. Maybe people booking a better quality holiday this year, particularly with the pound to euro rate being more favourable.

We see all of these as being temporary effects and therefore we are still confident that rising consumer confidence is going to be helpful to us in the second half and beyond. The key is to have a business that has got a well ordered range of brands that have got a really clear idea of what guests need in each and every one of them. They have got flexibility to offer great value and to open up more time slots for consumers to use them during the day. And that is what we are all about.

So just a quick reminder, we operate a portfolio of brands across five market spaces. We think this gives our business resilience and a very good spread. Gives the opportunity to take advantage of changing trends. And we have set on a journey which is to grow the overall size of this business in turnover terms and to get a larger quantity or percentage of that turnover coming from the three attractive market spaces that we have identified: family, upmarket social and special. And that is really important for us because we want to increase the quality of the turnover we have got whilst at the same time protecting the very, very attractive, cash generative Heartland business that we have got, which creates a lot of cash for us, creates a lot of buying power for us. And we are very committed to.

And how are we going to grow this business in attractive market segments? Well clearly what we are going to do is grow the core business, we are going to seek to develop the business through single site acquisitions, 9 opened this year. And the Orchid conversion plan is obviously critical to that story. And Tim has already alluded to that and we are very pleased with the progress we are making.

Just in terms of where we have put our growth capital. As you can see here more than three-quarters of our activity in the first half has gone in those three attractive market spaces: Upmarket social, Special and Family. So we have opened 9 new sites, 8 Orchid conversions and 8 internal conversions and we have had one conversion and 6 Orchid conversions in Heartland and Everyday social.

Just worth quickly explaining why there are 6 Orchid conversions in Everyday social just to give a bit of colour on that one. When we bought Orchid they had in their portfolio a concept that was a Thai Restaurant above a white collar community pub. We did not want to maintain that concept, it was going to get in the way of our integration of the business and the closure of the Head Office and the obvious thing to do was convert those pubs to Ember which is our more premium community pub offering. And we wanted to get those Thai pubs closed and dealt with so we could close the Head Office in April. So that explains why there have been 6 Orchid conversions in every day social in the first half. That is converting them to Ember Inns. And we have been very, very pleased with the performance of those pubs, sending them back to being really good, high quality community pubs.

Let's talk a little bit about how we have invested in growth in the attractive segments I have talked about by talking about two pubs in particular to tell a nice story and really illustrate the point. The first pub at the top is the Sawyers Arms. This is a beautiful listed building on Deansgate in Manchester that we acquired with Orchid. And Orchid were running it as a pizza kitchen and bar, which is fine. Pizza kitchen and bar though has relatively limited food offer and relatively low pricing. This is a classic pub which was just screaming out to be Nicholson's. So we converted it by moving it into Nicholson's we have also been able to improve the cask ale range, put in craft beer, extend the food offer significantly and take a much more premium position befitting a pub of this quality and we are really delighted with the return we are getting from this business. We are now taking £18-19,000 a week in the business and a really good example of how we can shift a business from a marketplace where price is quite difficult to a marketplace where we have more room to manoeuvre and more premium options.

The pub at the bottom isn't a pub, it is a restaurant. It is our new Miller & Carter in Cardiff, next to the new St David's shopping centre. It used to be an old Habitat store. It is a very big Miller & Carter. We have really invested heavily in this site and this site is taking on average £70,000 a week, it has been absolutely fantastic for us. And a real example of how this kind of move towards premium and when you do it well as we do in Miller & Carter you can be extremely successful. It is interesting at this end of Cardiff we have now been joined by Burger & Lobster and that has built a real kind of hub of premium eating at this end of Cardiff which is fantastic and this has been an enormous success for us. Real examples of how we are investing to grow in those attractive spaces.

Now back in November we talked about three hard-wired guest behaviours that we were really going to focus on to drive this business forward. They haven't changed at all, they remain as critical now as they did six months ago. And that is coming out of austerity and recession, what our guests want is they are really careful with their money and want to get best value for money possible. So value and experience is critical. Flexibility is a really big thing now, whether it be people eating in the middle of the afternoon, whether it be them taking breakfast. The kind of death of traditional meal times stays with us and I think being able to spread our offer throughout the day in our businesses is absolutely crucial. I will talk a bit more about that in a moment. And brand is where all the action is. There is no doubt at all that after a long period of difficulty, people want consistency and certainty and reliability and we are in a very strong position when it comes to our branded portfolio.

So let's talk about what we are doing. First of all on that first need which is about value for money and this is all about having top teams that deliver exceptional experience allied to great value. We are really pleased with the work that we have continued to do on reducing staff turnover which has paid dividends. So we are now at 77% which is the lowest this business has ever been at, there is still a load to go at. And I am really particularly pleased with this because we are in a market where the market is tightening, so quite high employment, so finding it more and more difficult to find good people. And obviously there are more and more people coming into the market. So there is constant pressure on good people. So I am really pleased that we have continued to take retail turnover down, which is super.

We have also been investing very heavily in apprenticeships and that is absolutely the right thing to do. We are investing in the next generation of people who are going to work in our pubs, bars and restaurants. We have 1,500 apprentices working in our business, we have just launched a new 3 year apprenticeship scheme that will give people a really broad based experience in our business and further evidence of our commitment to young people.

But not only have we worked on turnover and employing young people, but we have also worked really hard on enabling our teams to do a better job. Good to Great and the culture change programme that we have been running over the last two and a half years is really embedded in our business and is now running in the majority of our business. And that gives people real accountability and responsibility to get on and drive their businesses harder.

And of course the rollout of our EPOS systems has played a big part in making life easier and more efficient in pubs. So we have installed and upgraded 1,700 systems in less than two years and it has been a massive programme for us. We have generated £5-6 million of productivity benefit, but on top of that we have increased speed of service, we have increased reliability of ordering, increased the amount of time that our waitresses for example can spend at tables looking after guests, a very important project for us which we are very pleased to have delivered in full.

The key for us though is value is a combination of price and experience. And clearly that varies on a brand to brand basis. So you take for example two bottles for £5. In our Sizzling Pubs customers want really good value and they are prepared to look after themselves in return for good value, so happy to order at the bar, happy to go and get their knives and forks from a stand. But the return for that they want really good pricing. So price plays a big part in the experience. If you take something like Miller & Carter, the menu on the top right, clearly price sits alongside experience. How good is my waitress? Am I going to get good recommendation? Is the steak going to be brilliantly cooked? The key for us is on a brand by brand basis, understanding absolutely what is the balance of price and experience to really get that brand firing on all cylinders and we are very clear about that.

Moving on, flexibility to eat and drink when and where it suits me and this whole point of offer extension. Of course we have talked a lot about breakfast, but this is not just about breakfast in our business. Yes we have grown breakfast very significantly in our business and by the end of this year we will probably be selling something like twelve million breakfasts a year, something like 10% of our meal volume. But we have also grown our coffee business very, very significantly and this is in line with people stopping in the middle of the afternoon to have a coffee, a cake, take a bit of a break. And certainly what we are seeing is consumers are tending to eat more often, but less on each occasion. So the key is to have an offer and offers in our businesses that is really flexible, stretches from the beginning of the day right to the end of the day. And that is certainly one of the other things we have been doing is extending for example the opening times of our kitchens later into the evening to address people wanting to eat later.

Now as far as breakfast goes, Tim has mentioned the point about margins, breakfast is making a strong contribution to our profit. Yes it is lower margin, it is very competitive market, but we are very pleased about the contribution it is making to our business and it is really important we are competing not only in breakfast but in afternoon tea and so on because that is how the market is going. Importantly though, don't just see breakfast as low price. We offer breakfast across all of our brands and clearly we go from fantastic value through to really premium offers. So if you look at the range of breakfast offers here. We have our Harvester £4.99 breakfast, but if you can make it out in the middle and I was hoping to serve you some today (but the Nomura team weren't up to it, only joking!) is Lobster Benedict there which is served in Browns at £16 a plate so that gives you a real idea of how we are stretching breakfast from unbelievably good value all the way through to premium at the top end. So it isn't just about a price, back to my point about price and experience.

Now brands. Brands is where the action is as I have been explaining. There has been a huge amount of activity in the branded sector. If you look at all of the new entrants coming to market, they are generally speaking on the branded formats. And it is you know what brands offer, they offer reliability and consistency. In our case a lot of our brands offer fresh food, terribly important for families. So the salad bar in Harvester, and unlimited vegetables in Toby Carvery, are really critical. Brands also offer outstanding value.

I think the best way to illustrate the power of brands is to take you through two of the Orchid conversions just to show the impact of converting from unbranded to branded because I think this really brings this to life in terms of the consumer impact.

So let's start with the Halfway House which was an unbranded Orchid carvery in Southend. Now this was a really good pub, it was already taking £22,000 a week which is about our average weekly take and we converted it with a significant investment to a Toby Carvery. Now first thing is it looks substantially different, secondly it benefits from the branding of the number one carvery business in the UK and the sales uplift has been £14,000.

I think the point here is, yes we have invested capital in the pub. But a chunk of that turnover on growth has undoubtedly come from it being recognised as a Toby Carvery and I think that is a very substantial uplift and we are very pleased with the return we are making on that site, in excess of 30% and I think that really gives you and shows you the power of that brand in that particular site.

Now going on to the next one, this is a pub called the Hobby Horse which sits in Chesterfield, it sits on a Leisure Park next to a cinema. Frankie & Benny's nearby. And this was an unbranded two for one pub in need of investment, it hadn't been touched for quite a long time with a play barn associated with it. We converted it to Harvester, much more appropriate for that family led market in that location and again seen a very, very strong uplift £14,000 per week and will expect to make a return in excess of 30% on that investment.

And I think that really illustrates the effect of getting a well known brand into locations where people expect to find brands. The Hobby Horse as an unbranded two for one pub sat uneasily in that Leisure development where consumers are looking for certainty and reliability, speed of service and so on. So I think that gives you two really clear views on the value of branding.

Now we came out of the last financial year with food volumes just back into growth and I am really pleased that as you can see form this chart that has not been a flash in the pan. We have continued to drive very hard and have got good momentum coming into the second half. And I think we have been able to do that by growing the occasions when we serve food, by being disciplined on pricing. We are in an environment as somebody has coined us where there is no inflation. And consumers are particularly live to price increases or indeed tend to kind of reject them. So we have been very careful and disciplined on pricing.

The other thing though I am absolutely sure has driven this improvement is the fact that our experience in pub is getting better and better and you can see there the net promoter score has grown by two points to 65% and that is driven by our people fundamentally delivering better service and experience to our guests. So I am really pleased with that and think it should give you real confidence about the kind of direction of travel in this business.

Of course that then leads us to the inevitable question about how we are doing against the market. And I am pleased to report that we have undoubtedly made progress here. So the yellow line is the average of the Peach Tracker, the only available data in terms of how the market is performing. And as you can see that in FY13/FY14 we underperformed the Peach Tracker significantly. And we have really started to fight back through the second half of last year into the first half of this year and in March and April of this year we are on the market/slightly ahead. So clearly we are going to continue to drive hard to get ahead of the market. That is one of the key objectives of this business. Like-for-like sales growth ahead of the market. So I am really, really pleased that our growth is really flowing through so relative to that performance gap.

So what is the outlook for the business? Well we operate in a dynamic and demanding market. Now it was ever thus and you would not expect me to say anything different. Competitors are doubty, consumers are very demanding and we have got to believe that there are some cost headwinds around. So although we have been very pleased to have taken advantage of cost deflation around utilities and food. We must remember that labour is our single biggest cost and national minimum wage is going up by 3% this year. So we expect there to be ongoing cost pressure on labour and in a tightening employment market that is probably going to mean pay rates are also going to be under pressure. So we have just got to keep an eye on that.

However we are set up to deal with that, we have a very clear focus on value, on flexibility of offer and a very strong branded business that will enable us to be successful. And we are very clear about what we need to do on a brand by brand basis to win for the guests who use these brands and to win market share. We are very pleased with the strengthening food volumes, a key driver for us recovering that and that has fed into like-for-like sales progress. Over the last two years our like-for-like sales were pretty pedestrian. We are very pleased that we are beginning to break out of that cycle and that is why we are confident that we are well placed to grow further shareholder value in the next six months and beyond.

So thank you very much for your attention. We would be delighted to take any questions you have got.

Q&A Session

<u>Question 1</u>
Jamie Rollo, Morgan Stanley
Good morning Jamie Rollo from Morgan Stanley, three questions please. First of all in terms of the margin progression in the second half of the year, you have clearly got some things in your favour like the Orchid savings and maybe some price increases. Can you talk a bit about your expectations for group EBIT margins?

Secondly on the free cash flow bond amortisation, the fact it is positive was mainly due to the working capital inflow. Is that inflow just the Orchid impact and if not would you expect a similar inflow at year end which could clearly impact your pension decision?

And finally, what were Orchid's revenues in the first half please, I didn't see that in there and what was its like-for-like growth in the un-invested estate? Thanks.

Answer:

Tim Jones:
In terms of margin I think our full year margins will be down probably 30-40 basis points, so less than the half year margin is down. And that reflects some of the synergies starting to come through from Orchid, we closed the Head Office as I said, we are kicking in with all of that. And also I think you will see in the second half in the core M&B Estate, we start to have an increase in our spend per head. So that volume and spend per head price line I think you will see that starts to come up a little bit, which will help our margin. Some of it might be price, a lot of it is trying to stretch people up the menu as well. So a mix, not pure price. So a strengthening in our margin but it is not going to get to a flat margin for the full year, it will be somewhere between the two.

In terms of working capital, it is not all Orchid, some of it is just the reverse of the 53 week year we had a couple of years ago and that sort of goes away. I don't think you should expect to see the same working capital influence in the second half. I think you might see, we might hold onto what you see at the end of the first half so don't double up I guess is what I am saying.

In terms of revenues, Orchid turnover was just under £70 million in the first half of the year. Like-for-likes across Orchid have been fine, they have been fairly flat. There is an un-invested estate that is on a difficult trajectory. But we have been doing some remodels and that is having a big impact and that feeds into their like-for-likes as well. So like-for-likes have been fairly flat but below the M&B average.

<u>Question 2</u>
Tim Barrett, Nomura
Tim Barrett from Nomura, can I ask two things. Firstly on the Heartland Estate, the value end of things. It sounds like some of your competitors are struggling. Are your like-for-likes positive now in that segment and what do you attribute that to?

Secondly, can you remind us what the template is for the Orchid conversions? How much you are investing and is more than 50% uplifts like in Southend a good example?

Answer:
Alistair Darby:
Heartland like-for-likes, we are really pleased with the new growth in the first half. In fact we have growth across all of our market spaces which is really encouraging which is quite a change from where we were previously. I think we are seeing growth in Heartlands because we have slowly but surely seen the benefits of all we have been doing which have begun to gain traction and so we are very pleased to see progress in that market.

I also think that for us, our view is that people on lower incomes are beginning to see a bit more cash in their pocket and that is feeding through for us so we are encouraged. And if you look at some of the economic performance in Heartlands for us like the West Midlands and the North-West, actually regional performance has picked up so that is good news for us.

So we have seen some encouraging progress in Heartlands. As far as Orchid?

Tim Jones:
In terms of Orchid there isn't really a template as they go into different brands. So of the 90 or so sites that we have currently identified for conversion, 20 will be Harvesters, about 20 will be Toby's, about 20 will be Embers and about 10 will go to Vintage. Somewhere in the single digits, 7 or 8 Castle. There is one Browns in there. So the conversion cost is going to vary quite a lot across that. So I mean if you look at it in total if you like, roughly 90 conversions and about £38 million of conversion in capex. So that will give you an average, but it is going to vary quite a lot by site within that average depending on the size and the brand it is going to.

Further question
Sales uplifts?

Answer:

Tim Jones:
In terms of sales uplift, obviously early days at the moment, but we are getting in excess of 30% sales uplifts consistently.

Question 3

Alexander Mees, JP Morgan Cazenove
Thanks it is Alexander Mees from JP Morgan, Cazenove. Three questions for me please. The first one is an easy one, just on the maintenance capex. Given that the EPOS project is now completed, can you give us some guidance as to what you expect for maintenance capex for the balance of the year?

The second one, I wonder if you could just put a little bit more colour on your thinking around pricing and volume. Clearly there are strengthening volumes in food, does this give you any comfort or confidence to think about the small disciplined price increase?

And the third question is I wonder if you could comment on your like-for-like performance since the start of the second half?

Answer:
Tim Jones:
Maintenance capex for the full year is going to be around about £120-125 million. Like-for-likes since the half year, so we have disclosed weeks 1 to 32 and 1 to 28. So there is four weeks since the half year and they are negative but the reason they are negative is because they are up against Easter. So that is why we want to disclose those because the first half is flattered a bit by Easter. By the time you get week 32, that has washed through which is why I would advise you to look at weeks 1 to 32 as the untainted if you like like-for-like performance across the half year, even though it is a slightly longer performance. If you strip Easter out we are clearly positive in the other weeks and quite nicely positive actually, but just the impact of being up against Easter makes us negative in total.

Alistair Darby:
In terms of pricing and volume, we want business to grow in volume so winning back market share, clearly not at any price. Our view though remains that consumers are very sensitive to price increases and therefore as Tim said in his presentation, we have got to move prices but in a very nuanced way and I think rather than just putting price on items that people are very familiar with it is by giving people more choice or opportunities to premiumise up the menu. So for me a really simple way to describe that is if you take Vintage Inns for example, one of our single biggest selling starters is breaded mushrooms so we have added onto Vintage menus alongside the breaded mushrooms, mushrooms in a cream cheese sauce for about a pound extra. So that is, if you can get people to trade up to that then you have effectively engineered a price increase without hitting directly breaded mushrooms which people are very sensitive to.

So that is Tim's point about stretching and providing more premium options and providing more premium options on the wine list as well, so giving people the opportunity to trade up. And I think that is going to be where the battle ground is, so it is about more choice, more interesting items. Giving people dishes they have not experienced before and you can gain a higher price point for rather than just going straight after the price of fish and chips which is probably not the best way to do it.

Question 4

Richard Taylor, Barclays
Morning, Richard Taylor from Barclays. Three questions please. Firstly on the dividend, Tim you seemed to hint in your section slightly greater chance of that happening sooner rather than later. But the net cash flow is only up £2 million year-on-year even with that working capital. Could you clarify the point there?

Secondly on wage inflation, are you paying 3% more absolute minimum wage or are you having to go up a bit more than that given extra supply coming into the sector and more competition and so on?

And finally, I know bond yields have been moving around quite a bit, but can you remind us of the sensitivity to your pension with bond yields given we are five months away from the next one?

Answer:
Tim Jones:
So around the dividend, nothing has changed with the dividend, our criteria is absolutely the same as we have always been communicating for the last 3 or 4 years and which we have committed to with the Pension Trustees. Absolutely nothing has changed there. I think it is helpful just to tell you the half year looks like dividend, to bring it to life a little bit. Whether we can get there or not at the full year will depend of course on the second half cash flows and capex spent on trading etc. And the reason why it is harder for me to say anything more specific as you quite rightly say Rich, it is sort of on the margin. If you look at most of your forecasts it is very, very close. So £5 million either way could put us in that position. So it is very difficult to make a call on that now, but we will rigorously apply that criteria. As long as we can create sufficient to the headroom there to pay something that is not you know a nonsensical dividend, then we will once we have that headroom with the cash flow, but it is a finely balanced formula at the moment. And nothing has changed in the criteria.

In terms of wages, I mean certainly minimum wage is your best proxy for modelling our forward going staff costs. We do pay above minimum wage in certain places in London for example. I don't see that getting worse at the moment, although I suppose if you cycle through the economy for a couple of years and you delve in terms of economic conditions, then there could be some pressure there, but that should come along with a more benign consumer environment as well. So that should be more affordable and should give us more pricing power. But at the moment that is not an acute issue. Minimum wage is really the index forum.

Bond yields. Ten basis point decrease in bond yields adds about £30 million to our pension deficit is the sensitivity. I was a bit worried after the election that they were going to plunge down further, but the last few days they seem to have come back a little bit. So we are not a million miles away from where we were ten days ago.

<u>**Question 5**</u>
Jeffrey Harwood, Stifel
Jeffrey Harwood from Stifel. Could you give some more detail please on trading by brand and also by geography?

Answer:
Alistair Darby:
I think the encouraging thing is that if you think of our star on our five market spaces, we have got growth across all of those segments. It probably would come as no surprise that the strongest level of growth is in an upmarket kind of drinking brands like Nicholson's and Castle that are biased very heavily towards London. So we are

seeing our strongest growth is in those brands that are heavily exposed to London. But encouragingly you have got growth across all market spaces. So that is very, very good news for us. And that is actually quite a shift from where we were a year ago for example where there was a lot of pressure on our Heartland Estate.

The second part of your question Jeffrey was?

Jeffrey Harwood
Geography?

Answer
Alistair Darby:
Thank you. In terms of geography, there has been lots of talk about London kind of slowing down. Our view is that London may have slowed down a bit, but it is still growing and it is growing at a rate that is still ahead of the rest of the UK, so you have got to keep that in context. What is encouraging though is that there has undoubtedly been a step up in performance of the regions, notably West Midlands and North-West have actually looked a lot more perky over the last year. There are still some areas and regions that are tough. I think Scotland is tricky and the North-East remains tricky. But in aggregate we have seen a much stronger performance in the regions. So London's growth rate has softened a little, the regions have got stronger, the relative gap therefore has closed. That is probably the best way to think of it. But recognising there are still some regions in the UK that have got quite a lot of ground still to make up.

<u>Question 6</u>
Simon French, Cenkos
Morning it is Simon French from Cenkos, three from me please. Just thinking about current trading in another way, could you split out what Easter did this year versus Easter last year in terms of like-for-like performance please?

Secondly when do the procurement synergies from your Orchid acquisitions start to kick in?

And thirdly, in terms of your Heartland Estate, as the consumer recovery accelerates how many of those assets do you think you can shift into other parts of your marketplace?

Answer
Tim Jones:
Easter's like-for-like growth was 4.1% across all of our Estate. Our restaurants did particularly well and pub restaurants and pubs were similar. So pretty strong weekend. As has been Mother's Day, Valentine's Day and Christmas, all of the key events this year have been strong for us and certainly have all been well ahead of the average like-for-likes that we have seen across the whole of the 32 weeks.

Orchid synergies, well some are in already, so where there are, the quicker and easier synergies to put in are stuff on power, subject to contracts. A lot of them depend on conversions because we need to get the sites onto different supply chain. We use Brakes and Tradeteam, for example to be able to realise some synergies so they come through as we convert more sites. So you will just see them, we have got some already and you will see them increasingly come through the Estate over the next two years really on an ongoing basis and will just accumulate and the margin will strengthen with them.

Further answer:
Alistair Darby:
In terms of the Heartland question, opportunities to move Heartland sites up into more attractive market spaces, I think the answer to that is there probably will always be some opportunities at the margin, but not significant. And the reason I say that is that this is an estate of pubs that has been worked on very hard over the last ten years or so. So we are pretty content with the shape and position of the estate. We always seek at the margin, to shift a pub up to, I don't know, convert to Harvester, to a Miller & Carter for example if there has been quite a significant demographic shift in the area. But we are pretty confident that the Estate profile and the way it is balanced out is correct.

There probably is just one nuance to that though. There are a chunk of pubs that we bought in from Orchid that had recently been invested in by Orchid so substantial capital investment and it would be foolish at this point to go pouring more capital into them. We will probably go back around those sites that will sit in Heartland for now, in 2 or 3 years time when the benefit of that capital comes to an end and I think there will be more opportunity to shift some of those up into Harvester, to Toby for example and other sites. So it does not make economic sense to put capital into them now.

The one thing I would say though is that of course, don't just see Heartland as not being an opportunity to get a bit more price and a bit more premium. I think you know, back to this point about value and experience. The British consumer is pretty adventurous, well travelled, prepared to eat pretty exciting things and we are always very careful not to underestimate people who use our Heartland pubs who might be a bit tight for cash, they are still keen to experiment and try things unusual and with that goes the opportunity to charge a bit more. So we are always looking within Heartland for the opportunity to actually premiumise the offer within that sector. So we see an opportunity for people to trade up in Heartland just as much as we see people opting to trade up for example in Browns or Miller & Carter.

Question 7
Simon Matthews, Goodbody
Simon Matthews from Goodbody, just three from me. In terms of the spend on EPOS I think that was supposed to come in around £33 million, can you confirm where it came in and if you are substantially complete there?

In terms of remodels, how many did you do in the period and what was the spend on that?

And then finally on the dividend, my understanding was that once the dividend was initiated that that payout ratio is more or less fixed because of the agreement with the pension trustee, can you clarify if that is the case or have I got that wrong?

Answer
Tim Jones:
EPOS yes it came in just over £30 million, two-thirds of that is capital, one third was revenue. Substantially complete. Whilst we have new tills throughout the whole of the Estate, some of our more restaurant brands are getting table management software and we are doing some web interface work that is going on for the next couple of months. So that is why the word substantially is in there, they will all be done by mid-summer.

Second, remodels. We did what we considered to be 90 sort of full remodels and about 30 what we would call sparkle, so much lighter touches. They are included within our maintenance capex, don't normally break that down by category, but most remodels will come in around about £150-200,000.

And in terms of dividend there are two features of the criteria, I think your understanding is correct, but we agreed a criteria when we would initiate dividends which is this amortisation point. And then we would agree an escalation parameter once the dividend started and that was that we would not grow the dividend faster than the higher of general inflation and EPS growth.

Further question
Yes I guess once you initiate that then you are stuck at that level effectively for ten years is it?

Answer
Tim Jones:
No, the agreement with the Trustees runs out in June 2017. So it was an agreement that was intended to take us to the next Triennial which is next March so it then runs past that in the period you have to make that agreement. Because when you get to the next triennial it is all up for grabs again really, we do a fresh evaluation and see where we are. But it is not a perennial agreement that technically ends then.

<u>Question 8</u>
Nigel Parson, Canaccord:
Good morning, just a quick question on breakfast, did you say your turnover was already 12% on breakfast and is that where you want to be? And have you noticed any intensification of competition with Wetherspoon pushing hard in this area?

Answer
Alistair Darby:
No when I was talking, I was talking number of meals. So we sell something like 135 million meals per year. If our breakfast business gets to 12 million by the end of this year which is on track to do, you are not far off 10% of our meal volume, not quite, but getting there. So 10% of volume not sales. Obviously breakfast is a lower ticket price than lunch or dinner for example, so think of it in terms of volume. Volume contribution being close to 10%.

In terms of competition, our view on breakfast is that this is a growing occasion. Obviously there are more people coming into it. It has always been a very competitive sector and this is not suddenly breakfast has come from nowhere, if you think that McDonalds have been doing breakfasts very successfully for many, many years. I think what we have just, our view is on breakfast and tea and different kind of meal times is that what has happened as a result of the difficult period we have been through is that in order for people to stay in work, they have priced themselves back into work and also prepared to be much more flexible. So you can see people who are starting work at 11-12 o'clock for whom breakfast is a key meal before they go off to work for example. You can see people starting much earlier in the day finishing 2 o'clock and that kind of afternoon meal or a cup of coffee and a cake is a refuel at the end of the working day. So I think this kind of breakdown of traditional meal times, this more frequent eating but maybe less at each meal is just because people are just working much more flexibly in order to stay in work and that explains a bit I think how the UK over the last few years has managed to keep employment or unemployment relatively low considering how difficult things were. And that for us is why there has been such a spread of occasions where people are eating and why. You know you have got to be on all the time right from breakfast all the way through to the end of the day.

Closing remarks
Right, well thank you very much indeed and we wish you a very good day.

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