Please note, this transcript has been prepared by our third party webcast provider and is not reviewed by Tesco

Tesco PLC 3Q and Christmas Trading Statement

Thursday, 14th January 2021

Operator: Today's meeting will be hosted by Ken Murphy, Chief Executive Officer, and Alan Stewart, Chief Financial Officer. Today's call will be audio-only. Throughout the call, all participants will be in a listen-only mode, and afterwards there will be a Q&A session. Questions will be taken via the phone line. If you wish to ask a question, we recommend dialling in early as possible to avoid delays. Just to remind you, this call is being recorded. To start the meeting today, I'm pleased to hand you over to Ken Murphy, Chief Executive Officer. Please go ahead.

Introduction

Ken Murphy

Chief Executive Officer, Tesco PLC

Thank you, Tracy. Good morning, everybody, and a very happy new year to you all. Thank you very much for taking the time to join Alan and I this morning. I'll start by sharing a few reflections on Christmas performance, and then I'll talk to you through our ongoing response to the pandemic before we open the call to your questions.

We knew going into the festive period that this was likely to be a different celebration. And so, I want to start by thanking our colleagues for their heroic efforts in ensuring our customers could still celebrate Christmas this year. There was a lot of uncertainty, but the business responded with a real sense of teamwork. And everyone from stores to distribution through to our product and customer teams played their part brilliantly.

This was our sixth consecutive Christmas of growth and a record performance. We outperformed the market for each of the six weeks over Christmas, and we saw net switching gains from all key competitors. We had a really strong Christmas campaign and our ads got particularly high ratings with customers for effectiveness and emotional engagement.

Detailed planning ahead of Christmas ensured our customers could shop safely. And the comprehensive preparations for Brexit meant that we smoothly managed any potential for disruption. Our supply chain team did a fantastic job. And despite all the challenges, product availability reached record levels in December. Our customers also planned ahead.

Customers shopped a little earlier than normal with our busiest shopping day being on 21st December. To give you a sense of the scale, our colleagues sold over 110 million products on that day. All our formats and channels grew, but I want to call out this record Christmas for online. Online sales rose over 80% versus last year and over Christmas. We delivered more than seven million orders.

We continue to lead the market online capacity and we have more than 786,000 vulnerable customers registered with us, who were eligible for priority access. We have a fantastic range for customers this Christmas, offering both high quality and great value with more customers celebrating at home, many took the opportunity to treat themselves, find the sales grew over 14% this Christmas. Our customers enjoyed 69 million individual Finest mince pies and took home nearly eight million bottles of champagne and sparkling wine.

A demand for large turkeys was unsurprisingly lower this year. Our smaller meat products sold really well with, beef steaks over 100% growth and sales of our smaller finest roasted Turkey breast up 190%.

In the run up to Christmas, our research told us that over a third of households were going to be catering for an alternative diet this year. And to make that easier, we had our biggest range of plant-based Christmas food available, including nine vegan centerpieces. Our Plant Chef pigless blankets were favourite. Customers ate their way through 650,000 of them. And overall sales of the Plant Chef brand were up 90% in the run-up to Christmas.

More broadly, sustainability was important to many customers this Christmas. We took 20 million pieces of plastic out of this year's Christmas range. And by the end of December, we'd hit our target to remove a total of 1 billion piece of the plastic from our business. The work we had done on value also put us in great shape to.

We’re the most competitive we have been in nearly a decade against the entire market. And since Aldi price match launched in March, value perception has increased by 450 basis points.

Clubcard prices launched in September. And since then, Clubcard app has gained another two million active users. 80% of transactions in large stores now use a Clubcard. More broadly on the brand, we also saw a marked improvement in the overall brand health index over the period. In Ireland, total sales grew by 12.4% over Christmas, with a really strong performance in our large stores. All the work that has been done to improve the customer experience really came together as Christmas.

Online is a big focus in Ireland too, where we are the clear market leader with online sales up nearly 70% as we increased capacity to support record demand. Booker has done a fantastic job in very difficult circumstances. Total sales grew by 12.4% in the 19 weeks, and by 6.7% over Christmas, with a strong performance from the retail side of the business, which continues to support thousands of small business and independents.

The catering market was heavily impacted by restaurant closures at Christmas time with catering sales down nearly 50% over Christmas. While of course, that would weigh on Booker's profitability this year, it will play to continue outperforming the industry in what is a very difficult market.

Total sales in Central Europe declined by over 4% this Christmas. The team were well set up to serve customers in Central Europe, but sales were impacted by COVID-19 restrictions, such as limits on the sale of non-food, evening curfews and Sunday trading bans.

Now turning to COVID-19. This has been a really difficult year for so many people. We talk often about the professional challenges that our colleagues have faced, but I'm very aware that it’s had a personal impact for all of us too. I'm so proud of the Tesco colleagues. And more broadly, retail workers were digging deep and carrying on day after day looking after customers.

Throughout the pandemic, we have been very responsive to all the challenges that it brings. Our approach remains the same to provide food for all, safety for everyone, support for our colleagues and help for our communities. Our current estimate of the costs associated with our response to COVID-19 is around £810 million for the full year.

The most significant cost is people. As we support our colleagues with paid absences and have recruited thousands of temporary colleagues, we have also had one-off costs such as screened on signage, as well as the ongoing costs of things such as increased hygiene, which we expect to be with us for some time.

On food for all, as I mentioned, availability has held very strong throughout the period. And I want to thank all our suppliers for their partnership. I'm very proud that the 2020 Advantage Survey, suppliers named Tesco as the number one retailer for collaborations during a crisis. This week, we have extended our improved payment terms for the smallest suppliers until the end of our next financial year.

Since the start of the pandemic, we have made significant investments in safety and social distancing measures across every one of our stores, so that people can shop safely and with confidence. These include limits on the number of customers in store, a traffic light system in more than 1,300 stores, social distancing signage, sanitising stations, protective screen that checkouts and face coverings and other protective equipment for colleagues.

While I'm grateful to the vast majority of customers who have been supporting our measures throughout, this week to further protect our customers and colleagues, we strengthened the rules on face coverings so that we won't let anyone into our stores who isn't wearing one unless they're exempt in line with government guidance.

In response to the latest government guidance, we have asked our 7,000 most vulnerable colleagues to remain at home on paid leave. We have seen an increase recently in colleagues needing to self-isolate, but over Christmas, we had support from around 35,000 additional temporary colleagues on top of the 11,000 we would usually hire for the Christmas period.

I'm delighted that many colleagues who joined for Christmas will be staying on in the coming weeks. I am so grateful to everyone for getting stock in. And I'm very confident we will continue to deliver for our customers every day. In 2020, we did what we could to help communities across the country. And over the last year, we donated over £60 million worth of meals to food banks and charities, including a £4 million cash donation to fair share on The Trussell Trust to support them through the busy Christmas period.

So, in conclusion, I'm really proud of the business and everybody in it. As I mentioned at the beginning, every single colleague has stepped up for customers. Our focus on looking after our customers, prioritising safety, service and availability, alongside great value has contributed to a record Christmas. And I'd like to say a big thank you to the whole Tesco team for their efforts.

And with that, I'm happy to take any questions you might have. Thank you.

Q&A

Operator: Thank you. If you wish to ask a question, please dial star one on your telephone keypad now to enter the queue. Once your name is announced, please go ahead and ask your question. If you find it's answered before it's your turn to speak, you can dial the hashtag to cancel. So once again, that's star one to ask a question or hashtag to cancel. There will now be a brief pause while we register your questions. Thank you. Our first question comes from the line of Andrew Gwynn of Exane BNP Paribas. Please go ahead. Your line is open.

Andrew Gwynn (Exane BNP Paribas): Hi there. Good morning. It's almost like announcing the winner of a result but it's taken quite a while. Anyways, so just two questions for me. You've mentioned there a couple of times obviously the COVID costs have stepped up more recently and clearly a painful situation for many people. I'm just wondering to what extent would you expect those COVID costs to drift into the next financial year? Obviously, I appreciate that's difficult question to answer, but some early thinking there would be much appreciated. And there's obviously – aside from the obvious, the other big feature of Christmas for me certainly in store was the Clubcard initiative. So obviously shifting promotions, almost exclusively onto a Clubcard. Just wondering if you can elaborate on how that impact of the business, any kind of material takeaways you would talk about? And then also just very briefly on the Clubcard Plus, I mean, maybe it feels like that's beginning to build up a bit of ahead of steam, but any statistics, any numbers you could share would be very much appreciated. Thank you.

Ken Murphy: Hi Andrew. Many thanks for the questions. On the COVID costs, I think, the truth of it is a lot of the one-off costs I think that you could say are in the rear-view mirror. But that the cost that kind of linger with us are a combination of people costs and the ongoing cost of maintaining safety in the store, so sanitisation, etc.

And really the biggest cost by far is the people cost. And that is quite simply going to be a function of the rate of infection and the need to shield people and the continuing abnormally high demand levels. So, what I think you can take away is that that as infection rates subside, as the restrictions ease, as people start eating out again, as the need to shield people reduces, we will see a corresponding level of reduction in COVID – ongoing COVID-related costs.

What I can't guarantee is they'll disappear completely. I think we will see ongoing sanitisation costs, ongoing kind of social distancing for some time, and that we expect those to last well into the New Year. And of course, we'll also, I think, see a sustained demand for online delivery, etc. So that's our early thinking.

I think it feels really early or premature to try and put a number on that. But we're staying very close to it, and of course we'll give you hopefully a more precise update at the year end.

In terms of Clubcard prices, we have been very clear that our strategy has always been that Aldi Price Match is all about underpinning value. Rather than it being a kind of a leader of and a driver of shopping, we think it's designed to eliminate a negative. So, it eliminates a reason why you wouldn't shop Tesco because we're reassuring customers that the value, they'll get in Tesco is as good as the market-leading value, which we think encompasses the whole market, not just Aldi.

Clubcard prices is really all around rewarding our most loyal customers. And that we have found to be very successful. And we are continuing to see kind of increases in participation. As I mentioned, there has been a surge in Clubcards usage, and a surge in digital downloads of the app, which we think is part of the journey that we are going on to make sure that we are able to respond to all the individual needs and wants of our customers, and in particularly of our best customers.

With Clubcard Plus, we're happy with the way Clubcard Plus is going. I don't have any specific numbers to update you on, on that. I might pass you over to Alan, who might put a bit more colour on it. It remains a strong offering for a proportion of customers and they tend to be very high value customers. So, it is highly valued by a part of our customer subset. Alan, anything you want to add to those.

Alan Stewart: Thanks Ken. Morning, Andrew. The only thing I'd add is that it's clearly a proposition, which is aimed at in-store shopping. We've seen very strong in-store shopping. We haven't majored on it because of all of the other aspects but we're very clear that it continues to be part of our armoury going forward and we expect that to continue. But it hasn't been a major focus when I say the increased the course of the last year really because of all of the things we've been talking about.

Andrew Gwynn: Okay. Thanks guys and happy new year. Thanks.

Ken Murphy: Happy new year, Andrew. Thank you.

Operator: Thank you. And our next question comes from the line of James Anstead of Barclays. Please go ahead. Your line is open.

James Anstead (Barclays): Good morning, Ken, Alan. A couple of questions for me, if that's okay. So firstly, on Booker. You mentioned that you think it's outperformed the catering market as a whole. I wonder if you can just remind us roughly what Booker's share is in the catering market? And if it's possible, if there's any idea on how much of share you can just gain this year? And perhaps whether that share gain has accelerated as years gone on? So that'd be one question around the Booker and share. And the second thing would be, I know that Tesco doesn't typically like to comment on competitors on these sorts of calls. But clearly one of your big lists last year was Aldi Price Match. And I wanted to know whether you've seen any sign of Aldi reacting and bringing down its own prices? Thank you.

Ken Murphy: Thank you, James. So interestingly enough, we tend not to get overexcited per se with market share in the distribution market for catering, because barriers to entry are very low. It's a fickle market. Both customers and distributors enter and leave the market on a regular basis.

And really the focus of the Booker Team has always been around the quality of earnings and the quality of business that it maintained. So, it has been focused on winning share with the best customers in the catering market and it continues to do so. We don't get overexcited about market share because this is a market that's 10 new distributors will appear overnight in the catering industry.

I think where Booker has been brilliant is that it has really focused on making sure that it all was looking after the best quality operators in the market and making sure that they get the highest standards of customer service. And then, of course, typically they're the ones that weather the storm the best and therefore our relative share of market grows, and we grow with them.

So, I don't particularly want to put a precise number on it. Alan may wish to add more value or have more commentary to that. But all I can say is that our expectation is that Booker will emerge from this crisis as stronger business, even stronger than it is today.

In terms of Aldi Price Match, of course, we have seen Aldi react and we have responded to Aldi. I think what they have realised and what the market realised is our determination to maintain great value for customers. And I think if – they see it and we see it not in any way as a price war at all. We see it – they see it as much more kind of a statement of intent that we will provide good value and we will respond in whatever way we need to. And that I think has meant that we've been able to kind of maintain that position without destroying value. And I think that's really the important message.

James Anstead: That was really helpful. Thank you.

Ken Murphy: Thanks, James.

Operator: Thank you. And our next question comes from the line of Nick Coulter of Citi. Please go ahead. Your line is open.

Nick Coulter (Citigroup): Good morning and happy new year. Three, if I may please. Firstly, would you be able to share the exit rate or latest number of orders per week for the GHS, and broadly how that breaks down by delivery and collect, please? Then on Delivery Saver. Could you talk about the uptick there? And in more normal times, I guess, what that might mean for frequency and share of spend if it migrates onto the subscription scheme for Delivery Saver? And then lastly for Booker and Booker's wholesale to retail. Could you give a sense of the shape of 14% growth between the Q3 and the six weeks, please? Thank You.

Ken Murphy: Sure. No problem, Nick. So broadly speaking, the GHS order rate, it is running at about 1.25 million a week. And we are seeing about 25% of that being click and collect. So that's kind of the average. Sorry, just remind me of your second question again?

Nick Coulter: It was on Delivery Saver and the uptick and what that might mean, obviously post – what you've seen previously in terms of what that might mean for frequency, share of spend with the behaviour as people migrate onto Delivery Saver?

Ken Murphy: Well, I think what does the kind of uptick and Delivery Saver means from my perspective, and I think that this is shared more broadly in the industry, is that online penetration or at least proportion of online penetration that we do, the dramatic increase we've seen over the last 12 months is here to stay, and that is becoming institutionalised as part of customer behaviour, because as they've gotten into the rhythm of it, they've got comfortable with it. They've got their kind of regular shopping list. They find it very convenient.

They probably even get to know the drivers. It's just become an institutional part of their shopping habits. So, our thinking is that a reasonable proportion of the online – increase in online penetration we've seen this year is here to stay.

Nick Coulter: And do you think that Delivery Saver subscription rate. It looks like it's kind of broadly half of your weekly slots. So, is that an indication of how much sticks or what do you think more sticks?

Ken Murphy: I think it'll be a bit more than that. I think that some people like the optionality, but we'll continue to use the service without the Delivery Saver. And then there could be even among the proportion of customers that are using. There could just be a lack of awareness. So, as we kind of reinforce and remind customers of that proposition, we would expect a steady increase in the proportion of customers using the Delivery Saver option over time.

Nick Coulter: Thank you. And the last one was just on Booker's wholesale to retailer and the shape of the 14% between Q3 and six weeks, please.

Ken Murphy: Yeah. So, starting with the last part first. So, the Christmas trading for Booker was a positive sales change of 6.7%, but minus 8.3% on a like-for-like basis because the best in logistics had a significant impact on the total sales increase all over the Christmas trading period.

For quarter three, the sales increase for Booker was 15% but flat on a like-for-like basis. And then –

Nick Coulter: I'm asking about the retail element, so retail versus catering. So, I think you gave a 14% figure, and it was just how that 14% broke down between Q3 and six weeks.

Ken Murphy: I don't have that number.

Alan Stewart: Ken, I can give a bit of colour on it in terms of the colour. What we saw is that the – in Q3, particularly if you look at Q2 and Q3, they were actually pretty much the same percentages of impact, but actually the shape within that was very different. So as the Eating Out came stronger, so Booker's saw a drop off in its retail sales and the increase in this catering sales. That will be it. And the exit in Q3 as that then came to an end and as we got more constraint. So, we saw retail picking up quite strongly. And the element of catering falling off.

So, the retail 14% is actually a mix, Nick, in terms of shape. And that's something, which I think is something we'll continue to see in the Booker business because of that mix between people shopping locally, shopping from the Booker retail partners when they're particularly constrained and needing to shop locally. And then as soon as they're able to eat out, they stopped doing that.

And we've seen that particularly in Booker over the course. So, whilst the numbers are pretty flat, the shape within it is definitely impacted by external events.

Nick Coulter: Super. That's very helpful. Thanks so much.

Ken Murphy: Thanks, Nick.

Operator: Thank you. And our next question comes from the line of Andrew Porteous of HSBC. Please go ahead. Your line is open.

Andrew Porteous (HSBC): Hi. Good morning team and a happy new year. A few from me. Just can you come back on online? I mean, you talked about the fact that December was a record period, I think, in terms of profitability. Was that more driven by mix with a lot more click and collect in the mix than usual? Or have you seen the home delivery profitability improve as well? And then could you perhaps talk about what advantages you think you have in online? Does your scale mean that you should be structurally higher from a profitability perspective than any of your competitors can get to giving you a drop density? And then the last question I had was really, you talked about net switching gains for a lot of people. I think if you look back over the past year, clearly the business is in, in much better shape sort of strategically. I'm just wondering how you think you hold onto those gains in a more normal sort of trading environment and sort of what your thinking is around that?

Ken Murphy: Great. Thank you, Andrew. So, I think the online profitability story is one of ongoing improvements. So, we have increased the number of click and collect slots over the quarter three period. We're refining all of the time the picking methodology, van routing, the kind of efficiency of our kind of process from order taking through to delivery at the door.

So, we're on a kind of a constant trend of improvement. And I absolutely would say that our scale and our densities is an asset and as is our reach. And increasingly our flexibility, our ability to respond to surges in demand much more locally I think is an advantage. So, this is, I think, an ongoing journey, Andrew.

The important thing that we wanted to iterate and stay today is that we're committed to the online channel. We think it's a channel that's here for the foreseeable future and will only get stronger. We think that having been forced into this channel in the UK and having years – accumulated years and years of experience, we're really well-placed to maintain a constant rate of improvement of the customer experience to open up an increasingly convenient and frictionless experience for them and to do with a great value. So that's where we think our advantages lie.

In terms of the switching gains, I think that trying to pinpoint one single factor for those gains has been difficult. What we have come to the conclusion on is that it is the culmination of brilliant customer work, brilliant product work, brilliant supply chain work, brilliant in-store execution, and a kind a returning trust in the brand that it will do the right thing for customers, and it will do the right thing for the community.

And actually, thinking to take a leadership position in the market. So that's, I think – it's those combination of factors that we think will continue to serve us well, as we seek to hold on to those gains into the new year, and also make us agile enough and flexible enough to respond to whatever changes come down the track in terms of customer habits and customer needs.

Andrew Porteous: Thank you guys.

Ken Murphy: Thanks, Andrew.

Operator: Thank you. Your next question comes from the line of Clive Black of Shore Capital Market. Please go ahead. Your line is open.

Clive Black (Shore Capital Market): Good morning, gentlemen, and a very happy new year to you. A few questions from me, if I may. Firstly, you say that your out performance was market leading over the Christmas period. I just wondered on what measure that was based? Just interesting to know that context. Secondly, Ken, do you think that your online and offline activities can have similar rates of contribution to the business in the UK at any stage in the foreseeable future? And then lastly just more broadly from the context of a trading statement. I just wonder if you think we're reaching a point with the UK government where there may be a fundamental reappraise with business rates, and alongside that, an introduction of digital taxation that perhaps balances online and offline fiscal policies. Thank you very much.

Ken Murphy: Thank you very much, Clive, and happy new year to you too. So, in terms of a market leading performance, we, as you will know very well, monitor our performance relative to the market through kind of three different independent bodies that measure market performance and out performance relative to it. What we can tell you is that we beat the market consistently every week through the six-week period of Christmas trading.

And so that's really what's underpinning our definition of a market-leading Christmas. I do accept that the headline numbers of some of the other retailers is better. But as you know, because of different trading periods, different definitions of like-for-like it is not all of those as clear cuts. So, we're very comfortable that the measure we use is a very robust one and a relevant one and underpins our kind of relaxation that we have. We have achieved a leading Christmas performance.

In terms of online versus offline contribution, we're getting closer all the time, Clive. So, it's been a continuous improvement journey. We have a number of plans in place that we think will take us closer to parity in terms of operating contributions from online, equivalent to offline. We're not there yet. But we believe we can see our way there. By our definition foreseeable future, I would say absolutely yes. It is possible in the foreseeable future.

On your third question, in terms of the business rates, we believe that the decision by the industry to return the rates relate in conjunction with the fact that the government is already running a consultation process with the industry has put into dark really just how big the burden of rates is on the retail business, how dramatically that rates burden has grown despite no extra sales coming from the stores that are bearing that burden and how the transfer of that business online, those require fundamental reformation of the rate system. And we do believe that it should be all set by a digital tax.

So, we believe the governments are taking it seriously. And we sincerely hope that they respond to all of our urgings to make the changes that we think are necessary. I think we mentioned it that in an independent report commissioned to look at levelling up. It found that the areas most in need of inward investment for which retail is disproportionately important from implying perspective are the worst case in terms of rates.

So, it's actually having exactly the opposite of the intended effect that the government would desire.

Clive Black: Thank you very much for that, Ken. My only final comment is I am sorry for the disappointment of Munster versus Ulster over the Christmas period.

Ken Murphy: That's all right, Clive. We bounced back with a win against Connacht and we're still on top of the table. So, I'm pretty relaxed about it. Ulster played very well, Clive. I'll give you that.

Clive Black: Happy new year.

Ken Murphy: Happy new year.

Operator: Thank you. Our next question comes from the line of Sreedhar Mahamkali of UBS. Please go ahead. Your line is open.

Sreedhar Mahamkali (UBS): Hi. Good morning. A couple of questions on online and just another one on the profit outlook, please, if I can. So firstly, in terms of online, can you give us any early thoughts perhaps in terms of West Brom UFC on how that's shaping your thinking, what the learnings are so far? And secondly, I know you've shared a few thoughts again in terms of continuous improvement. Maybe just if I can just take one metric in terms of pick rates in store, are you able to say they are now where they were pre-pandemic? That's the second one. And maybe just kind of stepping back in terms of the outlook for the year in terms of profit, just trying to understand why you maintain the outlook for profit for the year despite very good trading performance? I know there are some clear puts and takes here, especially Booker, etc. But if you could talk through what some of those others would be, super helpful, thank you very much.

Ken Murphy: Thanks, Sreedhar. And happy new year to you too. So, starting with your first question, the West Brom UFC continues to perform strongly. So, we're seeing it now approaching the expected pick rate that we were – that we had in the business case. So, it is delivering on all the metrics that we hoped it would do. And as you know, we will have our second UFC open in Lakeside very soon and it will have an even higher pick race than West Bromwich.

So really, we are progressing our UFC tests and trials. We're watching and monitoring very closely. We're very pleased with the progress. And once we kind of move to a more meaningful kind of investment, I'll be sure to update all of you on that. All I can tell you is that it's progressing as we expected.

Pick rate haven't returned to the pre-pandemic level because there are a number of safety measures that we have to take in terms of picking. That mean that we're operating at about 10% to 20% lower in terms of pick rate that we would have had pre-pandemic. We know very clearly how to get those pick rates back up, but in the interest of safety, we have to live with it for now.

And in terms of profit guidance, I think that you answered the question yourself. In essence, we have a number of puts and calls. We have had a series of additional costs associated with the pandemic, which we've flagged to you in terms of absence rates in terms of paid leave and shielding in terms of the extra Christmas bonus, etc., and of course, in terms of the continued pressure on the catering market, which means that we think at this stage that where we are is an unchanged picture in terms of the profit guidance, we gave at the half year.

Sreedhar Mahamkali: Thank you.

Ken Murphy: Thank you, Sreedhar.

Operator: Thank you. And your next question comes from the line of Victoria Petrova of Credit Suisse. Please go ahead. Your line is open.

Victoria Petrova (Credit Suisse): Thank you very much and happy new year. I have three short questions first. It's an online and cannibalisation. As far as I understand your online market share has significantly improved. You talked about 5.5 billion of sales in the 2020-2021, potentially even 6 billion. Your figures are very strong. Who are you taking market share from in online? And also, can you provide some clarity on what percent of your online sales is cannibalised from your existing stores and existing customers and what percent is new? As well as when we look at the 800 million COVID costs, what percent of what amount of it is associated with your online ramp up? That's my first sort of group of questions. The second one is on discounters. Can you qualify or quantify the uplift of sales you were getting from discounters losing market share in 2020? And do you expect it to continue, or it's a COVID – in your view, a COVID specific development? And my last question is very similar to the previous one. Aren’t you expecting any operating leverage in the second half driven by this additional uplift in sales? Thank you very much.

Ken Murphy: Thank you, Victoria, and happy new year.

Victoria Petrova: Thank you.

Ken Murphy: Okay. So, let's talk about online first. So, the – roughly we think that the rate of new sales, additional sales is about 70% of the online sales that we have seen. So, we think the cannibalisation rate is about 30% give or take. And we think that a proportion of that we will keep. What we don't know is what the rate and by how much sales will either revert back to eating out and to shopping in store as the pandemic eases. That's something that we just don't have a feel for at this stage.

In terms of the COVID cost of 800 million, we don't really give a breakdown of how much is associated specifically with each channel. So, it's a reasonable proportion, but a large part of the COVID costs that we talk about are really the exceptional costs that we incur in terms of employee bonuses, in terms of shielding, in terms of covering for absence, in terms of the PPE and sanitisation equipment and consumables that we need to provide.

So that is it on COVID costs. And again, in terms of the discounters on how much market share. I mean, I think what we've seen is really a bifurcation in the discounter performance that obviously middle[?] having a very strong performance and Aldi is not. We don't think that our Aldi Price Match is actually necessarily directly impacting Aldi. We're seeing switching from everyone. And really our intent isn't to go after Aldi. It's actually to underpin a value message to our customers against the entire market really. And that's our continued desire. So, we're really interested in eliminating Aldi as a negative rather than – our price as a negative rather than going after one particular competitor.

Victoria Petrova: And in terms of online, who do you think you are taking most of market share from? Is it Ocado, or is it – because you seem to be growing as one of the fastest and you're obviously very biggest online retailer? So, when you look at this remaining 70% of customers, which are not cannibalised, who do you get them from?

Ken Murphy: So, I mean, Victoria, I think that's really the market is growing. And I think that almost all of the market growth is coming through the online sector. So really the market is coming from what would traditionally have been an ease out market. And we're just winning disproportionately.

So, I think that anyone with a strong online business, whether that'd be Ocado or Sainsbury's are seeing dramatic increases. It's just that Tesco because of its coverage, because of its size of its business to start with, because of the speed with which was able to scale up had just one disproportionate in terms of business volume. So, I'd say it's less about taking share and more about winning disproportionately the increase in share available.

Victoria Petrova: Understood. Thank you very much.

Alan Stewart: Ken, shall I pick up the question on operating leverage, or are you going to?

Ken Murphy: Yes, please, Alan.

Alan Stewart: Great. Thanks. Hi Victoria, happy new year. In terms of operating leverage, yes, we clearly see it. Our COVID costs, as you've seen, has gone up from what we estimated in early October at around 725 million. We're now estimating at 810 million. So that's an 85 million increase. Against that, we're holding our expectations for the year.

So, we've seen some clear leverage. We spoke about the improvements and how we see the online business improving. Booker went backwards because of the – in terms of our outlook and expectations from where we last were to where we are now because of the shifts in the catering market.

So, there are pluses and minuses, but clearly, we see operating leverage through what we're doing. And we'll continue to focus on that.

Victoria Petrova: Thank you very much.

Ken Murphy: Thank you, Victoria.

Operator: Thank you. Our next question comes from the line of Rob Joyce of Goldman Sachs. Please go ahead. Your line is open.

Rob Joyce (Goldman Sachs): Thank you. Good morning. Happy new year. Three from me. Just to follow on from that one, Alan, actually. I mean, I think we're estimating Booker is a sort of 100 million to maybe even 150 million profit headwind this year versus last year. Is that the right way to think about that, just so we can understand the difference in performance versus competitors perhaps? Second one, appreciate it's pretty early and a lot of unknowns. But as things stand, if you're looking into next year, FY22, do you think it's reasonable to assume you can grow profits from the base you're guiding to for this year? And then the third one is just haven't talked about Brexit yet, but I guess a lot of – still a few more reports of disruption in the ports. Are you seeing any disruption to your supply chain and any early impacts on prices as a result? Thank you very much.

Alan Stewart: Ken, should I take the first one and maybe second, and then you pick up the Brexit or how do you want to do?

Ken Murphy: Yeah. That works, Alan. That's perfect.

Alan Stewart: Okay. Thanks. In terms of Booker, the – Rob, the – as we've said, and as you know, the catering part of the business is the more profitable within the Booker's mix. And that's something which therefore does impact Booker proportionately, just profit and see, if you like, the leverage within Booker is particularly felt when catering sales go backwards.

So, the way you're thinking about it is absolutely right, clearly as the expectation and the hope is that the eating out markets recovers next year, and we would all hope that it's better from a customer perspective than it's been over the last 12 months. So, in that sense, there should be some upside in terms of Booker and its ability to recover profitability.

In terms of next year, really, I think it's too early to talk about next year. We will give the best possible view as we get to the year end. We're off a period of uncertainty, and fairly as we've seen, sales give leverage – operating leverage. But we see great opportunity. But really don't want to be, at this stage, given the fact that we're still six weeks away from the proposal this year and don't really want to be drawn into next year. But the moving parts I'm sure are as you understand them.

Ken, over to you for the Brexit.

Ken Murphy: Yeah. Hi. Thanks, Alan. So, Rob, in terms of Brexit, we have definitely seen some levels of disruption. What I can tell you though is that because of the planning the team has done and because of the supply chain preparation, investment in stock, etc., we weathered the storm incredibly well. And while we are seeing in some limited areas, continued issues, overall, our supply into the Northern Irish and to the Republic of Ireland and indeed into the mainland Great Britain, it remains very strong.

And we're working very closely with governments on both sides of the IRC to kind of iron out any residual issues in terms of the movement of goods, processes, paperwork, documentation, etc. But we're as well set up as we can be and that we're maintaining good levels of service into our markets.

Rob Joyce: Thanks, Ken. And just to follow up, I mean, early doors, do you think there's going to be much of an inflationary or even dis-inflationary impact from the changeover?

Ken Murphy: We think it would be very small. So, we're not planning any price increases into our business in the coming weeks and months as a consequence of Brexit. We're obviously going to keep a very close eye on it. But at this stage, given that the agreement does effectively provide for largely for tariff free movement of product, we are confident that the costs will be minimal.

Rob Joyce: Thanks very much.

Ken Murphy: Thank you.

Operator: Thank you. And our next question comes from the line of Maria-Laura Adurno of Morgan Stanley. Please go ahead. Your line is open.

Maria-Laura Adurno (Morgan Stanley): Thank you very much for taking my questions. I just have two. So, the first one, I was just wondering if you could potentially provide us some level of details with respect to everyday low-price strategy? And how much penetration you have from a customer basket standpoint? So that would be question number one. And question number two. Just wondering, given that this Christmas the basic understanding is that it was heavily online grocery led. So, from that standpoint, given the scale, given potentially also product mix improving into Christmas, would it be fair to assume that also the underlying profitability would have increased? Thank you very much.

Ken Murphy: Thanks very much, Maria-Laura. So specifically, online penetrate – EDLP penetration, we don't disclose, I think, and also it moves by period. But what we can tell you is that we have maintained our level, a number of products that are participating in the Aldi Price Match. And in fact, we increased it in the period leading up to the Christmas trading period.

And we've seen as was mentioned, in the trading statement, we've seen a 450-basis point improvement in our value perception as a business since we launched the campaign. So really, I think the message is that this is something that's working for us as a business. It's something that we will continue to focus on in terms of maintaining a very competitive price positioning, particularly as we head into economically uncertain times. And we will also continue to use the Clubcard pricing mechanism to offer our most loyal customers even better value.

In terms of the underlying profitability of the period, clearly, you're right that the mix effect is a positive one in some regards but actually goes the other way in other regards. So yes, you see a trade up over Christmas. And as we mentioned, we saw a 14% increase in participation in our finest ranges. But equally of course, you’ve seen a much higher level of penetration in beer wine spirits, and confectionery, etc., which is margin dilutive.

So, they tend to a certain extent, Maria, balance each other out. And of course, you're also anniversaring the previous Christmas, where you would've seen a similar mixed effect. So, we wouldn't say that there's been a dramatic change year-on-year on our kind of our margin mix.

Alan Stewart: If I can just add to the first question in terms of everyday low pricing really, our promotional participation is down year-on-year. And we're very clear on that. And we view it that also has been down relative to the market as well in the period. So, we feel that it's working. But as Ken says we don't disclose the numbers.

Maria-Laura Adurno: Thank you very much.

Ken Murphy: Thanks, Maria.

Operator: Thank you. And your next question comes from the line of James Grzinic of Jeffries. Please go ahead. Your line is open.

James Grzinic (Jefferies): Yes. Good morning. Happy new year. I just have a very factual and brief one really. Would you mind detailing the rates of absenteeism you're seeing the business now and perhaps where they were in November and where they were in lockdown 1.0, please?

Ken Murphy: The rates of absence.

James Grzinic: Yeah.

Ken Murphy: So, yeah. So, look, the first lockdown, I think you'll remember. And we flagged it at the half year that we at one stage had over 50,000 colleagues out of the business during the first lockdown. So, I think that really is the starting position. And clearly then as the rates of infection eased and the lockdown restrictions eased, etc., we saw the absence rates come right down through the second half of the year and into quarter three. In the recent weeks, we have clearly seen a spike in options, and we're now operating at about a 10% rate of absence, which is circa 30,000 colleagues.

So lower than the first spike, but materially higher than the rate of absence we had during the second and third quarters before we got into Christmas trading.

James Grzinic: Very clear. Thank you.

Ken Murphy: Thank you.

Operator: Thank you. Our next question comes from the line of Xavier Le Mené of Bank of America. Please go ahead. Your line is open.

Xavier Le Mené (Bank of America): Good morning. Thank you for taking my question. And happy new year to you. Two if I may. Just – first one just on the price positioning back to my last question. But you stated that you never been as strong as today. But can you share some data on how you compare potentially with your key competitors? What is the kind of price gaps you're seeing there? And then just on the year performance and the like-for-like performance more specifically. Can you just give us a bit of comment on volumes, inflation and you talked that to the mix already? But volume and inflation could be helpful. Thank you.

Ken Murphy: Alan, do you want to take the volume and inflation one?

Alan Stewart: Yeah.

Ken Murphy: And then I will come back on the price position.

Alan Stewart: Okay. Yeah, certainly. In terms of – great questions, Xavier, in terms of the – so whether you look at value or look at volume, we're really comfortable in terms of the growth that we're seeing against – about against it. You know that we weren't going to specific category by category, but as we look at it, we really are – we're really encouraged by what we're seeing, both at the volume and at the value end of it. If you want to ask any more, then I'll see if I can help you on it.

Ken Murphy: In terms of price positioning, Xavier, we look really at customer perception on that, because clearly, it's really difficult across all our products to kind of give an exact like-for-like message because the discounters carry so much own brand with different pack size configurations, etc.

But what we can tell you is clearly we are now effectively matching Aldi against thousands of products and we're maintaining that position. So, we think that puts us in a really strong position, particularly relative to the other major multiple. We don't talk about specific price gaps, but we think we're materially better value than certainly the large full range retailers.

Alan Stewart: So that's historic relativity. We're very comfortable with that historic relativity we've spoken about in the past as against each of the other peer players in the market, Xavier.

Xavier Le Mené: Right. And just if I may, but just on the inflation. So, would you say that you were in deflationary territory or inflationary territories in Q3 Christmas period?

Alan Stewart: Well, there was still slight inflation. I think it was somewhat lower than previously, but it's still pretty muted in terms of inflation generally. It's what we see on the input side.

Xavier Le Mené: Okay. Thank you.

Operator: Thank you. Our final question comes from the line of Tom Davies at Berenberg. Please go ahead. Your line is open.

Tom Davies (Berenberg): Morning, guys. Happy new year. I guess two questions for me. Firstly, in Europe, can you quantify whether there was like a top line drive from the Hungary retail sites, sales tax on like-for-likes? And secondly, given you have this roadmap to equivalents with the online/offline channels, and some of your peers being commenting that increased volumes for the online channels improve the profitability of it, do you think that'll be a change in behaviour with regards of the growth of online channel versus pre-COVID perceptions?

Ken Murphy: Thanks, Tom. So, yes, we have the drag from the sales tax in Hungary and we have seen it's a market-wide issue, as you know, the majority of retailers in Hungary are foreign multiple retailers. And so, with the sales tax, that's affected pretty much, North of 80% of the market. And we have seen an impact because it is – it has to a certain extent constraining volume growth because it has driven price increases.

But actually, more materially have been the variety of restrictions that Hungary has put in place to try and contain their rate of infection over quarter three, which have varied from curfews at 19.00 to an older age group restriction of only them being allowed to shop between 9.00 and 11.00 in the morning etc., etc. So, it has been a tough time for our teams in Central Europe in terms of responding to all the changes in restrictions that have been happening. So, without a doubt, it has been a drag.

In terms of the increase in volume online, the impact on profitability and the longer-term trends, we absolutely are seeing the same trends. So, we are seeing that the increase in volume is improving the efficiency of the overall picking process. It's – we are seeing improvements in brand rate utilisation and as a consequence – and because the basket sizes are larger, we are seeing an improvement in profitability year-on-year.

In addition to that, we definitely believe, and I think we alluded to it when we talked about the uptick in participation in the Delivery Saver option is that we do think that a proportion of these sales will institutionalise as online sales. And we do think it represents an inflection point in adoption of digital shopping in the grocery market.

And we think that this trend is only going to continue, particularly as customers find it easy and convenient to do, and they become very familiar with us. So really our focus as a team and as a business will be in the constant improvement of the efficiency and profitability of this channel, improving the customer experience, opening up new sharpening missions to customers through the digital channel, and just increasing the level of sophistication and personalisation of the digital channel for our customers.

Tom Davies: Okay. Thanks a lot.

Ken Murphy: Thanks, Tom.

Operator: Thank you. I'll now hand back to Ken Murphy for closing remarks.

Ken Murphy: Thank you very much, Tracy. So really all I wanted to do by concluding was just to reiterate what a strong performance I believe this represents for the business. Just to reiterate my thanks to our team, who I think have done a magnificent job in incredibly challenging circumstances, who continue to show up every day to look after customers under kind of a lot of pressure, really make me very humbled and very proud to be part of this team.

And really this performance is a reflection of their efforts. And I feel really proud of them. I think the last thing to say is really that Tesco believes it is in a very strong position to cope with whatever the market throws at us over the coming months and years, because I think we are heading into very uncertain times. But I feel that we're really well positioned to cope with it.

And so, I'd just like to finish by thanking you all for your time and for your questions and interest in the business today. Some really great questions. And I look forward to speaking to you all again in the near future. Thank you.

Operator: Thank you. That does conclude our conference for today. Thank you all for participating. You may all disconnect.

[END OF TRANSCRIPT]