Tesco PLC

Interim Results 2024/25

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Analyst Event

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Ken Murphy: Good morning everyone, and welcome to our interim results presentation. I'm joined here in Welwyn by our CFO Imran to give you an update on our progress in the first half. I'm really pleased to be announcing another strong set of results. Customers have continued to recognize the strength of our offering across value, quality, and service, and are choosing to shop with us even more. This is driving volume growth across the group. In the first half, we have lowered prices on thousands of lines, launched or improved hundreds of products, and continued to invest in our stores and digital capabilities to serve customers wherever and however they choose to shop with us. The combination of great prices, high quality, and continued product innovation means we're as competitive as we have ever been. We have been the UK's cheapest full-line grocer for almost two years now, and we are seeing improving customer perception across a broad range of measures, as well as strong market share momentum in both the UK and the Republic of Ireland.

We've also invested additional hours in our stores, the equivalent of more than 2000 extra colleague roles year-on-year, helping deliver market-leading availability. I want to say a huge thank you to all my Tesco colleagues for serving our customers so well and for their contribution to our strong performance. Customer satisfaction is critical to our success. The latest data for the UK shows that customer perception of the Tesco brand has grown year-on-year well ahead of the market average. What is really satisfying about these results is that we've seen progress across all six measured categories, including quality, value, and satisfaction. As a result of that broad-based improvement, our net promoter score has continued to trend upwards and is now approaching very high levels that we saw during the peak of the pandemic. Market share is another important measure of our progress. The UK grocery market remains extremely competitive and every day we need to be at the top of our game for customers.

It is therefore pleasing that alongside market share gains in volume and value, we've seen continued switching gains now for nearly two years. In recent months, we have taken share from across the market, including the limited-range discounters. The strength of our customer offer has translated into a strong financial performance for the first half. Imran will talk through the details shortly, but with group sales up 4% and our adjusted operating profit up 10%, we're very happy with the balance we've managed to strike between ongoing investment and delivery in the period. As a business, we are in great shape with our performance during the first half, building on a track record of delivery for all our stakeholders, but there's no room for complacency. We are laser focused on maintaining our competitiveness and delivering great value. Now, I'm going to hand you over to Imran to take you through our financial performance.

Imran Nawaz: Thank you Ken, and good morning everyone. I'm delighted with the strength of our performance in the half. As Ken highlighted, our customer satisfaction scores point to the progress we have made in developing our competitive advantage, and that has fed through into further market share gains driven by very strong volume performances. This trading momentum coupled with another strong contribution from our Save to Invest Program is reflected in our financial performance in the half, and we are well set up to continue to grow in the right way. As a reminder, we are currently in the process of selling our banking operations and credit cards, loans and savings to Barclays. We expect the transaction to complete before the end of the calendar year, so these activities remain classified as discontinued operations. The majority of my review this morning will be on a continuing operations basis. Our retail sales grew by 3 1/2% at constant exchange rates, which includes 2.9% growth in like-for-like sales, mainly driven by strong volume growth.

Inflation rates trended back to more normalized levels across the half as global commodity price inflation continued to ease. Retail adjusted operating profit grew by 10% year-on-year. We delivered total Save to Invest savings of 260 million and a half and are well on track to deliver our full year savings of 500 million. We generated 1.26 billion of retail free cash flow in the first half, and our net debt was 9.7 billion at the end of the first half, which is slightly down versus year-end. As our strong cash generation offset over 1.1 billion of shareholder returns in the half comprising both the final dividend payment and of course our ongoing share buyback program. Our headline earnings per share was strong at 14.45 pence, and we have proposed an interim dividend of 4.25 pence per ordinary share, which is in line with our policy of setting the interim dividend at 35% of the prior full year dividend.

Moving now to a more detailed view of performance. Total retail sales for the half were 30.9 billion. Our UK and Ireland segment delivered total sales growth of 3.7% with a particularly strong contribution from higher volumes. Inflation normalized to low single digit levels as input cost inflation ease, and we invested even further cutting prices on thousands of products. In Central Europe, sales were up 0.9% year-on-year, driven primarily by stronger volumes as customers continue to respond really well to our targeted value investments. Disposable incomes have started to recover in the region as the significant inflationary pressures customers have faced over the past two years are starting to ease. Tesco Bank revenue shown here relates to the retained insurance and money services business, which grew by 46.6% in the half. The revenue performance benefits from strong underlying progress in the insurance business, as well as two non-recurring benefits, which we set out in the release.

Over the next few slides, I will cover the performance of each of our segments in more detail, starting with sales before moving on to profit. In the UK, we delivered like-for-like sales growth of 4%. With inflation now at more normalized levels, I'm pleased to say that growth was mostly volume led and as Ken already highlighted, we consistently grew ahead of the market. Our food sales grew by 4.9%, including a particularly strong volume performance in fresh food driven by our ongoing investment in product quality and innovation. Finest sales continue to grow really strongly with volumes of 14.9% year-on-year. Our home and clothing sales grew by 0.3%. We are well progressed in our transition to our partnership with the entertainer. This will give customers an even better range of toys and improves our profitability in the category. This transition to a good mission model, however, puts a small drag on the reported growth rates in the half. Excluding toys, home and clothing sales grew by 1.6%, primarily driven by strong clothing performance where we continue to grow ahead of the broader store-based clothing market.

Our large stores in particular are seeing the return on our investments in value, quality and service. These include an even stronger promotional offer over key seasonal events and the benefit of putting more colleagues on the shop floor, helping to deliver market-leading availability, as well as an improved customer satisfaction score.

Convenience store sales, which include a higher proportion of food on the go, were impacted by poor weather in the half, as well as, of course, the ongoing decline in the tobacco market.

Our online sales grew by 9.3%, driven by higher volumes, predominantly due to further progress in our well-established grocery home shopping business. We also continue to see a strong contribution from Tesco Whoosh, our rapid delivery service. Our overall online average orders per week were up 9.3% year-on-year to 1.3 million in the half, and we continued to improve the proportion of perfect orders leading to further improvement in customer satisfaction scores. Excluding Whoosh, our basket size increased by 4.4% year-on-year.

In Ireland like-for-like sales grew by 4.7% in the half, primarily driven by stronger food volumes. Total sales grew by 5.6% in constant rates, including a 0.9% contribution from new stores. Our food sales grew by 5.4%, including particularly strong fresh food performance. Home and clothing sales declined by 0.8% year-on-year, which includes a 1.4 percentage point drag from our new partnership with The Entertainer. Excluding toys, our home and clothing like-for-like was up 0.6% year-on-year.

Booker performed well in a challenging market. Total Booker like-for-like sales of -1.9% reflected the continuing decline in the tobacco market and the weakness in parts of the fast food market, which is serviced by Best Foods Logistics, as we had highlighted in our Q1 update. Core retail sales, which excludes tobacco, increased by 0.6% year-on-year. Our retail symbol brands performed very strongly with sales up 3.1%, supported by further improvements in availability, leading to even stronger customer satisfaction.

Sales to independent retailers were softer as some customers are switching into large store formats. Core catering sales increased by 1.7%, primarily driven by stronger volumes as customers responded well to an extension of our Everyday Low Price campaign, with prices locked on over 700 products until January 2025.

In Central Europe, like-for-like sales grew by 0.6%, driven by both strong volume and mixed growth, reflecting a gradual recovery in consumer sentiment in the region. Our food sales grew by 0.9%, including a very strong performance in fresh food as customers responded well to our value investments. Our non-food sales declined by 1.7%, impacted by unseasonal weather in the second quarter, which affected sales of seasonal ranges.

Let's now move on to our retail profit performance. We delivered 1.56 billion of retail adjusted operating profit, which is 138 million ahead of last year, primarily driven by the strength of our trading performance. Our retail operating margin was 4.5%, up 30 basis points year-on-year. Within this, the UK and Ireland adjusted operating profit grew by 135 million year-on-year to 1.5 billion. Strong retail volume growth and the ongoing delivery of our Save to Invest program helped to power our investments in the customer offer and in our colleagues, while still driving strong earnings growth.

Our UK and Ireland operating margin was 4.7%, a 29 basis points increase year-on-year. The Central Europe adjusted operating profit was 49 million, an increase of 8.7% year-on-year at constant exchange rates, primarily driven by stronger volumes, improving mix, and a further contribution from Save to Invest.

This slide provides further detail of the components of our statutory profit performance, which increased by 135 million or 15.2% year-on-year, driven by adjusted operating profit growth. There was an adjusting charge of 37 million to operating profit in the half from the continuation of non-cash charges related to the 2018 acquisition of Booker. Our net finance costs were lower due to higher interest on cash, short-term deposits and money market funds, as well as favourable non-cash mark-to-market movements on certain hedging instruments. The group tax charge increased by 96 million to 370 million. This increase was primarily driven by higher profits and a higher statutory tax rate versus last year.

Let's now move on to our retail free cash flow. We delivered another strong performance, generating 1.26 billion, reflecting the strong operating profit performance in the half. The year-on-year reduction of 107 million primarily reflects lower working capital benefits and higher tax paid.

Our total working capital inflow was 169 million, reflecting trade seasonality and volume growth leading to higher trade balances. The higher working capital benefit last year reflects a higher level of cost inflation, which has now normalized. Cash CapEx was in line with the prior year and we continue to invest in high-returning projects, including Save to Invest and our digital platforms. Cash tax paid was 138 million higher year-on-year, mainly due to no longer benefiting from tax relief relating to the 2.5 billion one-off pension contribution we had made in 2021, now fully utilized, as well as the impact, of course, of the higher retail adjusted operating profit year-on-year.

Let's now turn to Tesco Bank. The sale of our existing banking operations to Barclays is progressing well and is on track to complete before the end of this calendar year. Continuing operations revenue grew by 46.6%, driven by growth in home and motor insurance volumes, as well as strong renewal rates and a one-off benefit from the signing of a new five-year pet insurance agreement.

Adjusted operating profit from continuing operations in the first half was 94 million. The performance in the half includes two non-recurring benefits, which total 42 million. The first is related to the new pet insurance contract and the second relates to net investment income, which will cease following completion of the proposed sale to Barclays. The remainder of the profit growth was driven by higher insurance income year-on-year, as I described earlier.

On an ongoing basis, we expect an adjusted operating profit contribution from the retained insurance and money services business of between 80 and 100 million per year. In the current year, the non-recurring benefits that I described mean that we now expect the contribution from the retained business of around 120 million.

Let's now turn to the balance sheet, which further strengthened in the half. Net debt was 9.7 billion, a reduction of 88 million versus year-end. This was predominantly driven by strong retail free cash flow generation of 1.26 billion, which more than offset the cash outflows relating to our ongoing share buyback program of 575 million and the payment of last year's final dividend, which was also 575 million. Our net debt to EBITDA ratio was 2.1 times at the end of the first half, slightly below year-end. The total indebtedness ratio not shown on the slide was 2.2 times compared to 2.4 times at year-end. Our fixed charge cover was 3.9 times at the end of the first half, which is an improvement since year-end, primarily due to the increase in retail EBITDA. Turning that to our outlook for the current year, we expect to deliver retail adjusted operating profit of around 2.9 billion in addition to 120 million from the retained Tesco bank business. We expect to generate retail free cash flow within our guidance range of 1.4 to 1.8 billion. And we are on track to complete our 1 billion share buyback by April 2025. Thank you. And now I'd like to hand you back to Ken to take you through our strategic progress.

Ken Murphy: Thank you, Imran. As you've seen, we've had a really good first half and I'm proud of what we've achieved. It's also important for us to take a step back and reflect on our performance over a longer period and how we intend to sustain our momentum. Our strategic priorities are hopefully familiar to you. They outline how we try to differentiate our offer from what remains a very competitive landscape. Our performance during the first half is evidence of the momentum we've built by closely anchoring to these priorities. We first set out our multi-year performance framework three years ago, and it's as relevant now as it was then. The framework was devised to create sustainable long-term value for every Tesco stakeholder. By focusing on customer satisfaction, it aims to drive top-line growth, grow absolute profits while maintaining sector leading margins, and in doing so, generate strong cash flow.

We couldn't have anticipated the many challenges we have faced, such as the cost of living crisis and the war in Ukraine. But despite those challenges, the framework has proven to be the right one, allowing us to deliver for our stakeholders while also investing in the future growth of the business. As we touched on earlier, our customer satisfaction scores and market share have significantly stepped forward as customers respond to our investments in value, quality, and service. Progress is rarely straight line, but we've taken a full percentage point of market share in the UK since the first half of 2021. We've also grown our absolute profits by leveraging the strength of our brand and network across all channels. We continue to take a disciplined approach to capital investments, prioritizing projects, which drive efficiency, growth, and digital capabilities. Through building our digital platform, powered by the scale and reach of Clubcard, we have unlocked new revenue streams.

In retail media, we are building out the breadth of what we can offer our advertising partners spanning multiple channels. As a result, we are seeing growth in active advertisers, campaigns per advertiser, and spend per campaign. We're still at an early phase in unlocking all we think we can achieve from retail media, but we are really pleased with our progress. Our save to invest program has also been an important part of our performance, helping fund some of our strategic investments and offsetting cost inflation. By the end of this financial year, we expect to have unlocked a total of 1.7 billion pounds of savings across the last three years. And finally, our cash generation has been really encouraging. While this year, we will face into a more normalized working capital inflow and an increase in tax paid. We expect to be within our medium-term guidance range of 1.4 to 1.8 billion pounds.

I mentioned earlier our priorities, and leading on value will remain number one. Although inflation has come down, we are acutely aware of the continued challenges that many customers are facing. And that is why we are working incredibly hard to keep value front and centre in our offering, ensuring that customers are spending less wherever they can. Our powerful combination of Aldi price match, low everyday prices and Clubcard prices means that customers are getting fantastic quality at great prices. This has made us the UK's cheapest full-line grocer since November 2022. Our approach to offering compelling value runs across the group. This half has seen us cut prices on at least 1500 products in each of our markets in Central Europe, offer a price lock on over 700 products within Booker Catering. And in Tesco Mobile, we've extended our offer of no EU roaming fees till 2026.

When it comes to value, we know that quality is as important as price. We're investing right across our range, making sure customers can enjoy some really fantastic products, regardless of budget. These investments are working and we have seen a step change in quality perception across the last 12 months, strongly outperforming the market. During the half, we developed over 860 new or improved products. Exciting launches across our dinner for tonight offer include brands such as Root & Soul and Pinch. In the Republic of Ireland, food sales are up over 5% thanks to our investment in quality, which were also recognized with eight gold medals at the 2024 Monde Selection Awards. One of the highlights of our investment into quality is once again Tesco Finest, which has seen further significant growth with volumes in the UK up nearly 15%.

During the half, we launched more than 180 new or improved Finest products, including our sourdough range and the relaunch of our hugely popular dine-in offer, which has since seen 18% volume growth. We've been innovating across our wine range as well. Our new Finest Floreal white wine, for example, tastes fantastic. And with the grape grown amongst wild flora, it fosters greater biodiversity. As a result of our continued innovation, we saw over 20 million customers buying a Finest product in the half, an increase of 5% year-on-year. And so it's switching gains from all our competitors into Finest. Our commitment to quality has been recognized externally too. With Finest been awarded own label range of the year at the Grocer Gold Awards. We continue to evolve our digital capabilities with the depth and breadth of Clubcard data, allowing us to offer a more personalized and relevant shopping experience for customers. We are seeing very high levels of engagement with over 23 million Clubcard households in the UK and over 16 million app users across the group. The opportunity to offer our customers a personalized experience through Clubcard remains hugely exciting. We have made good progress in the half and an example of this is Clubcard Challenges, which we launched to just under 5 million customers, rewarding them with personalized offers and promotions in a fun, gamified way. By combining Clubcard insights and leveraging dunnhumby's expertise in data, we are creating a market-leading digital capability that benefits our customers and supplier partners. Our media and insights platform continues to grow and build partnerships with new consumer brands coming on board and agency agreements signed with WPP and publicists. During the half, 91 brands participating in our Summer of Sport event.

In June, we introduced Tesco Marketplace, providing customers access to an even greater range on Tesco.com with products from trusted brand partners. Over the last few months, we've been ramping up the number of products available on the platform, which is now at over 150,000. The market for retail media is growing at pace and we're pleased with how customers and suppliers have responded. The combination of our physical and online footprint is unrivalled. I touched earlier on our progress across the last 12 months, but what is really shining through for me is the connectivity of the campaigns across our channels, whether that be a screen in store, a banner on Whoosh, or something much bolder, as you can see here on our Wembley store. Our ability to reach customers at every stage of their shopping journey means that as we work with more advertisers and launch more campaigns, the depth of media spend is increasing.

But easily the most convenient means serving customers wherever, whenever, and however they want to be served. Given the scale and quality of our network, we believe we can do that better than anyone, and so it remains crucial that we continue to invest in our stores and infrastructure in a disciplined and returns focused way. During the half, we opened 44 stores across the group and refreshed another 182. In Ireland, we're continuing our Fresh First rollout with a further 11 stores converted during the half, helping to support a strong performance in fresh food. We're on track to open a new chill distribution centre in Aylesford in the summer of

2025, making use of robotic automation to enhance efficiency for our warehouse colleagues and improve customer satisfaction. In Booker, we've signed 397 net new retail partners for our Symbol brands with Premier winning Symbol Franchise Retailer of the Year at the Grocer Gold Awards.

Tesco wouldn't be Tesco without our amazing colleagues and it's vital for me that we deliver for them and all our stakeholders. This calendar year, we made our largest ever increase in colleague pay, while also enhancing our parental leave policies and our wellbeing offering. Almost 15,000 colleagues have signed up to our virtual GP service in its first year, receiving free, quick access to GP appointments seven days a week for them and their families. All this progress has culminated in standout colleague satisfaction results and us winning Retail Employer of the Year at the Grocer Gold Awards, an accolade we're really proud of.

Turning to our communities, our Stronger Stars program continues to go from strength to strength and is now supporting over 8,000 projects across the UK through grants focused on providing food and support to young people. Together these projects have been awarded more than 9 million pounds of funding to date. We are continuing our vital work on food donations, having now supplied over 220 million meals in the UK working alongside our partners. We also introduced new initiatives over the summer to support children facing hunger, including additional donations to FareShare and the Trussell Trust, rolling out food donation bags across all large stores, and once again, running our popular Kids Eat Free offer across our 317 in-store cafes.

A few weeks ago, we announced that we would be supporting over 1,000 unemployed people by hosting free career clinics across the UK in November, specifically targeting areas that face higher deprivation and economic challenges. Our suppliers play a vital role in our business. We continue to work with them on a wide range of initiatives and we're delighted to have recently been ranked first in the Advantage Supplier Survey for the ninth year running. We signed up a further 16 innovative new brands as part of our 2024 accelerator scheme. Each brand will be provided with a year-long program of mentoring, learning, and development experience to help them flourish and grow.

At the same time, we've been working really hard to reduce our environmental impact and put sustainability at the heart of our operations. We signed an agreement to source renewable energy from a new wind farm in Scotland. And in partnership with one of the UK's largest dairy farms, we launched an innovative trial of methane-reducing feed supplement for dairy cows. Our work to reduce our environmental footprint can never be truly complete, but I am pleased with our progress so far.

In summary, we've delivered a strong performance during the first half on all fronts. The strength of our customer offer has delivered volume growth and market share gains, which has led to profit growth and a strong cash performance. We will continue to invest in value, quality, and service while unlocking longer-term growth opportunities. And through this, we are delivering for all stakeholders, ensuring we serve customers, communities, and the planet a little better every day. Thank you very much for your time and we'd now be happy to take any questions.

Moderator: Thank you very much, Ken. If you would like to ask a question, please click Raise Hand in the bar at the bottom of your screen and when you're introduced, if you could unmute your microphone and ask your question. If you do not wish to ask a question anymore, you can click the Lower Hand button in the bar at the bottom. We'll take our first question from Izabel Dobreva at Morgan Stanley. Please go ahead, Izabel.

Izabel Dobreva: Hello, good morning. I was hoping for my first question you could talk a little bit more about the Finest range, the product development that you have been making there. So where are you on that journey relative to where you ultimately want to get to? And also, is it fair to assume that the key path of ground this Christmas is premium? So how is Tesco positioned there?

Then my second question is on marketplace. So from memory, when you launched it in June, it was under 10,000 SKUs and now the range has expanded with a factor of 15. So could you maybe share some early learnings in terms of what you are seeing from customer demand for that marketplace range?

And then my last question is on retail media. So I think the charts around the advertising streams were very helpful. I was hoping to also get your thoughts in terms of how retail media can be a second order tailwind for your market share in the core grocery business. So is it also helping you achieve better volume sell through and lifting market share that way? And how is the retail media helping you strengthen your value credentials?

Ken Murphy: Thank you, Izabel. Great question. So let me start with Finest. We've seen very strong growth in the half on Finest, as you can see, over 15%. And within that there are some particularly pleasing things insofar as our dine in offer, which we kind of reinstated during the half, was particularly impressive at over 18% growth. And I think what that's reflecting is a tendency for consumers to dine in more and to treat themselves. And the range at Finest has really been compelling for them, particularly the quality and the value combination.

I think in terms of where we're taking Finest, I think we're constantly innovating and building out the Finest range. I think some of the highlights for me are that we've started to really excite consumers about what we can do in Finest. And the latest manifestation of that will be the Chef's Collection range, which will be in much wider distribution this Christmas. It's really exciting because it's really kind of the leading edge of our creativity in food innovation, and I'm very excited about it.

I'd also call out our wine innovation and particularly our Floreal brand, which we've just launched. It's a fantastic white wine and it's got rave reviews from consumers so far. So I think there are still a lot of room for growth in Finest. We're very excited about it. We're very committed to it as a brand. And as you know, we broke the two billion pound barrier at the end of the last financial year and we've got very strong ambitions for growth.

On marketplace, it's fair to say that we're learning an awful lot every single day. As you say, we've kind of 10 x'ed the number of SKUs on the platform and we're learning a lot of lessons about search, about quick and easy to pay, about what are the right ranges, et cetera. And that really much is where we're at in marketplace is we're in that test and learn phase of the launch and we still have a long way to go, but we're quite excited about it.

Finally, on retail media, the way I would think about retail media if I were you, is that it is one component of our ambition to be the best partner for brands to thrive in a retail environment. So we think that our success is primarily on the back of the best availability in the industry, the lowest priced full-line grocer in the industry, a real focus on quality and quite a significant investment in the store experience in terms of it being a good place to shop, being an easy and convenient place to shop and having a lot of people available to serve you and look after you.

Retail media over time, as it develops, will be a subset of being the best supplier partner in the industry and helping to build brands, helping to find the right audience for those brands and to feed to those audiences in a very targeted and personalized way compelling proposition. So the way I think about retail media is as a subset of a much bigger ambition around being a great place to list your brands and grow your brands rather than just for itself. And that's been our journey is to make that more and more compelling over time.

Izabel Dobreva: Thank you.

Ken Murphy: Thanks Izabel.

Moderator: Okay, thanks very much, Izabel. We'll now take our next question from William Woods at Bernstein. William, let's take your question, please.

William Woods: Good morning. Thanks for taking the questions. Three, and they're kind of short, medium and long term. The first one is obviously on the short term. Finest is doing very well. Customers are switching from the discounters to you. How are you feeling about the UK consumer at the moment?

The medium is, when we look at inflation over the next 12 months, we've started to see it tick upwards again. Do you think that will continue and do you think a 3 or 4% range for inflation next year feels reasonable?

And then the long term is, obviously you've had pretty good margin expansion in this half. How are you thinking about the putts and takes on margins over the next three to five years?

Thanks.

Ken Murphy: Let me start with the last one first, which is I think we've always been very clear on how we run the business. So first and foremost, we're very customer-centric and therefore market share for us is really the most important metric of how we think about the business because that's really what tells us that we're winning with customers.

Apart from that, we then run a very disciplined P&L in terms of how we think about pricing, costs, margins to maximize or optimize, let me say the cash profit contribution. And so we have quite a lot of capital discipline. We invest for good returning programs. And at the end of all that, we hope and expect to produce good cash returns for investors, but only after making sure that we're great value for money, we're the lowest priced full line retailer in the market, we've looked after our colleagues and they feel well paid and well looked after, we've got a great working relationship with our suppliers. And so that's how I would think about our business if I were you, is this focus on cash. If through the work we do and the additional income streams that we generate margins go up, then that's great. We don't have a problem with that, but that's not really what drives the way we think about the business.

Second point I would just say is that consumer sentiment is what I would describe as stable to positive. And we see that in recovering volumes. I can't predict how that is going to play out over the next six to 12 months, but we see no real reason for it to change in the UK context. Clearly there's a lot going on in the world and some of what's going on in the world is very concerning, but with the core UK's consumer, everything we're seeing in the business is relatively positive in terms of volume, momentum and trading up to Finest, as I mentioned earlier in the answer. And I think we plan for that to continue through the Christmas trading period.

Imran Nawaz: And maybe on inflation, just the midterm outlook, difficult to call, of course, exactly what will happen, but you remember when we started the year, we talked about is there a risk of deflation? And our view of the world was, look, we see low single inflation, low single digit inflation for the year, and that's pretty much what we've been seeing. I'd expect that clearly when you look at payroll, there will always continue to be upward pressure from that angle. Energy has been down, commodities have been very mixed, and on the whole it's ended up at that low single digit inflation. I'd expect nothing different as we go out into the outer years, as in at this stage, payroll will continue to be upward pressure. We'll continue working really hard save as much as we did, which has worked really well for us.

And then commodities will always depend on crop cycles, climate change, and everything else. But what is good in our view is we've demonstrated, I think to ourselves and frankly I think hopefully to you, that we can deal with whatever the market throws it up in terms of inflation.

William Woods: Excellent. Thank you very much.

Moderator: Thanks, William. We'll now take our next question from Sreedhar Mahamkali from UBS. Please go ahead.

Sreedhar Mahamkali: Hi, good morning. Thank you Ken and Imran.

I've got three questions as well please. Maybe, Ken, if I could pick up on your multi-year framework you've talked about in growing absolute cash profits and just trying to expand the answer you've just given us, and trying to understand it a bit more.

What I'm trying to understand is if you continue to do those things that you've talked about that you've done really well over the past few years, being competitive on pricing, paying good wages to staff, should profits continue to grow along the pace that we are seeing? For example, implied in the 2.9 billion profit guidance for the year, about 6%, is that a run rate to think about or is there a range in mind that you could talk to? That's the first one.

Secondly, I'm intrigued. You haven't really said anything about contribution from retail media in the first half margin performance. I think, Imran, you've called out volume growth and Saved to Invest, but not other areas. So does that mean whatever happens with retail media over the medium-term, that is incremental, again, subject to your willingness or market needs to reinvest that? That's the second one.

And third one, very simply is why isn't that 100 million, or so, profit upgrade not flowing through to free cash flows, please, today?

Ken Murphy: Okay. So do you want to take the last one first and?

Imran Nawaz: Well, yeah, maybe I'll start with the margin question that you asked. In terms of, if you look at the first half margin, what are some of the nice things that I feel good about?

We have more than one lever to drive up profits. So selling more of finest. We have had very strong brand performance, we've had Save to Invest. And frankly, the volume leverage of selling more to customers and keeping your cost base flat gives you that operating leverage expansion as well.

And as we always say, our target is the absolute profit growth. If you look over the last few years, we've always said that the number we solve for is the cash flow delivery. And we want to continue to grow or protect market share, which means hopefully we grow a bit above the market. That should translate into nice profit growth, ultimately into cash. And that's the number I'd ask you to keep thinking about.

The way I'm thinking about the range on cash is it's the commitment at a minimum we want to deliver every year for our shareholders so that we can continue what we're doing in terms of buyback, and dividends, and continue to invest into the business at the right pace.

In terms of cash flow outlook, look, as I said, the range is a range. We've done really well in the first half, and I'm really happy with the 1.2 billion. To be honest, I was expecting a little bit less when we started the year, but there's no bad thing.

It's true that over the last few years we've overdelivered every year on cash. So as you know, the guidance doesn't hold us back. If we can do better, we absolutely will do better.

The second half on the cash, the way I'm thinking about it is I'm expecting maybe less working capital inflow, a bit higher CapEx, and clearly the bigger part of the tax bill will also come. But by and large, I feel positive on cash and just we want to make sure that we are also protected against any fluctuations on working capital inflow as well, which can happen towards the end of the year.

Sreedhar Mahamkali: Thank you. And sorry, just to come back to Ken. Your thoughts on how we should think about that multi-year framework on profit growth?

Ken Murphy: Well, Sreedhar, as you know, we generally give guidance about one year ahead in maximum, so I really couldn't comment on the long-term. I think what you should take from this is a sense of confidence that we're focused on the right things. We're focused on sustainable growth for the long-term.

Everything we do in terms of our capital investment… And you've seen a meaningful take-up in capital investment over the last four years. And you've also seen at the year-end the ROCE we're achieving for that capital investment. So that should give you a lot of confidence that we are taking that medium, long-term view of the business, and that we are in it for the long haul.

And I could say no more than that, but I think that should give you some confidence.

Imran Nawaz: Yeah, and then on the media income, just to give you a sense, clearly, look, we're very happy when it's incremental and it drives absolute profit growth, so that's fantastic.

Then conditions decide what you do with that money. Am I happy to drop to the bottom line? Of course. If we want to reinvest it to drive even further wins and keep our edge versus competition, keep the cycle of winning going, we'd do that of course as well. So to me that always depends on the conditions, but look, we see it as an additional income stream that should in theory help us continue to grow even faster.

Sreedhar Mahamkali: Thank you both.

Moderator: Thanks, Sreedhar.

So now we'll take our next question from James Anstead at Barclays. James, if you can unmute yourself and ask your question?

James Anstead: Yeah, good morning Ken, Imran. Three questions, if that's okay?

Firstly, perhaps the really predictable question on guidance. So you've upgraded the retail EBIT number for this year today, if we take it literally, it seems to imply a very sharp slowdown in growth in 2H from the 10% you delivered in the first half. I just wanted to check, are there any technical reasons why growth should be lower in the second half, or is this mostly about you wanting to retain this flexibility?

Two other questions. Secondly, taking a step back, your retail EBIT margin is up 30 bps in the first half, which is a pretty big move in a low margin sector. Can you give us any more colour on what the main drivers of that was?

And a smaller one just to finish with, you've got this new partnership with The Entertainer on toys. Is that a model you'd consider for other non-food categories or is there something specific to the toy category that makes this partnership work here but not something to extrapolate?

Thank you.

Ken Murphy: Let me take the last one then I'll pass on to Imran to talk margin and guidance. The Entertainer has been a great success story for us in the sense that the partnership with The Entertainer has allowed us to have a partner who's an expert in toys, who's really focused on it, and who has a very strong range of proprietary owned brands that are great value products and great quality. So it's a very pleasing relationship and we're very happy with it.

I don't think it signals anything other than we are determined to find the best solution of value, quality, and range for our customers. And if that involves a partnership, then we're very open-minded about that.

If I were you, I wouldn't extrapolate that unnecessarily, but also I wouldn't be surprised if there were one or two more partnerships along the way. But it's not indicative of anything other than our desire to give customers the best possible proposition.

Imran Nawaz: So then let me take the question on guidance, James. Look, let me start by saying I'm really happy with the overall performance. Came in better than we anticipated to be fair.

And what was nice to see was the quality of the delivery in the first half. Share gains, volume-led growth. In fact, lower inflation than we thought we would have. And that felt really, really good. And based on that strong performance, we upgraded from the at least 2.8 billion to around 2.9 billion. And that feels good.

Now when it comes to the second half, what we want to do is retain flexibility to continue to win. And as we did last year, where we see opportunities to invest for customers and protect the momentum we have versus competition, I think you'd expect us to continue to look into those opportunities and retain that flexibility. That's what this is.

I think guidance has never stopped us from trying to do better and that's not going to change. So I think that's how we think about guidance, want to win over Christmas, want to make sure we have a nice momentum into the next year. But that's where we are. And at this stage, as you know, I call it like I see it and right now around 2.9 billion feels like the right place for Tesco. When it comes to the margin expansion in the first half, it is quite pleasing. As Ken said, we sold for-profit growth, absolute profit, and we sold for cash. But the how does matter, and in this case what was nice was the Safe to Invest program, we delivered 260 million of savings in the first half with actually improving customer satisfaction scores, which tells you the quality of the savings has more than offset some of the headwinds we've been having on the operating cost side. So that's a tick.

I would say the quality of the growth that we saw was also, as Ken mentioned, Finest had nice growth. Brands have had Finest growth. Both of those are accretive to margins. So you see a nice mixed benefit as well. And then lastly, and most importantly, being the cheapest grocer leading therefore to volume growth ahead of our expectations and you get that operating leverage has all led to that margin expansion. So in a good place.

James Anstead: That's very helpful. Thank you.

Imran Nawaz: Sure. Thanks, James.

Moderator: Thanks, James. So we will now take our next question, and that'll be from Freddie Wild at Jefferies. Freddie, if you could please go ahead.

Freddie Wild: Good morning, Ken, Imran and team. Thank you for taking my questions. So my first question is really about understanding the cadence of sales dynamics within Q2 itself, particularly around the progress of basket inflation, whether adverse weather impacted the early part of the court, particularly in non-food and whether Finest growth has accelerated in recent months. That'd be a fantastic colour. Thank you.

And then secondly, could you help us understand the moving parts of free cash flow into half two? Obviously we've already talked about the margin component, but the extra details given you very strong delivery on that front this morning. And finally, just a more structural question about whether you still feel your previous target leverage range is appropriate? Now, given you are substantially below that, and continue to get lower. Thank you very much.

Imran Nawaz: Thanks, Freddie. Should I start with the leverage and the cash flow moving pieces? I'll work backwards because those are the questions I wrote the way I wrote them down. So Freddie, in terms of leverage, look, the truth is we have a very strong balance sheet, and it's a result of the fact that we've outperformed on cash and profit yet again this morning. The leverage ratio, the way I think about it, it's a midterm range to make sure that have the right level of flexibility and maintain that and strength. The range we have set out is 2.3 to 2.8. As you point out, we're below that slightly, but I feel good about where the range is and have no real plans to change it. So I think we're in the right place. The truth also happens to be that when you have higher interest rates like we have at the moment, being at the lower end or slightly below is no bad thing for us, and managing your finance costs.

When it comes to the cash flow performance, look, really strong first half. Clearly profit worked well. Surprisingly, we did better on working capital inflow than I thought. So we had close to 170 million of inflow. I'd expect that in the second half, it does fluctuate much more than in the first half. So that's always for me is a bit of a watch out and it explains why we always have that wider range on working capital. Clearly, I expect the bigger tax impact from the fact that the tax rates have gone up. And if you remember, we were benefiting the last few years from the pension contribution deduction that has expired as of now. So for this year it's a more normalized tax bill that will also have a tax cash implication.

But look, the rest will be how profits will fall and everything else will decide that. But I feel good about cash. I'm expecting to be within the range. Last year, we had the same sort of shape, a much stronger first half and then a smaller second half. That's very normal for us. So this is not very unusual for us. What matters most to me is that we translate the profit we have into cash, as we said, within the range that we've guided to over the last few years.

Ken Murphy: And on Finest, Freddie, I think I mentioned earlier that we've seen 15% growth of Finest over the first half, which is pretty consistent with what we saw last year, which given, as you saw the overall market numbers, our numbers of about 3.5, 4%, it's really, really strong. And it shows a deepening penetration, more customers trading into Finest and particularly, as I said in our dine in offer, which saw 18% growth over the half. And I think we would hope as the winter months kick in and the evenings draw in, that that number will actually take up as we go into Christmas. So we're feeling really good about the innovation we had.

Over 862 new products are either innovated and launched or renovated over the 6 months, and 180 of those were Finest products. So that gives you a sense of our commitment to the Finest brands, the success it's having with consumers and the momentum we're looking to maintain on it. In terms of the cadence over the six months, I think the story really is, as

Imran said earlier, it's a volume led story. Honestly, inflation was softer than we had planned for, but that was more than offset by very strong volume growth. And that's particularly pleasing because that works very well in a retail business, as you can see, from the performance.

Freddie Wild: Fantastic. Thank you so much.

Ken Murphy: Thanks, Freddie. Sure.

Moderator: Okay. Thanks, Freddie. Just before we take our next question, I'd like to remind people if they do want to ask a question, if they could just press the raise hand icon at the bottom of your bar. So we'll now take our next question from Monique Pollard at Citi. Monique, if you can unmute yourself and ask your question. Thank you.

Monique Pollard: Thanks. Morning everyone. Just three from me. The first question, coming back once again to Finest, again, as you've mentioned a couple of times now, the Finest volumes in the UK up 15% in the first half with over 180 new products added. Just wondered if you could give us a sense of how that growth is comparing to the branded volume growth that you're seeing across the UK at the moment.

The second question on retail media. So really useful insights in terms of the fact that you are getting increasing numbers of advertisers, campaigns per advertiser, ad spend per campaign. I don't know if you are able to give us any indication of how big you think the size of this opportunity could be in three to four years versus where it is now or the potential growth in that channel?

And then the final one, just a quick one on Booker. Obviously, those weakness in the Best Food Logistics and the tobacco market. I think the tobacco market well understood that that is just structural decline. But how should we think about the fast food market service by Best Food Logistics going forward and how that might progress? Thank you.

Ken Murphy: Thanks, Monique. Let me take the last one first. I think I'd start off by saying that Best Food has a unique model in wholesale, and so far as it's a fee for service rather than actually a wholesaler per se. So to a certain extent, it's isolated from what's going on in the quick service restaurant market. I think also the second point is they tend not to be in the independent fast food sector. They tend to be in the multiples. And as you know, the multiples have over the last couple of years been challenged from a volume point of view, but that hasn't impacted Best Foods bottom line, but it has impacted their top line.

That said, I think now what you're starting to see is some of those multiples starting to fight back in terms of improving their pricing and we'd hope to see a recovery in that regard. So the way you should think about Best Food Logistics is that we acquired it as a loss maker. It's now a profit maker and a contributor to the group. It's very well run. It has a very good reputation with its clients and has a good future. So that's the way I would think about Best Food. If I think about retail media and how big it is, I think Monique, it's one of those things that we never speculate on for obvious reasons. I think, as I mentioned earlier, and I think possibly if you look at some others, they like to call it out as a very discreet thing. We see it as very integrated into the way we build trust and relationships with customers through personalization and targeting and filtering out the stuff that they're not interested in. And it's a way we build relationships with suppliers by giving them a much better bang for their buck in terms of their investment in marketing and brand building and not just trade funding. So where we want to get to is we want to get to a place where we are seen as the best destination for a supplier to invest marketing and building brands. And as a consequence of that, we look to build our media income as a subset of that.

But what it should be really doing is it should be driving out performance in terms of market share, out performance in terms of our share of new innovation products launched, and a higher rate of customer satisfaction and a sense of feeling like the Clubcard particularly, but also our media platforms are personalized to them. So that's the way I would think about it in the round. And I would go back to our multi-year framework of really we're all about driving market share, looking after all our stakeholders, investing for the future of the business and optimizing and maximizing cash profits. And then-

Imran Nawaz: Volumes.

Ken Murphy: If I then just talk about finest versus branded, I mean clearly finest is outgrowing branded in terms of volumes by a factor. What I would say to you though, which is important, is that the meal occasion market and that ready meal market and a lot of that fresh food market is own brand dominated. So it's not an apples for apples comparison. And so this trend of eating in is really a battle between ourselves, M&S, Waitrose, and the premium ready meals from the other multiples rather than us against the branded players. So I would think about it that way. Does that make sense, Monique?

Monique Pollard: Yes, that's very clear. Thank you.

Ken Murphy: Thank you.

Moderator: Okay, thanks Monique. And we'll now take our last question from Francois Digard from Kepler Cheuvreux. If you would like to unmute and go ahead please.

Francois Digard: Good morning. Thank you to take my question. The first is very short term technical one, but net financial cost. I understand that it was much better than anticipated for H1, could you guide us for the year in term of nine finance?

The second question is more long-term, coming back to the multi-year question of Sridhar. You and some of your international peers are gaining back shares against our discounter. You are adding retail media to your growth level. Are all these elements make you think that the competitive field offer a more pleasant perspective to you than it was five or 10 years ago? Are you switching from a defensive posture to a much more offensive one? So if you could, it's a little bit vague, but how do you see the Tesco in five years from now, knowing all this new paradigms you are evolving in? Thank you.

Ken Murphy: Well, I will start off and I'll pass on to Imran because he'll have a very strong view on this as well. I would always say that we felt, when we joined the business, myself and Imran, we always felt like the underdogs from the point of view that some of our, particularly our discounter competitors are much bigger than us as corporations. So we've been on the offensive from day one and we have set our stall out as a team that wants to grow share all the time, regardless of the conditions.

And so far that's what we've managed to achieve and that's what we plan to do in the future. And so we don't really give ourselves too many excuses in that regard because the competitive dynamics will always change in this market. They will always be intense. But we think we have a great team, we think we have a great proposition and we have no reason to believe that we can't keep winning. So I would say to you that this is a manifestation of how we see the world all the time, rather than a shift from defensive to offensive. I'll pass over to Imran now to respond on-

Imran Nawaz: I thought that was-

Ken Murphy: On guidance.

Imran Nawaz: Nothing to add to that. Just totally agree. On the net finance costs. Hey, yeah, look, net finance costs were better. I guess it's the benefit of having great cash performance and then managing to also earn income on that cash, which is good. So the flip side of high interest rates is that. For the full year guidance expect broadly similar to last year. That's what I'd go with at this stage.

Francois Digard: Thank you very much.

Imran Nawaz: Sure.

Ken Murphy: Thank you Francois.

Moderator: Thanks Francois. And we will take a further question and this one comes from Paul Rossington at HSBC. Paul, if you can unmute yourself and ask a question.

Paul Rossington: Good morning. Good morning. Thanks for taking the question. Just a quick one from me. Can you make any comments on promotional participation? I think we've covered most other topics, but just on promotional participation, any trends or changes there? Thank you.

Ken Murphy: Yeah, it's up.

Imran Nawaz: Look, I mean it's ticked up a few percentage points as you would expect. We've seen that trend especially remember during Covid it was abnormally low, then it started to come back up and I think now as inflation started to come down big time, clearly people are wanting to make sure they get their fair share of the brand performance. And as you could imagine, suppliers want to make sure that they part of our Clubcard prices campaigns and therefore keen to make sure we get the right level of promotions in our stores for our customers. So you do see it tick up.

Ken Murphy: Thanks Paul.

Moderator: Thanks Paul. Okay, at this point we have no further questions, so I'd like to turn it back to Ken for his closing remarks.

Ken Murphy: Thank you very much. Thanks everyone for joining us this morning, for taking the time to listen. We really appreciate it. We're very pleased with how we've performed for the last half. We believe it gives us great momentum going into the second half, and we look forward to seeing you all again in January to update you on our Christmas performance. Thank you very much and have a great day.