Halfords Group FY20 Interim Results

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Opening Remarks

Graham Stapleton

CEO, Halfords Group

Good morning everyone and welcome to the Halfords Group Interim Results presentation for FY20. It is good to see some familiar faces here today. We have a lot to update you on. We are going to do things slightly differently. Loraine will start with a review of the first-half, taking you through our financial results. I am pleased to say that half-one profits are in line with expectations, which is good. I will then provide an update on the progress we have made against the strategy we outlined at the Capital Markets Day last October. There is some good news here in that we have delivered some great early results across a variety of areas. I will then move on to how we plan to develop our strategy. A combination of the progress we have made on our existing plans together with an even better understanding of where we currently create shareholder value, gives us real confidence to accelerate our strategy. I am really excited to be able to share our thoughts here with you today. Finally, Loraine will conclude with a summary of our financial guidance. We will then take any questions that you may have.

H1 FY20 Performance

Loraine Woodhouse

CFO, Halfords Group

Operational Highlights

Good morning everybody. We saw progress in a number of important areas in the first-half, despite what has been a very challenging retail sector. After our 20-week statement trading improved and a strong end to the half, particularly in our cycling business, saw us return to growth over the last six weeks. Motoring products, as you know, was much more challenging. The last six weeks of the half were better but still down year-on-year. This is disappointing but we are encouraged by our relative performance where we took share in a number of key categories. Our services business, online and B2B all experienced growth and continue to represent a real opportunity for us going forward.

I will come on to talk about the Autocentre performance in more detail but our transformation programme is on track and we are on target to improve profitability for the third year running. You will have seen today that we announced the acquisition of McConechy's Tyre Services Ltd, giving us an additional 60 sites in Scotland and the North, a region in which we previously had little representation. Also within Autocentres we are particularly pleased with the rollout of Halfords Mobile Expert, a mobile proposition that our customers love. This will be bolstered going forward by our recent acquisition of the Tyres on the Drive business.

Last but not least, our cost and efficiency programme has netted tangible gains, with the cost savings we have made offsetting both inflation and our strategic investment in the period. Graham will cover some of these areas in more detail as he talks through our strategic progress over the last six months.

Group Financial Overview

Moving tour financial summary, I will of course cover these points in more detail but this slide represents our overall financial performance in the period. Lower sales, as we know, drove down profitability on a pre-IFRS 16 basis. We were, however, pleased with our gross margin improvement, our cost control and our cash management. It is worth mentioning IFRS 16 upfront as you will have noticed that the accounting adjustments added £4.3 million to our PBT in the first half. I should point out that I expect the impact of this to lessen as we go through the year and as we renew outstanding leases, as new leases will increase both the P&L charge and the lease liability. Any numbers I quote today, unless stated otherwise, are pre-IFRS 16.

Retail Financial Overview

If I turn to our retail business first you can see the summary performance on the left-hand side. Our like-for-like retail sales were down 3.1%. It is worth highlighting, however, that we saw an improved performance in the last six weeks of the half. Sales after 20 weeks were down 3.9% but from week 21 the next six weeks improved with like-for-like performance returning to small growth. Cycling saw particularly strong growth at 5.1% on the back of a very successful promotion. Motoring remains tough, primarily in big ticket, non-discretionary areas but as you can see, also improved versus the previous 20 weeks. Our retail sales were down year-on-year by nearly £20 million. However, we were able to mitigate some of the impact of this through a gross margin improvement of 40 basis points and tight cost control.

Retail Gross Margin

Turning first to retail gross margin, the growth in margin reflects several factors. The most significant of these is the work that we have been doing with suppliers to lower our cost of sales, whether through range reviews or through working together to identify joint efficiencies. At the same time we have seen margin improvement, particularly in cycling, through more targeted promotions. Graham will talk more about our Right Range, Right Store programme in cycling, that we nicknamed Project Peloton. Getting the right range of bikes in store and facilitating the sales of electric bikes has both improved margin and reduced stock levels. Offsetting these positive dynamics are a small adverse movement in FX and of course the mix effect of lower motoring sales.

Retail Operating Costs

Moving to costs, we flagged at the start of the year an overall cost increase of around 3.5%. However, given our weaker sales in the first half we worked hard to minimise cost where we could. As you can see from the chart, we have achieved efficiency savings of over 2%, more than sufficient to offset inflation and the incremental operating costs of some of our strategic initiatives. We have targeted a number of cost reductions over the first half but examples include rent savings of £1.5 million in retail, with rent renewals settling on average 6% lower, savings in distribution costs as we move from three to two store deliveries per week, a reduction in utility costs from better buying practices and the implementation of LED bulbs right across our estate. The one-off saving you see here is primarily from a release of our claims provision, whereby a new provider has helped us bring the cost of claims down. I should flag that you should not expect to see similar savings over the course of the second half. Many of the initiatives we have been working on started in the second half of last year, whereby if you recall, we were successful in bringing down the level of cost growth quite materially.

Autocentres Financial Review

Moving now to our Autocentre business, a really positive story in every regard. The ongoing transformation of the business underpinned by new technology is materially improving the business model, with operating margins now at around 4%, the third straight year of improvement. Like-for-like sales growth was 2.1% and like retail the sales growth in the six-week period at the end of the half was also stronger at 5.6%. It is notable that the garage market is much more resilient than retail, as much of the work is generally not discretionary. Gross margin, though a combination of better buying and lower tyre mix, was ahead of by 110 basis points. Costs grew by 3.3% as we continued to invest in colleague numbers. We know that we have additional demand that we can fulfil if we are able to fully resource each centre. The net result over the half was an EBIT uplift of £0.9 million or 39%. We are confident we will end the year with strong profit growth.

Group Cash Flow

I will move on now to cash flow. Before I go through the numbers I would just like to set this section up by explaining a couple of key points. Our half-year ended on 27th September which is unusually early. As a result we had around £30 million of supplier payments and payroll that had not cleared the bank. In these numbers we have adjusted for this payment run as though the payments had been made as otherwise, I believe we would be misleading you. Even with this adjustment the creditors figure is likely to be slightly flattered by timing and I will therefore come on to talk about what I believe is a more useful way of measuring underlying cash.

Notwithstanding creditor timing, we have improved our underlying working capital position in the first half and this has contributed to a healthy free cash flow of £44.2 million. Our cash flow, despite lower PBT is £10 million up on the previous half-year. However, whilst the balance sheet position at the reporting date is important, far more important to me is our average stock and creditor position over the course of the half. Half-year and year-end stock and creditor balances can be impacted by the timing of the reporting date. The average position, however, is much less likely to be distorted. Our average stock is down £15 million year-on-year and our average creditor days are ahead by around two days, as we work with suppliers to ensure that our days credit are reflective of the stock turn of a specialist retailer.

To flag, we have a 53rd week this year and it is likely that this will distort our year-end working capital position. Hence the importance of sharing the average position with you today.

Net Debt

For our net debt position I have also adjusted for the uncleared payment run, as without this adjustment our net debt would be artificially low. At 0.7x our net debt/EBITDA ratio pre-IFRS 16 is consistent with last year, with the improved working capital compensating for lower EBIT.

Interim Dividend

Moving now to the interim dividend, I will come back to the full year dividend later in this presentation but for the interim dividend the Board has approved a payment of 6.18 pence consistent with the dividend paid out last half-year.

Summary

To summarise briefly, sales were lower this half, driven primarily by big ticket, discretionary spend in motoring products. However, outside of motoring products where we did grow share, we saw growth in all areas of our business. We improved gross margins across the Group and our cost control was strong, mitigating the profit shortfall. Autocentres delivered another good profit performance and is on track to grow profit for a third year. Our cash generation was good with strong working capital management. Given their strategic nature, I will leave Graham to talk in a little bit more detail but after the balance sheet date we purchased the trade and assets of Tyres on the Drive and also acquired McConechy's Tyre Service Ltd, one of the largest independent garage chains in the UK.

Strategy Update

Graham Stapleton

CEO, Halfords Group

UK & Ireland's leading retailer of motoring and cycling products and services

Before I go into the strategy update I wanted to start with contextualising where our business is today. I will spend a little bit of time reminding us all of the shape of the Halfords business, both how we serve our customers and also how we currently create value for our shareholders. We are the UK and Ireland's leading retailer of motoring and cycling products and services. We are a trusted brand with over 125 years of heritage. We have market-leading brand awareness in our retail business. Over 20 million customers visit us each year. Today, despite a rapidly growing services business, we are largely recognised as a product retailer.

Nationwide Coverage

We have nationwide coverage across the UK and Ireland delivered through 317 garages trading as Halfords Autocentres, 448 Halfords retail stores, eight Halfords Mobile Expert vans and 26 performance cycling stores trading as Cycle Republic and Tredz. This gives us a unique mix of physical assets for both motoring and cycling and therefore a combination of mobile, store and garage locations.

Different parts of the business deliver different levels of return

Alongside a description of our business from a trading asset point of view, we also thought it would be useful to share with you how we create value for our shareholders today. As you will see on the slide behind me, we have divided our business into its key component parts. Retail motoring and cycling, products and services, Autocentres and B2B. On the bottom axis we show our return on invested capital and on the side axis we have the market opportunity or our growth opportunity. The size of the bubble reflects the relative size of the component parts of our business today. I should say at this point that the graph is indicative and that the bubbles are relative not absolute, for anybody intending to get a ruler out and just check the lines.

Even indicatively, however, you can see how the different parts of our business perform. Motoring products, for example, have a high return on invested capital but a relatively low market opportunity. As we know, we already have a high market share in a number of motoring categories. Autocentres on the other hand, has a good return on invested capital through low capital intensity and an improving profit margin. We only have 2% market share of a highly-fragmented market where there is no clear market leader in the UK & Ireland. This presents an interesting and very real opportunity.

For cycling, whilst we know we can grow our business we also know that it is a lower return category than motoring simply through lower gross margins. Finally, we can see that motoring services represents the vast majority of total service-related sales and delivers good return on invested capital. This gives us a significant market opportunity, especially when sold with our motoring products. This analysis tells us a lot about where we have value-creating opportunities. That is our business today, now moving to our strategy.

To Inspire and Support a Lifetime of motoring and cycling

Confident the strategy remains the right direction for the business

At the Capital Markets Day 12 months ago we set out our mission for Halfords: to inspire and support a lifetime of motoring and cycling. Our mission has not changed. It was developed with the benefit of significant customer insight and research, and we are therefore confident that it will stand the test of time. To deliver against our mission we set out these three strategic goals. Firstly, we will inspire our customers through a differentiated, super-specialist shopping experience. Secondly, we will support our customers through an integrated, unique and more convenient services offer. Finally, we will build relationships with customers aimed at enabling them to get the most from a lifetime of motoring and cycling. These goals also remain unchanged.

Inspire our customers through a differentiated, super-specialist shopping experience

Fully integrated Group website to deliver best in class digital customer experience

A year on from our Capital Markets Day we have made great progress against our objectives. Let us start with how we are inspiring our customers. We remain on track to launch our fully-integrated Group website. This will deliver a best-in-class digital customer experience enabling customers to access services from both retail, Autocentres and Mobile Expert vans through one website for the very first time. On the left-hand side you can see how the current experience looks. In simple terms, to take advantage of the full Halfords branded offer customers have to visit three separate sites that might well be laid out in three separate ways for the same product.

Later this year you can see on the right-hand side of the slide, we will be moving to one single website for our retail, Autocentre and Mobile Expert business. This will give a greater level of consistency and convenience to customers who in turn will become more aware of all that Halfords has to offer. You can see here on the left-hand side the options of a retail store, an Autocentre and if there was a Mobile Expert van in this instance, would be there as buying options for one product. So it all comes together.

Optimisation of cycling space in all retail stores

Turning to how we are inspiring customers in our stores, we have also optimised our cycling space, delivering a better shopping experience through a Right Range, Right Store approach. As well as improved sales and margin, we have also reduced working capital. Post-transformation we have seen a 20% reduction in cycling stockholding. You can see in the photographs behind me that a new approach to visual merchandising has simplified and improved our in-store customer experience. There is the before, there is the after. This has resulted in an increase of 2.5 points in cycling net promoter score.

Our range of innovative products delivered a 30% increase in sales of exclusive motoring and cycling products

Finally under inspire, our strategic focus on creating a more unique product offer has also delivered a 30% increase in sales of exclusive motoring and cycling ranges. Here you can see around the room just a few examples of exclusive products. Taking you through this slide very quickly, on the left-hand side you can see a Gtech electric bike. We have exclusive rights to the Gtech range in the UK. Moving to the right-hand side I think a really good piece of customer-led product development is the new Trunki folding kids bike we have designed with Trunki together from scratch using customer insights and is exclusive again to us. Last but not least, a favourite of mine anyway is the McLaren range of car polishing and finishing products which again we have worked solely in partnership with them. We have that exclusively in the UK too so some good examples of innovation and unique products coming through.

Support our customers through an integrated, unique and more convenient services offer

Our customers rate our proposition highly, bringing new customers to the Group

Turning to where our main focus has been over the last 12 months, how we are supporting our customers through a more integrated and unique services offer. Let us begin with our investment in Halfords Mobile Expert. As a reminder, this provides customers with a mobile solution to access our services in a way that is convenient for them. Halfords Mobile Expert is exceeding our targets and delivering very strong customer satisfaction, as you can see here. What is also really exciting is that it is attracting a younger and more female customer base than our traditional automotive services business. This means little cannibalisation of our existing business and more new customers to the Halfords Group.

Driving growth and profitability of Halfords Mobile Expert business

Clearly this is commercially sensitive but we want to give you a sense of why we are confident that we can drive profitable growth through a mobile business. Firstly, as you can see here again on the slide, we have acquired best-in-class proprietary software which allows us to maximise the number of jobs per day and deliver a healthy mix of tyre replacement and other services. This enables us to achieve a higher margin per job than a business offering a single service, for example just tyre fitting. Secondly, we also expect the costs of running the Halfords Mobile Expert business to continue to fall as we gain economies of scale and fully utilise the Halfords Group assets and skills. An example of this would be leveraging all the customers that shop on the new Halfords Group website. If you think all those going through the website seeing a mobile option. We think that will be a big acquisition tool.

Building relevance, awareness and value through new WeCheck services

Now, moving to how we are supporting customers in our retail stores. We have launched two new motoring services, WeCheck Free and WeCheck Premium. These are now delivering in excess of 30,000 car checks per week every week. The WeCheck services are important because they help us increase awareness of our services business, build our relevance and give us an opportunity to create value. Additional sales and margin comes from either identifying work that needs to be done in-store or Autocentre or by trading customers up to the WeCheck Premium offer.

On-demand WeFit trial in Autocentres continues to deliver promising results

We are also trialling our retail WeFit motoring services on demand in our Autocentres garages. This continues to deliver promising results. This offer not only broadens the range of services that we provide customers but has helped enable us to extend Autocentre trading hours.

Enable a lifetime of motoring and cycling

Accelerated investment in financial services offer giving us double-digit growth year-on-year and access to a new customer demographic

The final pillar of our strategy is focused on building stronger relationships with more customers over their lifetime. This year we have accelerated the investment in our financial services offer. We now have a much-improved proposition online and instore across retail and in trial and about to launch in our Autocentres business. This new proposition is delivering substantial double-digit growth year-on-year but also importantly gives us access to a new customer demographic, which is an exciting development for us.

Cost and Efficiency

Whilst I have focused on the customer initiatives here, it is also worth reminding you at this point that much of the investment we have made in our strategy over the last half-year has been funded from cost and efficiency savings. Whether in lower cost of goods for resale or in reducing selling and administrative costs. Loraine talked about this earlier, so I will not repeat the detail but that is an important point.

Summary of Business and Opportunity Today

Finally, to summarise all that I have just talked you through and where we currently stand with the business today. We have a market-leading, trusted brand with good customer awareness. We have a unique and differentiated omni-channel portfolio through our combination of stores, garages and vans. We have made great progress in delivering the strategy we shared with you at the CMD across all three of our strategic goals. We have shown you where we currently create value and where the potential market growth opportunity is.

Clear rationale to further accelerate our service-led strategy

In addition to leveraging these Halfords opportunities there are also a number of growing macro tailwinds which further support our service-led strategy. Cars and bikes are becoming increasing complex, driven in part by the growth in electric mobility. Maintenance, servicing and repair of both cars and bikes therefore requires even more specialist skills. Customers are demanding greater levels of convenience from businesses and brands, be that on-demand services and delivery or the growth in mobile options. There is a continued shift towards do it for me, exacerbated by the combination of increasing product complexity and consumers' everyday time pressures. The unique and growing parts of our business today, together with the opportunities and strengthening tailwinds in the market, give us a clear rationale to further accelerate our service-led strategy.

Accelerating the Strategy

I am now going to talk you through our updated plan. I will only focus on the elements of the strategy that we intend to accelerate in this part of the presentation. It is important to note that we will still be delivering the majority of the existing CMD plan. For example, innovation and the development of our cycling and motoring product business still remains key. This is an emphasis shift, not a wholescale change in direction. Put simply, if I was to summarise this shift over the medium-term, this is it. We will evolve into a consumer and B2B services-focused business with a greater emphasis on motoring, generating higher and more substantial financial returns. That is the heart of where we are going.

Accelerating the growth of our Autocentre business

Where will we be accelerating investment to deliver this shift? Firstly, we plan to significantly grow our Autocentre business. Our Autocentres remain on track to deliver a third consecutive year of profit growth and our operating margin has doubled in the last two years to circa 4%. Even though we are seeing growth we know that our Autocentres are not conveniently located for many customers to use. Our insight shows that customers require a drive time of less than 20 minutes if they are to access Autocentre services. This makes sense when you think of the customer journey. A customer has to drop a car off, sometimes go back home, then get back to the Autocentre and drive back home again. It is a lot of travel. In many parts of the country the Halfords Autocentre drive times are well-over 30 minutes. We therefore feel it is the right time to expand our Autocentre network to give more people better access to our motoring services.

What will this look like? In the first chart you can see our current footprint. This is represented by the orange dots. The good news is we have already made progress. I am delighted to share with you that as part of this acceleration we have acquired McConechy's Tyre Services Ltd, one of the largest independent garage chains in the UK. The business employs over 330 skilled staff and operates 60 sites in Scotland and the North of England, as well as having close to 100 vans providing 24-hour breakdown services for commercial customers. This is a highly complementary acquisition and will increase the size of our site footprint by around 20%. The McConechy's business is illustrated on this second chart by the blue dots.

Looking into the future we believe there is potential for 550 Autocentres across the UK & Ireland, which will bring our drive time in line with customers' expectations. You can now see the build from just under 380 autocentres to the 550 on the third chart on the next chart there. These are the bright green dots. You will see Ireland there being a big part of the opportunity.

Accelerating the growth of our Halfords Mobile Expert business

Moving to our mobile services business, we also plan to continue the development of our Halfords Mobile Expert proposition, aiming to increase this from eight to 200 vans over the next 3-5 years. The recent acquisition of Tyres on the Drive, a mobile tyre fitting business with best-in-class software, will significantly accelerate this rollout, taking the number of our mobile vans from eight to 68 by the end of this financial year. The first chart shows where our customers can currently access our Mobile Expert services. Building on this you can see on the second chart in the grey how our coverage increases with the acquisition of the 60

Tyres on the Drive vans. Finally, the last chart shows how we move from 68 vans to national coverage, giving most customers access to a Halfords Mobile Expert service. This is shown in yellow on the chart.

Increased investment to enable growth in our WeFit services

Finally in motoring services, we will increase investment in the provision of WeFit services in our retail stores. For example, the fitting of wiper blades and headlight bulbs. This will be enabled by best-in-class customer contact strategy and the redeployment of labour in store to provide more WeFit trained colleagues to better service customer needs. That completes the acceleration in our motoring services plan, I am now going to talk about our physical portfolio.

We will trial a more inspirational, convenient, integrated and digitally enabled customer experience within a location

You have already head me talk about the launch of our new website later this year and how that integrates our garage, retail store and mobile offer for the first time. Once this is complete we want to take the same principles and apply them to our physical portfolio in a town. This will mean creating a more seamless customer journey wherever a customer shops, be that in a retail store, an Autocentre or Mobile within that town. Alongside this we will also create a more inspirational and digitally-enabled physical shopping experience for our customers.

Let me walk you through where we are currently and where we are planning to be in the future. As shown on the left, is a typical large town or city today. Our customers have access to multiple retail stores, shown in the orange, and maybe an Autocentre garage, depending on where you are. Most of our retail stores are on expensive and busy retail parks, which have limited benefit from the associated footfall of other retailers. Customers expect easy access, parking and exit to come to Halfords from these very busy locations and typically come to us for a very specific purpose, very destination mission. Our research and insights suggest that there is an opportunity to deliver customer needs in a different and better way, and potentially at lower cost.

We are therefore trialling a new customer experience in two locations next year which you can see now on the right-hand side of this slide. It will encompass a more inspirational destination retail store, shown in orange in the centre, an updated Autocentres garage design, in green in the bottom-right hand corner, a new format that will combine an Autocentres garage with a small store for motoring products, represented in the blue and then obviously a Halfords Mobile Expert offer shown here by the vans. We believe this will enhance our customer offer and over time reduce our fixed cost by changing the mix of physical, digital and mobile assets in a single geographical location. It will also allow us to test whether we can deliver a greater level of sales from a reduced and less expensive footprint.

In order to deliver the plan investment will be required

Infrastructure

In order to achieve our plan and that acceleration we will need to invest. Firstly, in infrastructure. In order to build a bigger and more successful motoring services business we will need to ensure we are able to communicate with our customers better than we do today. We know that we will need to invest in technology to enable customers to seamlessly book our services and consistently receive the specialism and advice that we can offer. This will include a new customer contact centre and some digital investment. We are also developing a unique digital services customer and colleague management system for scheduling workflow and further improving customer experience. This is already in test in our Autocentres business and we are now looking at how we take the same principles and apply them to both our retail WeFit operation and our Mobile Expert Business. Similarly for our B2B business, we will continue to invest in systems and infrastructure to help maximise our growth potential and increase our market share.

People

We know that the growth in services will require greater investment in colleagues, both in terms of training to underpin our services offering and also to ensure that we retain the right skills in the right locations.

Acquisition

Thirdly, we will also continue to look at how we accelerate the growth in Autocentres, supplementing strong organic growth with acquisition opportunities. Our immediate focus will be on successfully integrating the McConechy's and Tyres on the Drive acquisitions into our existing business.

Marketing

Finally, we will invest in marketing, looking specifically at the ways in which we drive awareness of our Group services offer, with an increased focus on social and digital marketing.

Delivered through our ongoing focus on delivering cost and efficiency benefits

We will aim to fund a significant proportion of the incremental investment through an ongoing focus on cost and efficiency. We will continue to lower costs across all areas of our business but with particular emphasis on our supply chain, our property portfolio and our infrastructure costs through better procurement processes. To further improve our product costs I am very pleased to announce that we have entered into a strategic buying alliance with Mobivia, a market leader in the European motoring products and services space. Our first focus will be on collaborative buying opportunities but this partnership will also enable us to share best practice across a number of areas. Finally, as a reminder, earlier I talked about return on investment and market growth. We will also continue therefore to work on improving the profitability of our cycling business across both Halfords retail and performance cycling.

Customers, Colleagues and Shareholders

Customers will have…

By implementing this accelerated plan effectively and evolving into a consumer and B2B services-focused business, what does that mean we will deliver for our three key stakeholders? Let us look at our customers first. Customers will benefit from a significantly more convenient services proposition, with services delivered consistently and offered when and where they want them. They will have better access to technical advice and expertise, together with a market-leading digital customer experience both online and in stores, garages and mobile.

Colleagues will see…

For colleagues the plan will deliver even greater clarity and focus across the Group. Excitement around the accelerated investment and growth, further investment in colleague expertise and specialism, and a business which provides even more cross-Group career opportunity.

Shareholders will see…

Finally, for our shareholders the change in emphasis towards services, offers sustainable profit growth and improved return on invested capital over the medium-term. It delivers a business which is focused on areas of significant opportunity and is less exposed to the volatility of FX, weather and customer sentiment. Finally, it creates even higher barriers to entry for our competitors.

What does this mean for the business?

In summary, we are confident that this is the right path for long-term growth. It is an acceleration of the existing plan, built up with significant customer insight and research. A plan which exploits market share opportunities and builds on existing growth. It will mean that the shape of our business will change significantly over time. Over the medium-term as our business evolves, service-related sales will double as a percentage of total Group sales. Autocentres will represent a larger proportion of our Group profit. We expect to see a reduction in fixed costs with an opportunity to go further if our property trials are successful. We will lower our exposure to recent headwinds.

Focus for FY21

As we initiate the plan our focus for FY21 will be to specifically accelerate investment in optimising our new Group website; integrating our McConechy's acquisition and increasing our estate to 400 garages; integrating our Tyres on the Drive acquisition and growing our Halfords Mobile Expert offer to 100 vans; scaling our WeFit services in retail stores through investment in our customer contact strategy and increasing the number of WeFit trained colleagues; and finally trialling a more inspirational, convenient, integrated and digitally-enabled shopping experience in two locations.

To fund some of the investment required to deliver our plan we will remain very, very focused on cost and efficiency, specifically improving profitability in our cycling products business and the continued delivery of significant cost efficiencies across the Group. Thank you. I appreciate there is a lot to take in. Please save your questions for a few more minutes whilst Loraine updates you on our financial guidance. Thank you.

Financial Guidance

Loraine Woodhouse

CFO, Halfords Group

Full-Year Dividend

I have two final things to cover, our dividend going forward and our financial outlook. To take the dividend first, the Board has looked forward to the future level of dividend pay-out. In taking its decision we have considered the current market outlook, the need for investment in the business, as Graham has just described, the balance sheet position and of course the importance of our dividend pay-out to investors. In a challenging retail market Group profitability has been lower and as a result, against our expectations set out a year ago, operating cash flows have also been lower. At the same time there is a need to invest in the business and particularly to take advantage of some of the opportunities in front of us today. Whilst the Group remains very cash-generative, the Board believes it is prudent to preserve cash. We need to fund investment in the growth of the business whilst at the same time maintaining a healthy balance sheet.

As a result the Board is expecting to recommend a final dividend of 8 pence per share, a reduction of around 35% on the prior year final dividend. On this basis the proposed full-year dividend this year would be 14.18 pence against 18.57 pence last year. The reduction in the final dividend would also have the effect of reducing future dividend pay-outs with the FY21 dividend expected to be reset to circa 12 pence per share. The accelerated strategy set out by Graham this morning will deliver an improved return on invested capital over the medium-term. The targeted growth in less capital-intensive businesses enables us to sustain the reset dividend going forward.

Financial Guidance

Moving finally to our financial outlook. There are a few points worth highlighting. We are today reaffirming our underlying PBT guidance for FY20 which prior to any IFRS 16 impact and for the 52-week period remains between £50 million and £55 million. Naturally, our cash flow in the second half will be impacted by the acquisition and integration of Tyres on the Drive and McConechy's business. We expect additional capital, including the acquisition cost, of around £11 million and associated exceptional restructuring costs of £2-3 million. For FY21, as I think you would expect me to say, in the current economic environment it is too soon to provide specific financial guidance. Two things are worth flagging, however.

Firstly, our capital expenditure guidance excluding any cost of future acquisition, remains unchanged at between £40 million and £60 million. In operating cost, however, in FY21 we will be seeking to increase our relative investment in the infrastructure necessary to support an enhanced services business. For example, our new customer contact centre. We will also be aiming to invest in colleagues to ensure that we have the right number of trained colleagues in stores and garages at any given time. Some but not all of the increased cost will be mitigated by ongoing cost savings.

Summary

Thank you. I appreciate it has been a really long session today. We had a lot to share. I leave you with one final reminder of what we are setting out to achieve. We are evolving into a consumer and B2B services-focused business with a greater emphasis on motoring, generating higher and more sustainable financial returns. Thank you.

Q&A

Kate Calvert (Investec): Assuming your two trials, these property trials are successful, how many of these inspirational Halfords stores do you think you ultimately would need to cover the country and how many of your existing stores are in the right location for them?

Graham Stapleton: I suppose that is part of why we are doing the trial, to try and assess what that might look like. I think we have quite a number of large towns and cities with more than one Halfords store, which gives us the opportunity to reduce potentially some of our retail portfolio and move into the new format we have talked about of motoring products and Autocentres together. There will however though be some parts of the country where there is only one Halfords store in that location and we would probably wish to retain it because it makes sense from a customer and a profit perspective. In that location we may still decide to put in a new, more inspirational shopping experience though, albeit there is still only one store there.

Kate Calvert: A second follow-up to that, in terms of your Autocentres portfolio you have got at the moment, the McConechy's stores coming in as well, do you need to do much restructuring to the actual Autocentres do you think, to achieve your ambitions?

Graham Stapleton: In terms of numbers of Autocentres?

Kate Calvert: The numbers are going to go up but the existing portfolio is there much restructuring needed within that or are they well-located?

Loraine Woodhouse: I think they are generally well-located. There are opportunities. We know from our analysis that a bigger Autocentre performs better so we have a number of towns where we would like larger premises and if the right opportunity came up we would move those Autocentres. However, we do not have a wholescale restructuring to do of the estate. If anything, we have probably been doing that over time.

Graham Stapleton: One of the advantages we have got is there are 208 leases coming up over the next four years. We have the opportunity to reshape where some others may not. There is a lot more flexibility.

Matthew McEachran (N+1 Singer): Some more questions on Autocentres, if that is okay, please. The first one is regarding your target for next year, the 400 sites. Am I wrong in thinking that you are already at 417 post the acquisition or have I missed something there?

Graham Stapleton: We are just under 380 actually with the acquisition. I think it is 377, to be absolutely precise. We have got the opportunity and really a focus next year, as I think I mentioned, was integration. Making sure we integrate the businesses, get the model working across the McConechy's estate and then potentially add a few more centres at the end of the next year.

Matthew McEachran: You have obviously done some work around McConechy's and I understand that it is running roughly around breakeven. You are delivering a 4% margin internally. What are the major shortcomings, if you like, in that business? What are the three top things that you are going to go and hit when you integrate the business?

Graham Stapleton: It is opportunities. There is an opportunity to bring some of the scale of Halfords to that group. Obviously leveraging our brand, our brand awareness will be a big positive. We have got a very much better operating model now in our Autocentre business that we have worked on as part of the transformation programme for the last two years. That digital platform that I mentioned is an opportunity there for them. We will also do our best to leverage all the good bits that McConechy's already have. They have 330 highly skilled technicians. They are a quality operation in Scotland. They are well-known. They have a commercial operation, as I mentioned, with the vans that I think we may be able to learn from.

Loraine Woodhouse: I think there is also an opportunity, Matthew, to in the same way that we will do with Tyres on the Drive, is move the mix of business away from being predominantly tyres into more profitable, higher margin service and repair jobs. That model makes a significantly higher gross margin and it is advantageous for both Tyres on the Drive and for the McConechy's model, which is not entirely tyres but is much more tyre-based than we would be today.

Matthew McEachran: The last question is, you talk about 4% margin. Obviously the business is coming from a very low base but has historically driven a much higher margin than 4%. Could you give us a sense as to what the margin would need to be for the enlarged business, including McConechy's and Tyres on the Drive, to actually make or meet in terms of your return on capital employed, your weighted average cost of capital? Are you actually already beyond that level?

Loraine Woodhouse: The operating margin, as you say, is around about 4%. The operating margin of retail for the first half is 4.5% but if you look at our overall stock numbers, £1 million of it is tied up in Autocentres and the other £170 million is tied up in retail. We are already at a point because it consumes relatively limited capital, where the return on investment is reasonably strong. There is more to go and if we look at the market I would say operating at around a 6% operating margin seems to be broadly where the market is at.

Matthew McEachran: Sorry, can you clarify that? I am talking about the return on capital employed. The business acquired the Autocentres group so you have already got an established capital base in Autocentres. I am looking at it in terms of delivering a return over and above your weighted average cost of capital in Autocentres in its entirety. What level of margin you would need to achieve because I am wondering whether or not you are yet at that level.

Loraine Woodhouse: No, I do not think we would be quite yet at that level if you were looking at the historical goodwill associated with Autocentres. I am looking at where we are today investing going forward.

Tony Shiret (Whitman Howard): I wondered if you could give us some sense of the relative in terms of profit margin dynamics of cycling versus the rest. I have been increasingly thinking as we were going through, does it actually fit with what you are trying to do going forward? In five years' time when we are all sitting here, whether we will still be talking about cycling.

Graham Stapleton: It is a good question, Tony. Thanks for that. The cycling business is still very, very important to Halfords. We have established a brand relevance there over many years. We have a big market share. It delivers a lot of sales and margin to the Group and, as I said in the presentation, it is still a big part of the CMD plan. That still carries on. We have just talked about the acceleration today. There are still opportunities in cycling structurally, the health benefits, the investment in infrastructure, climate change. There is an enormous number of positive tailwinds for this business. As you have seen here, we are still seeing growth. The growth of electric I think is still at a very early stage of development. It might be 15% of our business but I think there is a lot more to go for. If you look at the penetration of electric bikes in the UK it is about 0.6%. In France it is 1.5%. In Germany it is 5.5% so there is a long way to go. The reason I say about electric is I think electric hybrid cars and electric bikes almost bring these two categories together from an electric mobility point of view for the first time more closely. They also mean more servicing of both bikes and cars because they are more complex. The bike becomes more complex too. I think, yes, it is relatively lower profit but there are opportunities to make more profit still in cycling and there are a lot of tailwinds to ensure that carries on growing.

Loraine Woodhouse: To your question on the other point, Tony, I am sure you are not expecting me to read off the relative gross margins.

Tony Shiret: I was thinking more of the operating margin.

Loraine Woodhouse: There is plenty of data out there around other businesses that give you a good sense of where cycling businesses tend to sit. The challenge with the cycling business is the lower gross margins as a starting point, the high cube that you have to move through your system, typically greater FX volatility because it is directly sourced often in dollars, and the lead time of some of the product, which means that you are perpetually trying to balance fluctuating demand with much less flexible supply chain. Now, we have made really good progress on all of those areas and much of the improvement in stock and gross margin that we talked about this morning is driven by our cycling business. We know we have got a lot more opportunity to go but the fundamentals of it mean that it is structurally more challenging. We tried to show you the differential on the chart as best we can without telling you what you really want to know.

Adam Tomlinson (Liberum): In terms of the more recent trading, that six-week period feels like it has been driven more by your own self-help, your own initiatives as opposed to any improvement in underlying customer or consumer activity. Whether that is a fair summary and the balance of those two parts? Then, other strategic components you have talked about in the past, improving the cross-shop between retail and Autocentres. I think you have mentioned that was 2% in the past. Any improvements there? Also on the services side, improving that penetration in terms of adding those service and those fitting services to product sales. Any comments you can give on that as well, please.

Graham Stapleton: I think the trading in the last six weeks is definitely some of the initiatives that we have talked about impacting the business and meaning that we are growing our performance from the first 20 weeks. There is definitely some of that, that we are driving. Obviously the weather comparatives year-on-year do ease a little bit. If you remember, we had the hottest summer for 100 years. That started to peter out in September last year so there is definitely in some of our weather-related categories some improvement there too. I think it is probably a combination of those two things, I would say, but some good progress on the strategy is definitely helping us move things forward there.

In terms of just take penetration first before we do cross-Group, penetration of services has increased significantly in the first-half. It is an area we are really pleased with. Our number of service jobs has gone up 12% year-on-year. That is what I look at as the real measure of activity, the number of customers that are enjoying the services that we offer. That 12% growth is largely down to the increase in penetration that we have seen and not just in motoring but cycling also with our Cycle Care Plan.

In terms of cross-Group, cross-Group percentage has grown from the 2%. We are seeing, for example, tens of thousands of the MOT customers that I referenced last year coming back a second time now, which is good. We are continuing to look at initiatives and ways of increasing that cross-Group relevance. The website will obviously help when we launch that. The trial next year, which is trying to bring all the parts of Halfords in a town together, will also help. Next year we will also be talking about some motoring services membership scheme programmes that we are going to be introducing to support the plan we talked about today.

Lucy Sharma (Liberum): First of all, you talked about increasing your marketing so I wondered if you can quantify what you spend at the moment as a percentage of sales to where that can go. Then also quantify the benefits of Mobivia, the buying alliance. If you could say what that could potentially deliver please?

Graham Stapleton: In terms of Mobivia the buying alliance will focus initially on Far East sourced products so where we both source products from China, for example. They have a very big own brand motoring products business and so do we. We are sometimes going to exactly the same factories with similar specs. We are going to start by testing how much opportunity there could be there to collaboratively source. Not just motoring, we are also looking at some cycling. They sell electric bikes too. That is where we will start. We have not quantified what that might look like cos we're still in very early stages of this partnership. However, we are obviously hoping there will be value there and that that will grow over time outside of just own brand.

Lucy Sharma: Can you say how much you source from that area at the moment?

Graham Stapleton: I do not think we publicly stated that. What I would say is that we have publicly stated that 50% of our sales are own brand and we are moving that to 60% as part of the CMD strategy. You can gather that that is quite a big number.

The first question was around marketing spend. I do not think we are talking about materially big increases here. We are probably looking at repositioning some of our existing marketing spend into services. A big emphasis in our marketing spend towards services as we accelerate into that part. However, we do accept that if we want customers to become more aware of our services business, and it has little awareness today, particularly Autocentres and Halfords Mobile Expert, there has to be some incremental investment on top of that. We are not talking tens of millions.

Question: A quick one on the 550 target for nationwide rollout [inaudible]. Is your preference to do that through putting in more capacity or would you prefer to do it via acquisition of independents?

Graham Stapleton: Honestly, we are looking equally at both. They both have their merits, there is no doubt. Sometimes you will be able to find better quality sites in the right locations doing it organically, rather than buying a business and then having to reorganise what you have bought. However, equally sometimes buying a business means that you are buying skills and skills in this particular market are difficult to find sometimes. There are pros and cons, hence why we are looking at it equally.

Erik Salz (JP Morgan): Good morning. You mentioned an initiative you are taking with Klarna for customers. Can you talk about what the benefits are for you in that respect?

Graham Stapleton: The financial services offer we are very excited about. We are seeing double-digit growth in that part of our business. We are excited about it because it is bringing a new customer demographic of younger customers into the business. It is helping customers afford more so wherever we are seeing that financial service take place customers tend to spend more because they can afford it over a long period of time. However, the area I am most excited about it the financial services business and what it will do to our Autocentres. That is in trial and just about to launch this week across our Autocentre business. In the Autocentres world, the garages world there is little financial services on offer and yet it is a world where customers get big bill shock after an MOT sometimes or a service. I think us being then able to help them spread the cost of that over time and being the only person potentially in a town that can do that could give us a very significant competitive advantage. It underpins part of why we want to accelerate our Autocentres business.

Thank you very much indeed. Thanks a lot.

Loraine Woodhouse: Thank you very much.

[END OF TRANSCRIPT]