

## Summary financial review



A handwritten signature in black ink, appearing to read 'H Dodd', with a horizontal line underneath.

Howard Dodd

'The year is characterised by success in driving higher sales and by substantial costs to modernise, improve competitiveness and make Boots more efficient. Clear business plans together with rigorous monitoring of performance have made a significant contribution to progress in the year. We were able to report that all the initiatives to drive growth were implemented within cost targets.

The Group have operated a revised process to approve investments and allocate capital over the last year. By adopting a broad range of measures it has enabled a better analysis of the risk and return associated with each proposal. We have also seen a significantly higher proportion of capital spend directed towards the two core businesses Boots The Chemists and Boots Healthcare International. To underpin the discipline and focus with which capital will be used within the Group, we intend to return £700m of surplus share capital to shareholders. It improves the efficiency of the balance sheet and it will be in two equal tranches over the next two years. The second £350m is dependant upon the cash flow performance of the Group and this is a major area of focus over the next 24 months.'

We have reviewed our financial strategy during the year and intend to increase our debt levels over the next couple of years by returning surplus capital to shareholders through our on-going share buyback programme. This will improve the efficiency of our balance sheet and enhance Earnings Per Share. Whilst balance sheet efficiency is important, we do intend to maintain a strong investment grade credit rating and will be targeting a range of financial measures, in particular cash flow, to ensure that this is achieved.

During the year we continued our share buyback programme and have now completed the return of the Halfords disposal proceeds. Since 1997 we have returned over £1.1bn of surplus capital by repurchasing shares.

We also implemented a new investment appraisal process based upon a range of cash flow and accounting measures to assess value and risk. These include cash flow based criteria such as net present value and payback, as well as return on capital employed and time to break even. This process is being rigorously applied to our store-opening programme in particular. It is targeting over 80 new stores at a capital cost of approximately £104m over the two years 2003/04 and 2004/05.

**Turnover** from continuing operations increased by 4.7% to £5,326.4m. This reflects the continuing good progress being made in Boots The Chemists where sales increased by 4.5% and the strong growth in Boots Healthcare International where sales were up by 7.8% (in local currency).

**Operating profit** from continuing operations including share of joint ventures grew by 6.0% to £550.1m. Growth initiatives drove up costs and higher Getting In Shape costs represented a major non-comparable cost increase. However, operating profit in the year benefited from significantly lower losses from businesses either closed or rationalised a year earlier. As you have read, during the year we announced a reduction in the head count at our head office. Around 1,000 of our people applied for voluntary redundancy – considerably more than we expected. The cost of these redundancies, which was £45.5m, has been taken against profits in 2003/04, although the people will actually leave during the current year. In total over 1,500 will have left the business under the Getting in Shape programme since it began last year.

All of the actions taken to date under the Getting in Shape programme will deliver benefits of £93m in 2004/05, with full year benefits of £132m for 2005/06. We intend to explore the scope for additional productivity and efficiency improvements during this year.

**Profit before tax** was up 18.0% to £581.0m. This has been helped by an exceptional gain of £36.4m primarily relating to the disposal of property. In addition, last year included £123.2m loss on the sale of Halfords and £34.5m costs for the closure of part of the wellbeing services offering. These were both shown as exceptional items and were partially offset by an exceptional interest credit last year of £92.1m arising from the closure of interest rate swaps.

**Taxation** Excluding non-operating exceptional items, the effective tax rate for the group was 30.9%, slightly lower than last year's rate of 31.7%. We continue to focus on reducing the effective tax rate, but any actions to bring it down must fully support business priorities and avoid complexity in group operations.

**Basic earnings per share** before exceptional items increased by 7.1% to 48.2p (basic earnings per share increased by 47.8% to 52.9p). The weighted average number of shares in issue decreased in the year from 838.1m to 780.0m as a result of the continuing share buyback programme.

**Dividend** The board has confirmed a policy of sustainable dividend growth and we will be targeting a dividend cover ratio of 1.75 times over the medium-term. Consistent with this policy the board has proposed a final dividend of 21.0p. This brings the total dividend for the year to 29.8p, an increase of 4.2% over last year and in line with the last three years' dividend growth. On the share price at 31st March 2004 of 619.5p this represents a yield of 4.8%.

**Capital structure** The company has continued its policy of returning surplus capital to shareholders by repurchasing shares in the market. This amounted to £259.9m in the year to 31st March 2004 (2003 £462.8m), of which £191.1m completed the return of the Halfords disposal proceeds to shareholders.

Surplus share capital has been identified and a £700m return of surplus cash to shareholders over the next two years through share buybacks is planned. This is viewed as prudent and demonstrates the determination to deliver the growth plans for Boots in a focussed and disciplined way. £350m will be returned in 2004/05 but clearly the second tranche will depend upon the performance of the business and its generation of net cash flow.