CHIEF FINANCIAL OFFICER'S REVIEW

Duncan Tatton-Brown
Chief Financial Officer

> "Operating profitability continued to strengthen in the period from better operational efficiency and the benefits of the Morrisons agreement."

View more information about our financials on pages 131 to 203

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For the period to 30 November 2014 Ocado delivered robust growth driven by an increase in the number of new customer acquisitions, improvements to the proposition to customers and an increase in the frequency of shops from existing customers. This was complemented by additional revenues from our first platform arrangement with Morrisons.

Operating profitability continued to strengthen in the period from better operational efficiency and the benefits of the Morrisons agreement. This was offset by the annualised impact from the depreciation and amortisation arising from CFC2 and additional costs from strategic initiatives to support future growth in the business.

	FY 2014 £m	FY 2013 £m	Variance
Revenue[1]	**948.9**	792.1	19.8%
Gross profit	**312.9**	247.5	26.4%
EBITDA[2]	**71.6**	45.8	56.3%
Operating profit before share of result from JV and exceptional items	**14.2**	1.0	
Share of result from JV	**2.4**	0.9	
Profit/(loss)before tax before exceptional items	**7.5**	(5.1)	247.1%
Exceptional items[3]	**(0.3)**	(7.4)	(95.9)%
Profit/(loss)before tax	**7.2**	(12.5)	157.6%

1. Revenue is online sales (net of returns) including charges for delivery but excluding relevant vouchers/offers and value added tax. The recharge of costs to Morrisons and fees charged to Morrisons are also included in Revenue
2. Excluding exceptional items and share based management incentive payments EBITDA was £76.6 million (2013: £48.3 million)
3. FY 2013 exceptional items include exceptional finance costs

REVENUE

	FY 2014 £m	FY 2013 £m	Variance
Retail	**903.8**	784.2	15.3%
Morrisons recharges[1]	**27.8**	2.4	1058.3%
Morrisons fees[2]	**17.3**	5.5	214.5%
Total revenue	**948.9**	792.1	19.8%

1. Morrisons recharge income is derived from the charging of distribution costs and administrative expenses
2. Morrisons fees related to annual licence fees, technology support, research and development and management fees

GROSS PROFIT

	FY 2014 £m	FY 2013 £m	Variance
Retail	**267.8**	239.6	11.8%
Morrison recharges[1]	**27.8**	2.4	1058.3%
Morrisons fees[2]	**17.3**	5.5	214.5%
Total gross profit	**312.9**	247.5	26.4%

1. Morrisons recharge income is derived from the charging of distribution costs and administrative expenses
2. Morrisons fees related to annual licence fees, technology support, research and development and management fees

Revenue increased by 19.8% to £948.9 million for the period. Revenue from retail related activities was £903.8 million, an increase of 15.3%, which we believe to be ahead of the online grocery market. Revenue growth was driven by an increase in average orders per week to 167,000, up from 143,000 in 2013, offset by a modest reduction in average order size, down from £113.53 in 2013 to £112.25 in 2014.

We continued to expand our non-food offering in the period and revenue from it increased by 51.9% year-on-year.

The Morrisons agreement contributed £45.1 million of revenue in 2014 (2013: £7.9 million). This comprised annual licence fees for services, technology support, research and development, management fees and a recharge of relevant operational variable and fixed costs.

Gross profit rose by 26.4% year-on-year to £312.9 million (2013: £247.5 million). Gross margin was 33.0% of revenue (2013: 31.2%), ahead of 2013 due to additional gross profit attributable to the Morrisons arrangement in the period.

Retail gross margin reduced by (1.0)% to 29.6% (2013: 30.6%) as a result of increased price competition, but offset by lower average product wastage. Average product wastage reduced to 0.8% of retail revenue (2013: 1.0%) mainly caused by improvements at CFC2 as volumes increased. Gross profit from our arrangement with Morrisons was £45.1 million, an increase from £7.9 million in 2013, driven by the growth in the Morrisons.com business and the full year effect from the Morrisons fees.

Other income increased to £39.4 million, a 70.6% increase on 2013 (2013: £23.1 million). Media income of £25.5 million was 2.8% of retail revenue (2013: 2.4%). Income from website related activities continued to grow ahead of the rate of increase in revenue because of increased demand from our suppliers, the benefits of scale and a wider product range. Other income also included £8.9 million (2013: £3.0 million) of income arising from the leasing arrangements with Morrisons for MHE assets and £2.5 million (2013: £0.9 million) of rental income relating to the lease of CFC2. This income, for the MHE assets, is generated from charging MHE lease costs to Morrisons and equates to the additional depreciation and lease interest costs that we incur for the share of the MHE assets effectively owned by Morrisons. Other income also included a payment of £1.2 million for the surrender of the lease at our existing White City spoke whose operations are being transferred to a new build site nearby at Park Royal.

OPERATING PROFIT

Operating profit before the share of the result from the joint venture and exceptional items for the period was £14.2 million, compared with £1.0 million in 2013.

Distribution costs and administrative expenses included costs for both the Ocado and Morrisons picking and delivery operations. The costs relating to the Morrisons operations are recharged and included in revenue. Total distribution costs and administrative expenses including costs recharged to Morrisons grew by 25.4% year-on-year. Excluding Morrisons, costs grew by 16.1%, in line with the growth in the retail average orders per week.

	FY 2014 £m	FY 2013 £m	Variance
Distribution costs[1]	**193.2**	168.6	14.6%
Administrative expenses[1]	**62.1**	54.7	13.5%
Costs recharged to Morrisons[2]	**27.8**	2.4	1058.3%
Depreciation and amortisation[3]	**55.0**	43.9	25.3%
Total distribution costs and administrative expense	**338.1**	269.6	25.4%

1. Excluding chargeable Morrisons costs, depreciation, amortisation and impairment charges
2. Morrisons costs include both distribution and administrative costs
3. Included within depreciation and amortisation is a £2.6 million impairment charge in the period

CHIEF FINANCIAL OFFICER'S REVIEW continued

"The improvement in mature CFC UPH was driven mainly by CFC2 productivity which now exceeds CFC1."

"In July 2014, Ocado announced plans for our next CFC located in Andover, in the south of England."

View more information about maximising efficiency on pages 22 & 23

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At £193.2 million, distribution costs increased by 14.6% compared to 2013, lower than the growth in retail sales of 15.3%. Operational efficiency improved at both CFC1 and CFC2. Overall mature CFC UPH in the second half was 147 in 2014 (for CFC1 and CFC2 combined) compared with 135 in 2013 (for CFC1 only). The improvement in mature CFC UPH was driven mainly by CFC2 productivity which was over 150 UPH by the end of the period. Deliveries per van per week have risen to 163 (2013: 160) as customer density improved as a result of the increase in orders with only a modest growth in geographic delivery areas, offset by a reduction in road speeds due to increased congestion and an investment to improve on time delivery in a number of locations (deliveries on time or early improved from 95.2% in 2013 to 95.3% in 2014). During the period we opened a four new spokes in Ruislip, Enfield, Sheffield and Knowsley to increase our distribution capacity rather than to grow our geographic coverage. As a result, spoke fixed costs as a percentage of sales increased, but will reduce as our business scales and the capacity is more fully utilised.

Total administrative expenses excluding depreciation, amortisation and costs recharged to Morrisons increased to £62.1 million, a 13.5% increase from 2013 and 6.9% as a percentage of retail revenue (2013: 7.0%). Some of the cost increases are due to additional technology costs to operate the Morrisons services which are not recharged to Morrisons but for which the Group earns fees, additional payroll costs in technology and non-food and greater share based management incentive costs. Marketing costs excluding voucher spend were £10.0 million (2013: £10.1 million), 1.1% percent of revenue (2013: 1.3%). Despite lower marketing spend, there was an increase in new customer acquisitions.

Total depreciation and amortisation costs were £55.0 million (2013: £43.9 million), an increase of 25.3% year-on-year. This increase includes an impairment charge of £2.6 million (2013: £1.3 million) and higher depreciation and amortisation arising from the increased investment required for the development of CFC1 and CFC2 and includes depreciation on assets effectively owned partially by Morrisons. The impairment charges are due to the write off of certain assets at the White City spoke which is being relocated to Park Royal and due to improvement projects at CFC1 and changes to systems or fulfilment assets to enable the Morrisons operations at CFC2 which result in impairment to existing assets.

SHARE OF RESULT FROM JOINT VENTURE

MHE JVCo Limited ("MHE JV Co") was incorporated in 2013 on the completion of the Morrisons agreement, with Ocado owning a 50% equity interest in this entity. MHE JV Co holds CFC2 assets, which Ocado uses to service its and Morrisons' businesses. During the period the Group sold £23.4 million (2013: £129.2 million) of CFC2 related assets to MHE JV Co, £31.0 million (2013: £113.1 million) of assets were leased back to the Group under a finance transaction. The Group share of MHE JV Co profit after tax in the period amounted to £2.4 million (2013: £0.9 million).

EXCEPTIONAL ITEMS

Exceptional items of £0.3 million (2013: £4.6 million) were incurred in relation to a group restructuring of corporate entities.

	FY 2014 £m	FY 2013 £m	Variance
Central costs – other[1]	**47.1**	42.1	11.9%
Central costs – share based management incentives	**5.0**	2.5	98.1%
Marketing costs (excluding vouchers)	**10.0**	10.1	(1.0)%
Total administrative expenses	**62.1**	54.7	13.5%

1. Excluding chargeable Morrisons costs, depreciation, amortisation and impairment

NET FINANCE COSTS

Net finance costs were £9.1 million (2013: £7.0 million excluding exceptional finance costs of £2.8 million). This increase was attributable to £3.5 million of additional interest from the sale and leaseback arrangements with MHE JV Co, offset by a reduction of £1.9 million of interest costs in 2013 on loans in connection with the construction and fit out of CFC2, which were not incurred in 2014.

PROFIT BEFORE TAX

Profit before tax and exceptional items for the period was £7.5 million (2013: loss of £(5.1) million). Profit before tax for the period was £7.2 million (2013: loss of £(12.5) million).

TAXATION

Due to the availability of capital allowances and Group loss relief, the Group did not pay corporation tax during the year. In the period, the Group has made a claim for energy saving technologies within its existing CFCs under the enhanced capital allowances scheme, resulting in an amount due from HMRC of £0.1 million. No net deferred tax credit was recognised in the period. Ocado has approximately £285.3 million of unutilised carried forward tax losses at the end of the period. During 2014 Ocado paid £29.1 million in a range of taxes including fuel duty, PAYE and Employers' National Insurance, business rates and VAT.

EARNINGS/(LOSS) PER SHARE

Basic earnings per share was 1.24p and diluted earnings per share was 1.18p.

CAPITAL EXPENDITURE AND CASH FLOW

Capital expenditure for the period was £86.4 million (2013: £76.3 million) and comprised of the following:

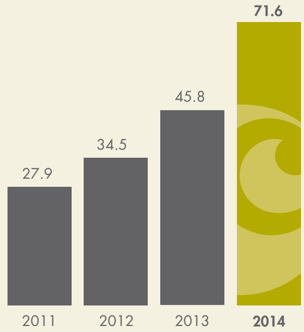
Investment in CFC1 capital expenditure was £9.2 million on resiliency projects (e.g. additional cranes and refurbished zone pick aisles) and improvement projects (e.g. bagging machines). This is at a higher rate compared with 2013 as the switch of some volume to CFC2 during 2014 provided a temporary period of lower utilisation of the CFC1 which gave an opportunity to undertake these capital projects.

In the period a further £1.7 million capital expenditure was incurred for the completion of Phase 1 works and various minor projects in CFC2.

In July 2014, we announced plans for our next CFC located in Andover, Hampshire in the south of England. Andover CFC will be smaller than our existing CFCs (expected capacity of 65,000 OPW), and will include the first example of our proprietary picking system which is designed in the long term to be faster to install and more cost and capital efficient than the system at the current CFCs.

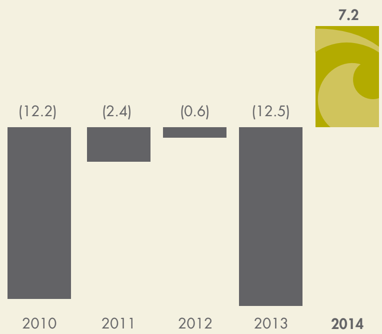
EBITDA (£m)

71.6
2013: 45.8



PROFIT/(LOSS) BEFORE TAX (£m)

7.2
2013: (12.5)



	FY 2014 £m	FY 2013 £m
CFC1	**9.2**	5.9
CFC2	**1.7**	38.0
CFC3	**16.5**	–
Delivery	**22.1**	10.8
Technology	**16.8**	14.1
Other	**20.1**	7.5
Total capital expenditure[1,2] (excluding share of MHE JV Co)	**86.4**	76.3
Total capital expenditure[3] (including share of MHE JV Co)	**98.1**	132.3

1. Capital expenditure includes tangible and intangible assets
2. Capital expenditure excludes assets leased from MHE JV Co under finance lease arrangements
3. Capital expenditure includes Ocado share of the MHE JV Co capex in 2014 of £11.7 million and in 2013 of £56.0 million

CHIEF FINANCIAL OFFICER'S REVIEW continued

"Our technology headcount grew to 550 staff at the end of the period."

"We continue to reinvest our cash for our future growth plans."

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Investment in new vehicles, which are typically on five year financing contracts, was £12.5 million which is higher than the prior year (2013: £9.0 million) to support the business growth. Delivery capital expenditure also included investments for new spokes of £8.5 million, including the purchase of the freehold of a site in Dagenham which opened, after the period end, in January 2015.

Ocado continued to develop its own proprietary software and £14.1 million (2013: £10.4 million) of internal development costs were capitalised as intangible assets in the period, with a further £2.7 million (2013: £3.7 million) spent on computer hardware and software. Our technology headcount grew to 550 staff at the end of the period (2013: 400 staff) as increased investments were made to support our strategic initiatives, including the commencing of a major replatforming exercise of Ocado's technology and migration of most of its systems to run on a public or private cloud. This will allow Ocado to achieve greater technical agility and enable the technology to support possible international expansion opportunities. In addition, we have invested internal technology resources as part of developing the following capital projects: CFC2 Phase 2; next generation of fulfilment solutions; development of the Morrisons proposition; and launch of new destination websites.

Other capital expenditure includes £16.3 million of investment in developing our next generation fulfilment solution, £1.8 million for the second phase of the NFDC to provide further capacity to support our non-food business growth and a further investment of £1.3 million to support the growth of our non-food destination sites and webshop.

At 30 November 2014, capital commitments contracted, but not provided for by the Group, amounted to £22.9 million (1 December 2013: £28.8 million). We expect capital expenditure in 2015 to be approximately £150.0 million, to be invested in the next generation of fulfilment solutions, roll out of our new CFCs and additional investment in new vehicles to support business growth and the replacement of vehicles coming to the end of their five year financing contracts.

During the year the Group generated improved operating cash flow after finance costs of £74.3 million, an increase of 23.0% year-on-year, up from £60.4 million in 2013, as detailed below:

	FY 2014 £m	FY 2013 £m
EBITDA	**71.6**	45.8
Working capital movement[1]	**8.7**	23.5
Exceptional items	**(0.3)**	(4.6)
Other non-cash items[2]	**4.0**	2.8
Finance costs paid[1]	**(9.7)**	(7.1)
Operating cash flow	**74.3**	60.4
Capital investment[1]	**(78.8)**	(77.5)
(Decrease)/Increase in debt/finance obligations[3]	**(33.4)**	34.2
Proceeds from share issues net of transaction costs	**3.7**	3.8
(Decrease)/Increase in cash and cash equivalents	**(34.2)**	20.9

1. FY 2013 capital investment was adjusted for capitalised borrowing costs attributable to an adjustment in working capital and finance costs paid
2. Other non-cash items include movements in provisions, share of income from MHE JV Co and share based payment charges
3. FY 2013 includes sale and leaseback of MHE assets to MHE JV Co

The operating cash flow increased by £13.9 million during the year primarily as a result of an increase in EBITDA of £25.8 million. This was offset by a reduction in positive movement in working capital of £14.8 million driven by a reduction in trade and other payables due to timing of payments for capital projects and the amortisation of a one off payment received in 2013 as part of the Morrisons agreement. In addition trade and other receivables reduced by £6.5 million arising from a capital contribution into MHE JV Co to finance the acquisition of CFC2 fixed assets. Additional funds to finance these CFC MHE fixed assets is received from the payment by Ocado of finance lease obligations owing to MHE JV Co.

We continue to reinvest our cash for future growth and as a result the cash outflow due to capital investment increased to £78.8 million comprising investments in CFC3, development of our next generation fulfilment solution and spend on spoke sites.

In the period £33.4 million of cash was utilised for the repayment of debt and financing obligations. The prior year included the proceeds from the MHE sales and leaseback arrangement entered into as part of the Morrisons agreement.

BALANCE SHEET

The Group had cash and cash equivalents of £76.3 million at the period end (2013: £110.5 million) the decrease mainly owing to a net cash outflow from investing activities and repayments of finance leases in the period.

Gross debt at the period end was £175.7 million (2013: £161.4 million). Gross debt has increased by £14.3 million reflecting an increase in obligations payable to MHE JV Co of £18.1 million offset by a reduction of £3.8m in property mortgages and asset finance obligations.

External gross debt at the period end, excluding the finance leases payable to MHE JV Co, was £44.9 million (2013: £48.7 million).

INCREASING FINANCING FLEXIBILITY

In the period, we put in place a 3 year £100 million unsecured revolving credit facility. The participating banks are Barclays, HSBC, RBS and Santander. We believe this new facility enhances our flexibility to exploit the increasing growth opportunities open to us in the future. The facility remained undrawn throughout the period.

KEY PERFORMANCE INDICATORS

The following table sets out a summary of selected unaudited operating information for 2014 and 2013:

	FY 2014 (unaudited)	FY 2013 (unaudited)	Variance %
Average orders per week	**167,000**	143,000	16.8%
Average order size (£)[1]	**112.25**	113.53	(1.1)%
Mature CFC efficiency (units per hour)[2]	**145**	135	7.4%
Average deliveries per van per week (DPV/week)	**163**	160	1.9%
Average product wastage (% of revenue)[3]	**0.8**	1.0	(0.2)%
Items delivered exactly as ordered (%)[4]	**99.3**	99.0	0.3%
Deliveries on time or early (%)	**95.3**	95.2	0.1%

Source: the information in the table above is derived from information extracted from internal financial and operating reporting systems and is unaudited.

1. Average retail value of goods a customer receives (including VAT and delivery charge and including standalone orders) per order
2. Measured as units dispatched from the CFC per variable hour worked by CFC1 and CFC2 operational personnel in 2014. We consider a CFC to be mature if it had been open 12 months by the start of the half year reporting period
3. Value of products purged for having passed Ocado's "use by" life guarantee divided by retail revenue
4. Percentage of all items delivered exactly as ordered, i.e. the percentage of items neither missing nor substituted

Which?

Best Online Grocer 2014
Members Annual Satisfaction Survey
Best Online Grocer 2013
Members Annual Satisfaction Survey

Loved By Parents

Best Online Retailer 2014
Best Grocery Product 2014
Best Child's Snack 2014

Website of the Year

Best Shopping Website

Soil Association

Best Organic Supermarket 2014

Health and Fitness, and Women's Fitness

Best Retailer 2015 — Gold
Healthy Snack Boxes 2015, Ocado
Organic Fruit Box — Gold
Organic Food 2015, Ocado Organic
Small Veg Box — Gold

Foods You Can

Best Large Online Supermarket 2014

OUR AWARDS 2014

CONSUMER AWARDS 2014

During 2014 we were delighted to be recognised for our achievements, a number of which are highlighted below.

Ocado was voted Best Online Grocer by Which? Magazine (Members Annual Satisfaction Survey) and Best Online Retailer (Gold). We also received recognition as Best Large Online Supermarket 2014 in the Foods You Can, Free From People's Choice Golden Apple Awards, for our extensive offering in our Free From Range.

We were also voted by more than 11,000 consumers as the Best Organic Supermarket 2014 in the 28th annual Soil Association Awards. Our webshop offers over 2,800 organic products available for delivery to customers in the UK. Our rapidly growing range of organic groceries, toiletries, beauty and baby products, pet food and household goods are available at the touch of a button at Ocado.com/organic.

We also won a number of awards for our Ocado own-label products. These included the Loved by Parents Best Grocery Product for our Ocado own-label organic juicing boxes, fruit boxes and vegetable and salad boxes, as well as for a range of our fresh fish by Quality Food Awards.

The annual Britain's Next Top Supplier campaign was acclaimed in the PRCA Awards, which showcase the best in the PR industry as judged by leaders in the field. We also secured the Corporate Social Responsibility accolade, which recognises work that promotes an organisation's CSR programme, via either a one-off campaign or ongoing work.

BRAKE FLEET SAFETY AWARDS 2014

Ocado fleet trainers and Service Delivery Team were awarded the Company Driver Safety Award (medium fleet) for fleet safety by BRAKE. This highly regarded award, recognises the high standards delivered each day by our fleet of drivers.

Neil Shaw, Head of Training and Development — Service Delivery, was also recognised as Road Risk Manager of the Year for his commitment to delivering a programme which has enabled Ocado to lead the way in fleet safety amongst our peers.

2014 BUILDING PUBLIC TRUST AWARDS

Ocado won the award for "Corporate Governance Reporting in the FTSE 250" at the 2014 Building Public Trust Awards, in respect of the Annual Report for 2013. This award highlights the Group's efforts in developing a strong framework of governance and risk management and continued excellence in its reporting to shareholders.

APPRENTICE OF THE YEAR 2014

Ryan Scales was voted Apprentice of the Year by the '3aaa Academy' beating 12,000 apprentices to take the title. Ryan was one of 25 people to be nominated, put forward by employers and staff from the 3aaa Academies across England, for their hard work and dedication throughout the year.

View more information about the Apprentice of the Year on page 56

View more information online at www.ocadogroup.com