Pennon

25 November 2016

Half Year Results 2016/17
for the period ended 30 September 2016

Building Momentum, Driving Growth

Chris Loughlin, Pennon Chief Executive said:

"Pennon has delivered a good performance in the first half of 2016/17 across its water and waste businesses. South West Water continues to achieve a sector-leading RORE(1) at 11.7% as it outperforms for its customers, and is expecting momentum and delivery to continue. Viridor is on track to contribute the targeted c.£100 million of EBITDA from its ERF(2) portfolio this year while self-help measures are driving improved EBITDA margins in recycling.

We are continuing to invest for growth. Following a review, we have taken the decision to commit to a £252 million ERF at Avonmouth, expanding our portfolio to twelve plants. This is a significant investment in the UK's environmental infrastructure and will add to the already expected significant increase in EBITDA from our ERF portfolio once all facilities are fully operational. In water, we are announcing a new retail venture for business customers with South Staffs/Cambridge Water.

We remain focused on driving value through efficiency. South West Water has delivered £80 million of Totex savings since the beginning of K6 (2015-2020), while our recently completed Shared Services Review will increase total Group cost savings from the c.£11 million previously announced to c.£17 million p.a from 2019.

We believe Pennon is well positioned for the future and is on track to meet management expectations for the full year 2016/17. Our performance underpins our sector-leading dividend policy of 4% growth per annum above RPI inflation to 2020."

[1] Return on Regulated Equity (RORE)
[2] Energy Recovery Facility (ERF)

Financial Highlights

Underlying[3]	H1 2016/17	H1 2015/16	Change
Revenue	£685.5m	£689.1m	(0.5%)
EBITDA	£245.4m	£231.7m	+5.9%
Adjusted EBITDA[4]	£277.2m	£261.6m	+6.0%
Operating Profit	£153.9m	£135.3m	+13.7%
Profit Before Tax	£128.1m	£106.8m	+19.9%
Tax	(£30.7m)	(£21.9m)	+40.2%
Earnings per share[5]	23.6p	23.2p	+1.7%
Dividend per share[6]	11.09p	10.46p	+6.0%

Underlying Profit After Tax (PAT) to Statutory PAT

Underlying PAT	£97.4m	£84.9m	+14.7%
Non-underlying Items (Profit After Tax)	(£8.3m)	-	-
PAT (attributable to holders of hybrid capital)	(£16.2m)	(£16.2m)	-
PAT (attributable to shareholders)	£72.9m	£68.7m	+6.1%

- Underlying earnings are presented to provide a more useful comparison on business trends and performance. Non-underlying items are adjusted for by virtue of their size, nature or incidence to enable a full understanding of the Group's financial performance
- Underlying operating profit and PBT up +13.7% and +19.9% respectively following higher revenues and cost savings at South West Water and growth at Viridor driven by the Energy Recovery Facilities (ERFs) and recycling 'self-help' initiatives, net of an expected decline in landfill activities
- Return on Regulated Equity at 11.7%, unique WaterShare mechanism benefiting customers
- Sustainable, low cost funding position underpinning continuing capital investment
- Interim dividend per share +6.0% to 11.09p
- On track to meet management expectations for the full year 2016/17

[3] Before non-underlying items
[4] Statutory EBITDA plus share of Joint Venture EBITDA and IFRIC 12 interest receivable
[5] Before deferred tax and adjusted proportionately to reflect the half year impact of the annual hybrid periodic return. Basic earnings per share (statutory basis) 17.7p
[6] The RPI rate used is 2.0% as of September 2016

Operational Highlights

- Water business outperforming the regulatory contract, on track to deliver a net ODI reward for 2016/17, and a cumulative net ODI reward for the performance to date[(7)]
- Eight operational ERFs performing well, focus on increasing average availability, expected to be c.90% for 2016/17
    - Construction of three further ERFs ongoing – Dunbar and South London (Beddington) progressing to budget
    - Commissioning has commenced at parts of Glasgow's Recycling and Renewable Energy Centre, though contractor delays mean takeover of the centre is now expected in 2017. The project will now be completed by an experienced team assembled by Viridor with contractual remedies supporting completion
- c.80%[(8)] of existing ERF portfolio volumes (and associated price) contracted long-term
- Recycling 'self-help' measures driving increased EBITDA, commodity risk sharing with clients
- Driving value through efficiency - integrating, sharing best practice, reducing costs through a Shared Service Review
- Secured further growth opportunities
    - New non-household retail venture with South Staffs / Cambridge Water
    - Committed to 12th ERF at Avonmouth - expected to be completed in 2020/21
    - Over 50% of inputs to Avonmouth are already agreed

Presentation of Results

A presentation for City audiences will be held today, Friday 25 November 2016, at 10am at the London Stock Exchange, 10 Paternoster Square, London, EC4M 7LS.

A live videocast of the presentation can also be accessed using the following link:

www.pennon-group.co.uk/investor-information

For further information, please contact:

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[7] £3.8m net cumulative reward reflecting £5.7m net reward which will be recognised at the end of the regulatory period and £1.9m net penalty which can be reflected during the regulatory period
[8] Excluding Avonmouth

About Pennon Group

As one of the largest environmental infrastructure groups in the UK, Pennon is at the top end of the FTSE 250. Pennon has assets of around £5.8 billion and a workforce of around 5,000 people.

The merged water company of South West Water and Bournemouth Water provides water and wastewater services to a population of c.1.7 million in Cornwall, Devon and parts of Dorset and Somerset and water only services to c.0.5 million in parts of Dorset, Hampshire and Wiltshire. South West Water was awarded enhanced status for its 2015-2020 Business Plan, and has the highest potential returns in the water sector.

Viridor is a leading UK recycling, energy recovery and waste management company, providing services to more than 150 local authorities and major corporate clients as well as over 32,000 customers across the UK.

Pennon currently has a sector leading dividend policy of 4% year-on-year growth above RPI inflation to 2020. This is underpinned by the highest potential Return on Regulated Equity in the water sector over K6 (2015-2020) and the growth in earnings being delivered by Viridor's ERFs.

Upcoming Events

9 February 2017	Trading Statement
24 May 2017	Full Year Results 2016/17
6 July 2017	Annual General Meeting
September 2017	Trading Statement
29 November 2017	Half Year Results 2017/18

Interim Dividend Payment Information:

2 February 2017	Ex-dividend date
3 February 2017	Record date
13 March 2017	Scrip election date
4 April 2017	Payment date

PENNON BUSINESS REVIEW

Pennon's priority continues to be the creation of shareholder value through its focus on UK environmental infrastructure across water and waste sectors.

The Group has performed robustly in H1 2016/17, and results for the full year 2016/17 are on track to meet management expectations. Pennon generates significant operating cash flows, and has a strong liquidity and balance sheet position.

Pennon continues to seek and identify further growth opportunities within the UK, assessing the long-term viability of the market and achieving an appropriate risk/reward balance. Pennon has now committed to a further ERF at Avonmouth near Bristol, taking the portfolio to twelve ERFs and is a significant infrastructure investment post-Brexit. Pennon is also announcing a new retail venture for business customers with South Staffs/Cambridge Water.

Strong water and waste businesses

The merged water business of South West Water and Bournemouth Water is well-prepared to take opportunities in a changing regulatory environment, looking at options for future consolidation and growth while continuing to deliver and outperform the business plans. South West Water's RORE has been 11.7% since the start of the regulatory period and is expected to continue to be at a sector-leading level through to 2020.

Viridor's ERF portfolio is performing well and is on track to deliver c.£100 million of EBITDA in 2016/17. We expect demand for ERFs to continue to exceed capacity into the long term. With four ERFs now under construction or committed we will generate significant growth in EBITDA over the next few years as the plants come on stream. The focus for the ERF portfolio remains on increasing the operational performance with average availability now expected to reach c.90% in 2016/17.

Recycling 'self-help' measures are supporting an increasing EBITDA, with the market shift to sharing commodity risk/opportunity with customers improving the dynamics of the contracts. Good progress has been made in contract renegotiations to date with a further opportunity as over half of contracts are still to review on renewal. The focus on reducing costs and simplifying the organisation is also contributing to the improved performance. We expect further opportunities to increase returns through improving asset utilisation and rationalising the portfolio.

Cost efficiency a continued focus

South West Water continues to strive for ever greater efficiency, with Totex outperformance resulting in cumulative savings of £80 million and financing outperformance of £48 million in the first eighteen months of K6 (2015-2020). South West Water is focused on maintaining this momentum over the full K6 regulatory period and is confident in its ability to remain at the frontier of cost efficiency for the water sector.

South West Water is targeting c.£27 million of net synergies over K6 following the integration of Bournemouth Water. Support functions and operational structures have been aligned across the regions.

Pennon has also focused on cost savings across the group, with the c.£11 million of cost savings and synergy plans announced last year now increased to c.£17 million p.a. from 2019 following the successful conclusion of the Shared Services Review. The review has resulted in the planned centralisation of key corporate services and operational functions, including Corporate Affairs and Communications, Facilities, Finance, HR, Information Services, Logistics, Procurement and SHEQ[9]. Combining these activities is expected to create annual savings of c.£6 million. As a result of this review a restructuring provision of £1.2 million has been provided and an asset value of £9.5 million has been de-recognised, relating to a Viridor IT system which will no longer be used as the Group standardises its processes and systems.

Driving growth

Avonmouth ERF Committed

In line with Pennon's growth ambitions, the Board has made the decision to commit to a further £252 million ERF at Avonmouth near Bristol to be completed in 2020/21, taking the portfolio to twelve plants. Once completed, the plant will have a capacity of 320,000 tonnes per annum and will deliver 33MW of electricity which equates to c.260,000MWh per year. Viridor is confident in filling capacity on opening with over 50% of fuel already agreed. This includes c.35% of total capacity secured through a long term contract for the life of the plant with Somerset Waste Partnership which is in the final stages of negotiation. There are further contracts in the pipeline, in addition to our own collections fleet and strong regional commercial and industrial (C&I) demand. This project will be completed by an experienced construction and consulting team.

[9] Safety, Health, Environment and Quality

Combustible waste market under-capacity in the West of England matches the UK trend, stretching out to 2030 and beyond. Viridor is confident of its market projections, which are also supported by independent third party analysis. The waste arisings in the area surrounding Avonmouth ERF substantially exceed the plant's capacity and available capacity in neighbouring facilities. In addition to the contracts already secured, a further c.800,000 tonnes is available in the area surrounding the ERF from a combination of municipal and commercial & industrial sources. Avonmouth ERF will offer a cost effective solution relative to other disposal methods and is well placed to secure the waste tonnages to fill the plant at competitive prices.

New non-household retail venture with South Staffs/Cambridge Water

Pennon Water Services, the separate legal entity operated from Bournemouth providing retail services for our existing non-household retail brands, along with South West Water's wholesale operations successfully entered the shadow market on 3 October 2016.

A key part of our non-household strategy has been to retain our existing customer base of c.85,000 customers and to capitalise on Viridor's national footprint, its commercial culture, order book, expertise and existing customer relationships.

Pennon has always recognised the need to achieve scale in order to compete within this market and as a result a new retail non-household venture arrangement with South Staffordshire Plc Group (incorporating South Staffs and Cambridge Water) has been agreed, with Pennon retaining an 80% share and the operations being merged in Bournemouth. The activities will be merged from April 2017[(10)] and will benefit from strong customer service and a common IS platform which will continue to be supported by the South Staffordshire Group.

The combined business will have c.£170 million of revenue, c.8% of the non-household retail market share and is expected to be the 4th largest retailer.

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[10]Subject to competition clearance

Well prepared for regulatory and market developments

Engaged in Water 2020

South West Water is fully engaged in Water 2020 as we prepare and position ourselves for PR19. The company is in a very good position to anticipate and influence future regulatory reforms and is working hard to play its part in shaping the future of the industry, including engagement with Ofwat's process for licence changes.

The debt consultation which Ofwat published in October 2016 confirmed a number of areas already expected and South West Water led the way at the last price review in adopting our pain/gain mechanism WaterShare which already shares benefits with customers. In addition, South West Water has always strived to remain efficiently financed and is comparable with the notional structures and gearing levels set by Ofwat.

The changes in approach to indexation along with the expected market reforms within the water resources and bio-resources (sludge) areas were previously signalled and the impact on South West Water's Regulatory Capital Value (RCV) is relatively less at c.4% and c.2% respectively of RCV currently included within these areas.

South West Water continues to deliver its operations and capital schemes effectively and with our strong strategic alliances and innovative planning and scoping techniques we see opportunities within the direct procurement proposals.

Household Retail competition

South West Water was fully engaged with Ofwat, helping in their assessment of costs and benefits through customer research and the Water UK "Market Place for Ideas".

The government is expected to make a decision in late 2016 and this will influence the Water 2020 approach to retail.

Pennon

PENNON FINANCIAL PERFORMANCE

Pennon Group

Underlying[11]	**H1 2016/17**	**H1 2015/16**	**Change**
Revenue	£685.5m	£689.1m	(0.5%)
EBITDA	£245.4m	£231.7m	+5.9%
Adjusted EBITDA[12]	£277.2m	£261.6m	+6.0%
Operating Profit	£153.9m	£135.3m	+13.7%
Profit Before Tax	£128.1m	£106.8m	+19.9%
Tax	(£30.7m)	(£21.9m)	+40.2%
Capital investment[13]	£183.3m	£165.9m	+10.5%
South West Water	£79.7m	£58.0m	+37.4%
Viridor	£103.6m	£107.9m	(4.0%)
Earnings per share[14]	23.6p	23.2p	+1.7%
Dividend per share[15]	11.09p	10.46p	+6.0%
	30 September 2016	**31March 2016**	**Change**
Net debt	£2,566.1m	£2,484.4m	+3.3%

South West Water

	H1 2016/17	**H1 2015/16**	**Change**
Revenue	£287.9m	£279.3m	+3.1%
EBITDA[11]	£183.0m	£173.6m	+5.4%
Operating Profit[11]	£127.2m	£117.7m	+8.1%
Profit Before Tax[11]	£97.0m	£87.0m	+11.5%

11 Before non-underlying items
12 Statutory EBITDA plus share of Joint Venture EBITDA and IFRIC 12 interest receivable
13 Including construction spend on service concession arrangements
14 Before deferred tax and adjusted proportionately to reflect the half year impact of the annual hybrid periodic return. Basic earnings per share (statutory basis) 17.7p
15 The RPI rate used is 2.0% as of September 2016

Viridor

	H1 2016/17	H1 2015/16	Change
Revenue[16]	£397.9m	£410.1m	(3.0%)
EBITDA[17]	£63.3m	£61.0m	+3.8%
ERFs	£50.5m	£43.8m	+15.3%
Landfill	£3.2m	£4.5m	(28.9%)
Landfill Gas	£12.9m	£16.0m	(19.4%)
Recycling	£11.0m	£7.2m	+52.8%
Contracts, Collections & Other	£16.0m	£20.1m	(20.4%)
Indirect Costs	(£30.3m)	(£30.6m)	(1.0%)
Share of JV EBITDA	£23.0m	£21.6m	+6.5%
IFRIC 12 Interest Receivable	£8.8m	£8.3m	+6.0%
Adjusted EBITDA[17]	£95.1m	£90.9m	+4.6%
Profit Before Tax[17]	£23.1m	£12.9m	+79.1%

Underlying performance ahead of last year and in-line with management expectations

Group revenue was broadly in line with last half year at £685.5 million. Revenue from the water business was up by 3.1% to £287.9 million as a result of 1.3% higher demand, tariff increases of 1.4% (with RPI of 1.1%) and increased new connections but is within regulatory tolerances for revenue controls. Viridor's revenue decreased by 3.0% to £397.9 million due to the expected decrease in construction spend on service concession arrangements as plants come on stream and lower landfill volumes, partly offset by the growing contribution of operational ERFs. Excluding the impact of construction revenue, Group revenue would have increased in the period.

Group EBITDA and adjusted EBITDA were ahead of H1 2015/16 up 5.9% at £245.4 million (H1 2015/16 £231.7 million) and 6.0% to £277.2 million (H1 2015/16 £261.6 million) respectively. Operating profit increased by 13.7% to £153.9 million (H1 2015/16 £135.3 million) and profit before tax increased by 19.9% to £128.1 million (H1 2015/16 £106.8 million). This has been achieved through an increase in profits from Viridor, together with continuing strong South West Water financial performance and efficient ongoing finance costs across the Group.

Following the merger of Bournemouth Water into South West Water the water business recorded strong performances against the K6 regulatory contracts, outperforming regulatory assumptions. The water business' underlying profit before tax increased by £10.0 million, or 11.5%, to £97.0 million (H1 2015/16 £87.0 million) reflecting tariff increases, increased demand of 1.3% and a reduction in operating costs of £0.8 million, or 0.8%, to £104.9 million (H1 2015/16 £105.7 million).

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16 Including landfill tax and construction spend on service concession arrangements
17 Before non-underlying items

With the highest potential returns in the sector for K6, South West Water is outperforming its business plan, resulting in a cumulative return on regulated equity of 11.7%[18].

South West Water's EBITDA increased during the period due to higher revenue and cost efficiencies along with other cost reductions. While average RPI has been increasing (2.0% as at September 2016), total operating costs in H1 2016/17 fell compared to the same period last year, with savings arising from operational maintenance, synergies from the company mergers as well as targeted efficiencies contributing to cost performance. In addition, South West Water's bad debt charge continues to fall, down by over a quarter since the end of K5, to 1.1% as a percentage of revenues (1.7% at the end of K5). This was driven by strong collections as we work with our customers to manage their debt with the operations continually updating their approaches in targeting those customers with the means to pay whilst supporting those who have genuine affordability challenges.

At Viridor, the portfolio of operational ERFs continues to perform well, with the six most recently delivered ERFs ramping up as Viridor optimises each plant. As a result, Viridor's EBITDA increased by 3.8% to £63.3 million (H1 2015/16 £61.0 million) whilst H1 2016/17 adjusted EBITDA increased 4.6% to £95.1 million (H1 2015/16 £90.9 million). Viridor has three further ERFs under construction. Dunbar and Beddington (South London) are progressing well and to budget with steps being taken to ensure construction of Glasgow ERF is completed successfully.

Viridor's EBITDA was ahead of last half year due to the ramping up of the existing ERF portfolio and recycling self-help measures, where significant progress has been made in reducing the cost base and improving the utilisation of assets, net of anticipated declines in landfill earnings primarily due to expected lower volumes. Our ERF activities delivered EBITDA of £50.5 million (H1 2015/16 £43.8 million), a significant increase compared to H1 2015/16. We remain on track to deliver our target of c.£100 million of EBITDA from ERFs by 2016/17 (before IFRIC 12 interest receivable and our share of joint venture EBITDA). Joint venture EBITDA increased to £23.0 million (H1 2015/16 £21.6 million) due to continuing strong EBITDA from Lakeside and higher EBITDA from Runcorn I reflecting improved operational performance. This resulted in a share of joint venture profit after tax of £2.8 million (H1 2015/16 £1.0 million).

Recycling and resources EBITDA, comprising recycling, collection and contracts and other, was broadly in line with last half year at £27.0 million (H1 2015/16 £27.3 million), despite lower profits from asset sales, which has been offset by higher recycling EBITDA. Recycling revenue at £87 per tonne (recyclate sales plus gate fees) (H1 2015/16 £87 per tonne) is in line with last half year.

[18] RORE reflects the Ofwat regulatory guidance of Base RORE plus Outperformance. It is calculated using actual results before non-underlying items (deflated into 2012/13 prices) and compared against the Final Determination allowances sourced from Ofwat published models and based on notional gearing and annual average RCV.

Average costs fell by £5 per tonne to £74 per tonne (H1 2015/16 £79 per tonne) as a result of self-help measures including the Input, Throughput and Output Optimisation (ITOO) programme, and therefore the recycling EBITDA margin increased by £5 per tonne to £13 per tonne (H1 2015/16 £8 per tonne). Although the short term outlook for recyclate prices is relatively stable, we remain cautious about future recyclate price growth and are not relying on a near term recovery. We are instead focusing on 'self-help' measures to drive margin improvement and to look to share commodity risk/ opportunity with our clients.

Landfill earnings from waste disposal and power generation are down compared to last half year by £1.3 million and £3.1 million respectively. The decrease in earnings is primarily due to expected lower volumes, which are in line with management expectations, and lower power prices.

Interest

Underlying net finance costs of £28.6 million were £0.9 million lower than last half year, predominantly reflecting higher capitalised interest due to continuing ERF capital investment, in addition to lower average net borrowing rates.

We have secured funding at a cost that is efficient and effective. The Group interest rate on average net debt for H1 2016/17 has reduced to 3.3% (H1 2015/16 3.4%).

Tax

The Group's underlying mainstream UK corporation current tax charge for the half year (before prior year) was £23.1 million, reflecting an effective tax rate of 18.0% (H1 2015/16 £18.5 million, 17.3%); the increase is primarily driven by higher profits. There was a prior year credit of £0.3 million recognised for the half year (H1 2015/16 credit of £14.7 million). The larger credit in the prior period of £14.7 million reflects the clarification of uncertain tax positions, which resulted in a lower tax charge than the original assessment. In addition there is a non-underlying £1.3m current tax credit relating to non-underlying items.

Underlying deferred tax for the half year (before prior year) was a charge of £9.5 million (H1 2015/16 £6.4 million). The charge for H1 2016/17 primarily reflects capital allowances, including on ERFs, in excess of depreciation charge. There was a prior year deferred tax credit of £1.6 million recognised for the half year (H1 2015/16 £11.7 million charge) reflecting the impact of the clarification of uncertain tax items. In addition there is a non-underlying £20.1 million deferred tax credit relating to the enacted reduction in the UK rate of corporation tax to 17% in 2020 and a £4.0 million deferred tax charge relating to other non-underlying items.

This resulted in a total tax charge for the half year of £13.3 million (H1 2015/16 £21.9 million).

Underlying profit before tax growth from previous half year

Underlying profit before tax was £128.1 million, an increase of 19.9%, compared with the prior half year (H1 2015/16 £106.8 million). On a statutory basis, profit before tax was £102.4 million (H1 2015/16 £106.8 million) reflecting non-underlying charges of £25.7 million.

Earnings per share before deferred tax, non-underlying items and adjusted proportionately to reflect the half year impact of the annual hybrid periodic return, was comparable with the prior half year, up 1.7% to 23.6p (H1 2015/16 23.2p). The impact from higher underlying group profits before tax is largely offset by higher corporation tax charges, with last half year's charge including a £14.7million prior year credit (H1 2016/17 £0.5 million charge).

The interim dividend of 11.09p per share reflects an increase of 6.0%[(19)], in line with our dividend policy of RPI +4%. This will see dividends per share almost doubling over 10 years to 2020.

The dividend will be paid on 4 April 2017 to shareholders on the register on 3 February 2017. The Company is also offering a scrip dividend alternative. The final date for receipt of Forms of Election Mandate in respect of the scrip dividend alternative for the interim dividend will be 13 March 2017.

Non-underlying Items

Net non-underlying items totalling a charge after tax of £8.3 million have been recognised (H1 2015/16 £nil). The net charge is a result of:

- restructuring costs - £10.7 million charge relating to restructuring costs from the Group wide Shared Services Review and migration to a Group IT platform (including a £9.5m non-cash de-recognition of an existing IT asset)
- taxation - £17.4 million credit predominantly arising from the enacted reduction in the UK rate of corporation tax from 18% to 17% in 2020.
- derivative movements - £15.0[(20)] million charge reflecting non-cash movements as a result of a change in legislation and market movements on our long-dated floating rate vanilla swaps

The vanilla floating rate swaps are held over South West Water's long-term 2040 Bond and as market rates have fallen the value of the derivative asset has increased, offset by;

A derivative entered into in 2011 designed to improve the Group's overall interest rate performance (c.£8m p.a. benefit, cash settled).

[19] The RPI rate used is 2.0% as of September 2016
[20] Two arrangements are accounted for in non-underlying derivative movements

This derivative arises from a combination of non-derivative instruments; included in the instrument is a £200m floating interest rate-linked loan from Peninsula MB Ltd to Pennon and a fixed rate £200m obligation to Pennon from Peninsula MB Ltd. In combination this arrangement is targeted at providing an index-linked[(21)] return.

Whilst Peninsula MB Ltd is not consolidated for accounting purposes, it does fall within Pennon's corporation tax group. Following a change in legislation, the fair value of the derivative at H1 2016/17 results in a liability recognised in Pennon of £39.5m (H1 2015/16 asset £0.6m).

Pennon has the ongoing option to transfer the financial instrument from Nomura to Pennon on which interest payments are owed by Peninsula MB Ltd and acquire 100% controlling interest in Peninsula MB. At this point all balances relating to this arrangement would be within Pennon Group.

Through the fair value recognition of the instruments and appropriate tax provisioning, financial exposure to Pennon of this arrangement is minimised.

Strong funding position underpinning capital investment

The Group has a strong liquidity and funding position with £1,603 million cash and facilities at 30 September 2016. This includes cash and deposits of £658 million (including £219 million of restricted funds representing deposits with lessors against lease obligations) and undrawn facilities of £945 million. At 30 September 2016 the Group's loans and finance lease obligations totalled £3,224 million.

During the first six months of the 2016/17 accounting period the Group has drawn the South West Water EIB funding of £130 million signed H1 2015/16.

Following the Press release in March 2016 after a visit to Cardiff's Trident Park Energy Recovery Facility the EIB confirmed its intention to provide funding to Viridor for its ERF programme, we can confirm that the final documentation has now been agreed for the £110m loan to Pennon Group Plc. The funding provides support to Viridor's ERF Programme by the way of long term financing which matches the profile of the project's cash flows.

Following the signing of the contract we are also looking to continue our strong relationship with the EIB with negotiations already underway to secure additional funding for South West Water. The investment in Avonmouth ERF will be corporately financed and options are being considered, including a new hybrid, to continue the Group's diversified funding position.

[21] Proprietary Nomura Index

Net debt position

The Group's net debt has increased by £82 million to £2,566 million, with the increase reflecting significant capital investment. The Group's gearing ratio at 30 September 2016, being the ratio of net debt to (equity plus net debt) was 65.3% (31 March 2016 62.5%), reflecting continuing capital investment, advancement of the 2015/16 final dividend and the increase in the pension accounting deficit.

The combined South West Water and Bournemouth Water debt to RCV[(22)] ratio is 62.2% (31 March 2016 59.7%), which aligns with Ofwat's K6 target for efficient gearing of 62.5%.

Group net debt includes £1,055 million of investment in wholly-owned ERFs (Runcorn II, Oxford, Exeter, Cardiff, Glasgow, Dunbar and South London) and £82 million of funding for investments in joint ventures through shareholder loans (which together represents 44% of Group net debt). In addition the joint ventures have non-recourse net debt from third parties (excluding shareholder loans) of which Pennon's share is £200 million. c.85% of ERF and joint venture funding is from corporate finance.

Strong cash inflow from operations, reflecting continuing investment

The Group's operational cash inflows in H1 2016/17 were up £39 million to £258 million (H1 2015/16 £219 million) including the benefit of higher earnings. These funds have been put to use in efficiently financing the Group's capital structure and investing in future growth, through our substantial continuing capital investment programme. This investment has resulted in higher Group net debt.

The total value of dividends paid in H1 2016/17 is higher than the prior half year which reflects the payment of both the 2015/16 interim and final dividend due to the advancement of the 2015/16 final results and Annual General Meeting. In addition, during the period the Company continued to benefit from offering a scrip dividend alternative. £6.9 million of potential cash dividend was retained in the business (H1 2015/16 £6.3 million) and resulted in issuing 771,563 shares.

Efficient long-term financing strategy

The Group has a diversified funding mix of fixed, floating and index-linked borrowings. The Group's debt has a maturity of up to 41 years with a weighted average maturity of 21 years matching the asset base. Much of the Group's debt is floating rate and derivatives are used to fix the rate on that debt. The Group has fixed, or put swaps in place to fix, the interest rate on a substantial portion of

[22] Based on RCV at March 2017 assuming RPI of 2.5%

the existing water business debt for the entire K6 period, in line with the Group's policy to have hedging in place before the start of a regulatory period.

£486.3 million of South West Water's debt is index-linked at an overall real rate under 2.0%. As a result of the aforementioned initiatives, South West Water's cost of finance is among the lowest in the industry. Two thirds of the water business debt is finance leases giving a long maturity profile. Interest payable benefits from the fixed credit margins, which were secured at the inception of each lease. Bournemouth Water was successfully integrated into South West Water on 1 April 2016 and as a result a quarter of the gross funding for the water business is RPI linked consistent with Ofwat's notional level.

The Group's interest rate on average net debt for the period to 30 September 2016 is 3.3% (after adjusting for capitalised interest of £6.1 million, notional interest items totalling £3.1 million and interest received from shareholder loans to joint ventures of £5.0 million). For South West Water this figure was 3.2%.

During the period underlying net finance costs (excluding pensions net interest, discount unwind on provisions and IFRIC 12 contract interest receivable) were £31.7 million (H1 2015/16 £30.8 million), covered 4.9 times (H1 2015/16 4.4 times) by Group operating profit.

Capital investment focused on regulatory expenditure and ERF build out

Group capital investment[(23)] was £183.3 million in H1 2016/17 compared to £165.9 million in H1 2015/16.

South West Water's capital expenditure was £79.7 million compared to £58.0 million in H1 2015/16. The beginning of the new regulatory period reflects a change in the nature and extent of capital activity and an increase in activity in year 2.

As anticipated the largest single project for South West Water's spending is the development of the innovative Mayflower water treatment works at North Plymouth. Construction works are well advanced and the formation of the process elements is underway with over 5km water pipeline and effluent pipes already installed. Advanced techniques have been used to limit the impact on the surrounding area including micro tunnelling under a major road into Plymouth. In addition investment has been targeted to improve wastewater compliance with process upgrades and improvements at 6 sites.

[23] Including construction spend on service concession arrangements and £6.1 million of capitalised interest

Viridor's capital investment of £103.6 million was broadly in line with H1 2015/16 (£107.9 million). The majority of expenditure this period reflects the ongoing ERF programme, with significant expenditure at South London, Dunbar and Glasgow ERFs.

The infrastructure at Dunbar is nearing completion with a significant element of the process plant having been delivered to site prior to installation. The plant is expected to be operational in H2 2017/18. Construction at Beddington is progressing to plan with access routes to the site being improved and the core infrastructure under construction. Operations are expected to commence in H1 2018/19.

Whilst contractor delays and underperformance are delaying the full completion of Glasgow ERF, commissioning of parts of the facility have begun and the project will now be completed by an experienced team assembled by Viridor.

Pensions

The Group operates defined benefit pension schemes for certain employees of Pennon Group. The main schemes were closed to new entrants on or before 1 April 2008.

At 30 September 2016 the Group's pension schemes showed an aggregate deficit (before deferred tax) of £115.6 million (March 2016 £40.9 million). The deficit has increased due to the post-Brexit fall in bond yields, increasing the valuation of liabilities. However, over half of the increase in the valuation of liabilities has been offset by increases in asset values.

The net aggregate liabilities of £93 million (after deferred tax) represented around 3% of the Group's market capitalisation at 30 September 2016.

The 31 March 2016 actuarial valuation of the main scheme is currently underway, and our expectations are that the outcome will not be materially different than expected at the 2013 valuation and contributions are currently in line with Final Determination (FD) allowances.

OPERATIONAL PERFORMANCE

Pennon – evolving for the future

Driving benefits from a combined group

Pennon is focused on driving greater synergies and savings across the Group, sharing best practice and ensuring it is well placed to capitalise on emerging opportunities.

As part of the evolution in Pennon's structure, a Shared Services Review was undertaken and has resulted in the centralisation of a number of corporate functions including corporate affairs and communications, human resources, finance, information services and SHEQ[(24)], as well as operational functions including procurement, logistics and facilities. This will result in a cost saving of c.£6.0 million per annum from 2019. In addition, Pennon is targeting savings through a group-wide procurement approach.

Both Viridor and South West Water have a breadth and depth of experience in managing large asset bases and in using engineering excellence, technology and innovation to deliver efficiency and effectiveness. By sharing knowledge across the Group and harnessing our combined skills we can provide even better services to our extensive customer base of local authorities, major corporate clients, businesses and household customers.

For example, through the Group's portfolio management approach to energy hedging, Pennon now has the ability to hedge its market position for periods up to five years ahead, further helping to protect revenues.

c.90% of energy (generation net of internal usage of electricity) is hedged for 2016/17 and over 60% is hedged out to 2019/20. Pennon's hedging was largely completed in H2 2015/16, with further trading in early H1 2016/17. In addition, the Group has a natural hedging opportunity which represents one third of Viridor's energy generation, as South West Water is a net user of electricity.

Good operational and financial performance in Water

We are focused on providing water and wastewater services in the most efficient and sustainable way possible. Innovation, new technologies, and the pioneering of a holistic approach to water and wastewater management are playing a key role in delivering service improvements and long-term value.

[24] Safety, health, environment and quality

Outperforming our Final Determination Return on Regulated Equity (RORE) range

South West Water has continued the momentum in delivering outperformance and has confidence in our ability to deliver outperformance throughout the 2015-20 (K6) regulatory period. As a result of our targeted approach to efficiency South West Water has delivered a cumulative indicative annual equivalent Return on Regulated Equity (RORE)[25] of 11.7% arising from base, financing and operational returns. Of the 11.7%, 6.0% is the base return, 2.3%[26] reflects Totex savings and efficiencies, 0.3% reflects a net reward on Outcome Delivery Incentives (ODIs) and 3.1%[27] reflects the difference between actual and assumed financing costs.

Totex - securing outperformance

South West Water is striving for ever greater efficiency and is confident in maintaining the momentum achieved in K6 to date with £80 million of cumulative Totex savings delivered up to H1 2016/17. These savings are being driven by:

- continuing advantages from our strategic alliances including a new water distribution framework and the H_5O capital alliance in place since 2010, now delivering efficient schemes within the Bournemouth region
- ensuring efficient capital investment through the use of data analytics optimising the capital and operating solution and promoting efficient off-site build techniques
- changing ways of working through our iOps programme including utilising new technology and equipment to increase the resources needed to deliver wastewater improvement, real-time pressure management targeting efficient interventions
- delivering Bournemouth Water synergies with £27 million of synergies targeted over K6 and further support function efficiencies.

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25 RORE reflects the Ofwat regulatory guidance of Base RORE plus Outperformance. It is calculated using actual results before non-underlying items (deflated into 2012/13 prices) and compared against the Final Determination allowances sourced from Ofwat published models and based on notional gearing and annual average RCV. Reflects cumulative performance for the 18 months to 30 September 2016. £24m Totex savings delivered in H1 2016/17.

26 Includes integration synergies already delivered. Phasing of actual expenditure compared to the planned programme has been reflected. Outperformance includes a reduction in the RCV run-off for the RCV element of Totex outperformance calculated based on the Final Determination PAYG. Tax impacts reflect actual effective tax rates.

27 Interest outperformance is based on the outturn effective interest rate using the expected K6 RPI of 2.8%, aligned with the long term RPI assumptions, notional debt gearing of 62.5%, and a notional tax impact of 20%.

Delivering net ODI reward

South West Water has 23 ODIs and Bournemouth Water 10 ODIs, including SIM, which have potential financial rewards or penalties. Incentives for performance are recognised in the year of delivery, whether the measure is recovered in period or as a regulatory true-up at the end of the period. Operational performance for the half year has continued to improve and based on performance to 30 September 2016 a net ODI reward of £1.7 million is delivered (£3.8 million cumulatively) reflecting RORE outperformance of 0.3% for K6 to date. Good asset reliability with stable serviceability across all four areas has been maintained. Rewards are forecast across bathing water quality and water restrictions with interruptions to supply and leakage also expected to yield a reward – a significant improvement from the 2015/16 position.

The cumulative net reward of £3.8 million comprises £5.7 million of net rewards recognised at the end of the regulatory period and £1.9 million of net penalty which could be adjusted during the regulatory period.

Whilst penalties are currently forecast for significant pollution events (Category 1 and 2) and external flooding wastewater continues to be an area of focus performance to date has improved from last year.

Financing investment efficiently

Alongside strong operational outperformance, South West Water is confident that the efficient and effective financing strategy in place will continue to deliver cumulative K6 financing outperformance, with £48 million delivered in the K6 period to 30 September 2016. The focus on maintaining efficient gearing levels, having a good balance of fixed and floating rate debt and continuing to implement cost efficient debt through finance leasing all contribute to South West Water having one of the lowest effective interest rates in the industry.

Drinking water quality expected to be in upper quartile

Drinking water quality remains a top priority for South West Water and is forecast to maintain the very high standards achieved in 2015/16. The Drinking Water Inspectorate's (DWI) report published in July 2016 (for 2015/16 performance), confirmed South West Water to be in the top quartile, and Bournemouth Water was top of the table at 100%.

South West Water has met its leakage target every year since its inception and through investment in real-time pressure management and additional network monitoring, leakage for 2016 is expected to outperform its target and deliver an ODI reward. Water resources in the South West region remained unrestricted for a twentieth consecutive year and the Bournemouth water region maintained its position of having no water restrictions since privatisation.

The average duration of supply interruptions per property for South West Water for the first half of the year has reduced significantly compared to 2015/16 and based on current performance would result in a small reward for the year (compared to the penalty incurred in 2015/16). Where an interruption does occur we aim to restore supplies as quickly as possible and keep customers informed of progress.

Significant investment in drinking water

Customers regard a clean and safe supply of drinking water as their top service priority and therefore maintaining water resources and reducing supply interruptions are essential to meeting customer expectations. Key areas of investment and activity during H1 2016/17 included:

- ongoing expenditure for a new £60 million state-of-the-art North Plymouth water treatment works
- improved water treatment processes at two more water treatment works across the region
- real-time pressure management and network modelling technology targeting interventions efficiently
- continued investment in the 'Upstream Thinking' programme of catchment management working in partnership with a range of stakeholder groups including wildlife trusts and river authorities.

SIM continuing to improve

South West Water's overall customer satisfaction is tracking ahead of the prior year at 90% with value for money satisfaction at an all time high for the second quarter of the year.

A key indicator of customer service performance for the water business is the service incentive mechanism (SIM), which Ofwat uses to compare the performance of water companies. The SIM score is calculated against a qualitative element (based on a customer survey) and a quantitative element that takes into account, among other things, the number of complaints received in writing or by phone. South West Water's SIM score for 2015/16 was confirmed at 78.6 and is forecast to increase for 2016/17 continuing the improving trend of recent years. Bournemouth Water's SIM score at 86.2 remains at the frontier as one of the highest in the industry for 2015/16 and is maintaining this trend for H1 2016/17.

In this half year written complaints have fallen by 28% in South West Water and 20% in Bournemouth Water (compared to the same period last year). In addition the customer experience quality scores for the first half of the year have improved across both regions. We are continuing to focus on delivering improvement in the customer experience through faster resolution of issues and lower call waiting times.

South West Water is also focused on providing support for customers and a new employee training and development programme has been implemented extending the support specifically for vulnerable customers. In addition, to further support those customers with affordability issues, a social tariff will be rolled out in the Bournemouth region from 2017/18.

Wastewater improvements

We aim to ensure the safe and efficient removal and disposal of wastewater while minimising the likelihood of sewer flooding or pollution affecting homes, businesses or the environment.

South West Water continues to focus on a targeted programme of wastewater treatment improvements while also working to prevent potential failure through increased monitoring. The targeted investment in high risk sites and change in operational approach has resulted in a significant improvement in numeric compliance (the percentage of wastewater treatment works deemed compliant) with current performance at c.98% compared to the 95.8% in the previous year.

Both the total number of pollution incidents (Categories 1-4) and significant incidents (Categories 1-2) continue to fall. However, the cumulative number of significant incidents at 11 is higher than target and will result in a penalty for the K6 period to date. Improving performance in this area remains our top priority in the wastewater area.

Key areas of wastewater investment and activity during H1 2016/17 included:

- process improvements and upgrades at four key sites including increasing filters and additional treatments
- investing in supply demand schemes increasing capacity at our wastewater treatment works, specifically at Fluxton in Devon and Hayle in Cornwall
- improvements in the sewerage network reducing the impact of saline infiltration.

Bathing water improvement, despite tougher EU standard

Our legacy of major investment to protect bathing waters continues to be reflected in extremely positive results for the 2016 bathing water season, which was assessed under tougher new EU standards. Of the 143 bathing waters tested in the South West Water region, 141 (98.6%) were classified ‘sufficient’ or better, with more than 81% classified as ‘excellent’. Of the two bathing waters rated as ‘poor’ these were not attributed to any failure of South West Water’s assets.

Targeting investment to reduce sewer flooding

Whilst the number of external flooding incidents has reduced, (and are forecast to fall by c.5% from last year), a penalty is still expected to be incurred. South West Water continues to invest in improvement schemes, ongoing capital maintenance, and we are working to improve our response times to flooding incidents. In addition to the significant schemes completed last year at three key catchments, further investments in flooding improvements continue in H1 2016/17 across a number of smaller areas including St Columb in Cornwall.

Furthermore South West Water has also invested over £1 million supporting the Exeter Flood Defence Scheme at our Countess Wear wastewater treatment works.

Good operational and financial performance in Viridor

	H1 2016/17	H1 2015/16
Total Waste Inputs (MT)	3.8	3.8
ERFs	0.9	0.8
Landfill	0.9	1.0
Recycling and Other	2.0	2.0
Recycling Volumes Traded	0.9	0.9

ERFs Driving Growth

We are successfully establishing a significant asset base of ERFs, with eight plants now in operation. Our focus is now on optimisation of the operational plants and increasing performance and average availability, which is expected to be at c.90% for 2016/17.

The operational ERFs are working at a capacity of 2.1 million tonnes of waste inputs and 178 megawatts (MW) per annum including our share of joint ventures. This will extend to 3.2 million tonnes of waste, generating 275 MW by 2021.

Overall, Viridor expects to export over 1 Terawatt hour (TWh) of power to the national grid in 2016/17.

Construction of three further ERFs progressing, committed to new Avonmouth ERF

Of the three ERFs under construction, Dunbar and Beddington ERFs are progressing well and to budget. Glasgow's Recycling and Renewable Energy Centre is receiving waste and the Materials Recycling Facility (MRF) is in commissioning. The Anaerobic Digestion (AD) facility is ready to enter commissioning and the Advanced Combustion Facility (ACF) is c.85% complete, though contractor delays mean full takeover of the centre is now expected in 2017. These delays have resulted in Viridor terminating the construction contract with Interserve. The project will be completed by an experienced team assembled by Viridor with contractual remedies supporting completion. The client (Glasgow CIty Council) has been consulted throughout this period of change, and is supportive of Viridor's actions and the revised plan for completion.

In addition, the Avonmouth ERF near Bristol is now committed and is expected to be completed in 2020/21. Following the commitment to build the Avonmouth ERF the number of ERFs in the portfolio will rise to twelve, eight of which are already in operation. Before capitalised interest, cumulative ERF investment to date is £991 million, excluding the £72 million spent on the Peterborough ERF, which was local authority financed. This leaves c.£460 million left to invest in the ERF programme; c.£80 million in H2 2016/17, c.£180 million in 2017/18, c.£140 million in 2018/19 and c.£60 million in 2019/20.

Maximising value from landfill gas

Our landfill energy business is being managed to maximise the value of landfill gas power generation, whilst exploring alternative commercial development opportunities and other energy uses such as photovoltaic (PV) and energy storage at our landfill sites.

At present, Viridor operates a network of landfill gas power generation sites, contributing 99MW of landfill gas capacity. As the volume of gas declines over time, the actual generation is below the capacity, giving rise to the alternative generation opportunities. In H1 2016/17 the landfill gas power generation output was only marginally down to 263 gigawatt hours (GWh) (H1 2015/16 287 GWh).

Average revenue per Megawatt hour (MWh) was 10.7% lower at £80.35 (H1 2015/16 £89.93) reflecting the lower market prices. The switch from legacy Non Fossil Fuel Obligation (NFFO) contracts to ROCs continues with 93% of energy now sold under the higher value ROCs. We still have NFFO eligibility on one remaining site, equivalent to 7% of energy sold, this will migrate to ROCs in December 2016. Average operating costs increased slightly to £35.33 per MWh (H1 2015/16 £34.76).

Landfill sites being managed for cash and alternative use

Viridor continues its strategy of delivering cash flow from landfill sites. We anticipate the continued reduction of operational landfill capacity in line with government policy, closing or mothballing uneconomic sites. Viridor closed two sites during the half year, bringing the total number of operational sites to thirteen, as part of a planned move to a forecasted retention of a handful of strategic sites by 2020.

While sites are being wound down to closure and aftercare, our emphasis is on reducing costs and we continue to review our approach, optimising the profile to closure as the market for waste arising for this area moves.

The landfill business continues to be cash generative. Viridor's average gate fees increased by 1.3% to £20.88 per tonne in H1 2016/17 (H1 2015/16 £20.62 per tonne). Consented landfill capacity reduced from 47.4 million cubic metres (mcm) to 45.4 mcm in the 6 months to September 2016, reflecting usage and site closures during the period. As previously provided for, c.33 mcm of Viridor's consented landfill capacity is not expected to be used.

Recycling self-help increasing EBITDA

During the period, recycling volumes traded remained consistent with last period at 0.9 million tonnes.

Overall recyclate prices remained flat, but under pressure, with fluctuations accross commodities, reflecting world economic conditions and competitive markets.

Across the period, ongoing self-help measures continued to drive improved margins with EBITDA margin increasing by £5 per tonne, from £8 per tonne in H1 2015/16 to £13 per tonne in H1 2016/17.

Viridor has intensified its Input, Throughput and Output Optimisation (ITOO) programme. In addition to an intensified focus on input quality, including contract renegotiation where required, Viridor has continued to drive cost improvements from further organisational simplification, cost and overhead reduction, with costs reducing by £5 per tonne. Further work is ongoing to improve asset utilisation and rationalise sites.

In line with previous reporting, Viridor continues to observe a new economic realism as the market continues to realign to a model focused on material quality, sharing commodity risk and opportunity between partners. Good progress has been made in contracts renegotiated to date with further opportunities for improvement as over half of contracts are still to be reviewed on renewal.

With the most extensive Material Recycling Facility (MRF) capacity in the UK, focused on resource quality, established markets across the UK, Europe and Asia (including China), where it holds accreditations for export and continued regulatory and societal drivers, Viridor's outlook remains stable.

Contracts and Collections securing waste inputs and ERF fuel

Performance across our major local authority contracts around the UK (the more significant contracts include Greater Manchester, Glasgow, Lancashire, Somerset and West Sussex) and the Thames Water contract remains broadly in line with last period.

We have begun operating our 25-year contracted service for Tomorrow's Valley in Wales (where four local authorities have come together to create a £190 million residual waste contract for 90,000 tonnes per annum) securing fuel for Trident Park ERF.

The performance of the collection business reflects the continued importance of the business in securing increased input tonnages for the business.

Joint Ventures

All three of Viridor's joint ventures continue to perform well.

The joint venture at Lakeside ERF (a 50/50 joint venture with Grundon Waste Management) is in its seventh year of operation and continues to outperform its original power generation and waste processing targets. The second half performance of the asset will be impacted by the timing of a planned shut down.

Viridor Laing Greater Manchester (VLGM), a joint venture between Viridor and John Laing Infrastructure, is delivering the 25-year Greater Manchester Waste PFI. The recycling, recovery and waste management facilities serving the contract are operated by Viridor on a sub-contract basis.

Solid recovered fuel produced from the residual waste from Greater Manchester is used to generate heat and power at Runcorn 1 ERF (TPSCo, a joint venture between Viridor, John Laing Infrastructure and Inovyn) which has operated well since it came on line in 2015.

As planned, at this stage of the joint venture arrangements, a significant proportion of Viridor's income from joint ventures is in the way of finance income on shareholder loans into the projects.

Brexit

As with all major decisions and changes that affect our business, Pennon conducted a thorough analysis of the possible implications of a vote to leave the EU. Pennon did not take a public stance on the EU Referendum as Pennon's Board of Directors believed that the vote itself was a personal decision.

It is too early to know the technical implications of the vote to leave, which will only become clear once the political negotiations are complete. Pennon continues to be well-placed to deliver for customers and shareholders.

Board matters

With effect from 1st September 2016 Phil Piddington was appointed Managing Director of Viridor. Phil joined Viridor in 2014 as Chief Operating Officer to lead the energy division. Since joining the Group, Phil has played a key role in delivering Viridor's portfolio of Energy Recovery Facilities.

Chris Loughlin
Group Chief Executive Officer
25 November 2016

Financial Timetable

(YEAR ENDED 31 MARCH 2017 AND UPCOMING EVENTS)

2 February 2017	Ordinary shares quoted ex-dividend
3 February 2017	Record date for interim dividend
9 February 2017	Trading Statement
13 March 2017	Scrip election date for interim dividend
4 April 2017	Interim cash dividend paid and Scrip shares issued
24 May 2017	Full Year Results 2016/17
Early June 2017	Annual Report & Accounts published
6 July 2017	Annual General Meeting
6 July 2017*	Ordinary shares quoted ex-dividend
7 July 2017*	Record date for final dividend
14 August 2017*	Scrip election date for final dividend
1 September 2017*	Final cash dividend paid and Scrip shares issued
September 2017	Trading Statement
29 November 2017	Half Year Results 2017/18

* These dates are provisional and, in the case of the final dividend subject to obtaining shareholder approval at the 2017 Annual General Meeting.

PRINCIPAL RISKS AND UNCERTAINTIES

In accordance with DTR4.2.3 and 4.2.7 of the Disclosure & Transparency Rules the principal risks for the remaining six months of the financial year which could have a material adverse affect on the Group have been reconsidered, including the potential uncertainties arising from the UK leaving the EU. The Board considers that the principal risks remain in line with those outlined in our 2016 Annual Report, summarised as follows:

Law, Regulation and Finance

- Compliance with law, regulation or decisions by Government and regulators, including water industry market reform
- Maintaining sufficient finance and funding to meet ongoing commitments
- Non-compliance or occurrence of avoidable health and safety incidents
- Uncertainty arising from open tax computations where liabilities remain to be agreed

Market and Economic Conditions

- Non-recovery of customer debt
- Macro-economic risks arising from global and UK economic downturn impacting commodity and power prices
- Increase in defined benefit pension scheme deficit

Operating Performance

- Poor operating performance due to extreme weather or climate change
- Poor customer service and/or increased competition leading to loss of customer base
- Business interruption or significant operational failures/ incidents
- Difficulty in recruitment, retention and development of appropriate skills required to deliver the Group's strategy

Business Systems and Capital Investment

- Failure or increased cost of capital projects and/or exposure to contract failures
- Failure of information technology systems, management and protection including cyber

CAUTIONARY STATEMENT IN RESPECT OF FORWARD-LOOKING STATEMENTS

This Report contains forward-looking statements relating to the Pennon Group's operations, performance and financial position based on current expectations of, and assumptions and forecasts made by, Pennon Group management which may constitute "forward-looking statements" within the meaning of the U.S. Private Securities Litigation Reform Act of 1995. Forward-looking statements are identified in this Report by words such as "anticipate", "aim", "believe", "continue", "could", "due", "estimate", "expect", "forecast", "goal", "intend", "may", "outlook", "plan", "probably", "project", "remain", "seek", "should", "target", "will", "would" and related and similar expressions, as well as statements in the future tense. All statements other than of historical fact may be forward-looking statements and represent the Group's belief regarding future events, many of which, by their nature, are inherently uncertain and outside the Group's control. Various known and unknown risks, uncertainties and other factors could lead to substantial differences between the actual future results, financial situation development or performance of the Group and the estimates and historical results given herein. Important risks, uncertainties and other factors that could cause actual results, performance or achievements of Pennon Group to differ materially from any outcomes or results expressed or implied by such forward-looking statements include, among other things, compliance with law, regulation or decisions by Government and regulators, including water industry reform; maintaining sufficient finance and funding to meet ongoing commitments; non-compliance or occurrence of avoidable Health and Safety incidents; uncertainty arising from open tax computations where liabilities remain to be agreed; non-recovery of customer debt; poor operating performance due to extreme weather and climate change; macro-economic risks arising from the Global and UK economic downturn impacting commodity and power prices; poor customer service/increased competition leading to loss of customer base; business interruption or significant operational failures/incidents; talent management and succession planning in place to meet business requirements; failure or increased cost of capital projects/exposure to contract failures and information technology systems, management and protection including cyber risks. These risks were described in greater detail in the Pennon Group Annual Report published at the beginning of June 2016. Such forward looking statements should therefore be construed in light of such risks, uncertainties and other factors and undue reliance should not be placed on them. Nothing in this report should be construed as a profit forecast.

Any forward-looking statements are made only as of the date of this document and no representation, assurance, guarantee or warranty is given in relation to them including as to their accuracy, completeness, or the basis on which they are made. The Group accepts no obligation to revise or update publicly these forward-looking statements or adjust them as a result of new information or for future events or developments, except to the extent legally required.

UNSOLICITED COMMUNICATIONS WITH SHAREHOLDERS

A number of companies, including Pennon Group Plc, continue to be aware that their shareholders have received unsolicited telephone calls or correspondence concerning investment matters which imply a connection to the company concerned. If shareholders have any concerns about any contact they have received then please refer to the Financial Conduct Authority's website www.fca.org.uk/scamsmart. Details of any share dealing facilities that the Company endorses will be included in Company mailings.

PENNON GROUP PLC

Consolidated income statement for the half year ended 30 September 2016

		Unaudited			
	Note	**Before non-underlying items half year ended 30 September 2016 £m**	**Non-underlying items half year ended 30 September 2016 (note 5) £m**	**Total half year ended 30 September 2016 £m**	Half year ended 30 September 2015 £m
Revenue	4	**685.5**	**-**	**685.5**	689.1
Operating costs					
Manpower costs		**(89.9)**	**(1.1)**	**(91.0)**	(89.7)
Raw materials and consumables used		**(56.1)**	**-**	**(56.1)**	(55.8)
Other operating expenses		**(294.1)**	**(9.6)**	**(303.7)**	(311.9)
Earnings before interest, tax, depreciation and amortisation	4	**245.4**	**(10.7)**	**234.7**	231.7
Depreciation and amortisation		**(91.5)**	**-**	**(91.5)**	(96.4)
Operating profit	4	**153.9**	**(10.7)**	**143.2**	135.3
Finance income	6	**19.7**	**24.4**	**44.1**	22.0
Finance costs	6	**(48.3)**	**(39.4)**	**(87.7)**	(51.5)
Net finance costs	6	**(28.6)**	**(15.0)**	**(43.6)**	(29.5)
Share of post-tax profit from joint ventures		**2.8**	**-**	**2.8**	1.0
Profit before tax	4	**128.1**	**(25.7)**	**102.4**	106.8
Taxation	7	**(30.7)**	**17.4**	**(13.3)**	(21.9)
Profit for the period		**97.4**	**(8.3)**	**89.1**	84.9
Attributable to:					
Ordinary shareholders of the parent		**81.2**	**(8.3)**	**72.9**	68.7
Perpetual capital security holders		**16.2**	**-**	**16.2**	16.2
Earnings per ordinary share (pence per share)	8				
- Basic				**17.7**	16.8
- Diluted				**17.6**	16.7
- Before non-underlying items, deferred tax and adjusted proportionately to reflect the half year impact of annual hybrid periodic return				**23.6**	23.2

The notes on pages 36 to 50 form part of this condensed half year financial information.

PENNON GROUP PLC

Consolidated statement of comprehensive income for the half year ended 30 September 2016

	Unaudited			
	Before non-underlying items half year ended 30 September 2016 £m	**Non-underlying items half year ended 30 September 2016 (note 5) £m**	**Total half year ended 30 September 2016 £m**	Half year ended 30 September 2015 £m
Profit for the period	**97.4**	**(8.3)**	**89.1**	84.9
Other comprehensive loss:				
Items that will not be reclassified to profit or loss				
Remeasurement of defined benefit obligations	**(73.1)**	**-**	**(73.1)**	(8.6)
Income tax on items that will not be reclassified	**14.8**	**(3.6)**	**11.2**	1.8
Total items that will not be reclassified to profit or loss	**(58.3)**	**(3.6)**	**(61.9)**	(6.8)
Items that may be reclassified subsequently to profit or loss				
Share of other comprehensive income from joint ventures	**(2.8)**	**-**	**(2.8)**	(1.0)
Cash flow hedges	**(2.7)**	**-**	**(2.7)**	7.4
Income tax on items that may be reclassified	**0.5**	**(0.5)**	**-**	(1.5)
Total items that may be reclassified subsequently to profit or loss	**(5.0)**	**(0.5)**	**(5.5)**	4.9
Other comprehensive loss for the period net of tax	**(63.3)**	**(4.1)**	**(67.4)**	(1.9)
Total comprehensive income for the period	**34.1**	**(12.4)**	**21.7**	83.0
Total comprehensive income attributable to:				
Ordinary shareholders of the parent	**17.9**	**(12.4)**	**5.5**	66.8
Perpetual capital security holders	**16.2**	**-**	**16.2**	16.2

The notes on pages 36 to 50 form part of this condensed half year financial information.

PENNON GROUP PLC

Consolidated balance sheet at 30 September 2016

	Note	Unaudited 30 September 2016 £m	31 March 2016 £m
ASSETS			
Non-current assets			
Goodwill		**385.0**	385.0
Other intangible assets		**65.1**	63.8
Property, plant and equipment	17	**3,970.6**	3,897.3
Other non-current assets		**279.7**	267.8
Derivative financial instruments		**90.3**	62.7
Investments in joint ventures		**0.1**	0.1
		4,790.8	4,676.7
Current assets			
Inventories		**23.4**	20.6
Trade and other receivables		**333.9**	323.5
Derivative financial instruments		**13.4**	9.5
Cash and cash deposits	14	**657.5**	632.2
		1,028.2	985.8
LIABILITIES			
Current liabilities			
Borrowings	14	**(92.2)**	(65.0)
Financial liabilities at fair value through profit		**(1.3)**	(2.2)
Derivative financial instruments		**(30.8)**	(17.4)
Trade and other payables		**(327.5)**	(264.6)
Current tax liabilities		**(54.5)**	(37.1)
Provisions		**(58.7)**	(50.4)
		(565.0)	(436.7)
Net current assets		**463.2**	549.1
Non-current liabilities			
Borrowings	14	**(3,131.4)**	(3,051.6)
Other non-current liabilities		**(113.4)**	(113.2)
Financial liabilities at fair value through profit		**(51.9)**	(51.0)
Derivative financial instruments		**(66.9)**	(38.5)
Retirement benefit obligations		**(115.6)**	(40.9)
Deferred tax liabilities		**(252.7)**	(272.0)
Provisions		**(157.2)**	(171.0)
		(3,889.1)	(3,738.2)
Net assets		**1,364.9**	1,487.6
Shareholders' equity			
Share capital	10	**168.4**	167.8
Share premium account	11	**216.9**	213.3
Capital redemption reserve		**144.2**	144.2
Retained earnings and other reserves		**540.6**	667.5
Total shareholders' equity		**1,070.1**	1,192.8
Perpetual capital securities	12	**294.8**	294.8
Total equity		**1,364.9**	1,487.6

The notes on pages 36 to 50 form part of this condensed half year financial information.

PENNON GROUP PLC

Consolidated statement of changes in equity

	Share capital (note 10) £m	Share premium account (note 11) £m	Capital redemption reserve £m	Retained earnings and other reserves £m	Perpetual capital securities (note 12) £m	Total equity £m
	Unaudited					
At 1 April 2015	162.4	118.6	144.2	634.1	294.8	1,354.1
Profit for the period	-	-	-	68.7	16.2	84.9
Other comprehensive loss for the period	-	-	-	(1.9)	-	(1.9)
Total comprehensive income for the period	-	-	-	66.8	16.2	83.0
Transactions with equity shareholders						
Dividends paid or approved	-	-	-	(129.5)	-	(129.5)
Adjustment for shares issued under the scrip dividend alternative	0.3	(0.3)	-	6.3	-	6.3
Equity issuance	4.9	95.4	-	-	-	100.3
Distributions due to perpetual capital security holders	-	-	-	-	(20.3)	(20.3)
Current tax relief on distributions to perpetual capital security holders	-	-	-	-	4.1	4.1
Adjustment in respect of share-based Payments	-	-	-	2.4	-	2.4
Own shares acquired by the Pennon Employee Share Trust in respect of share options granted	-	-	-	(1.1)	-	(1.1)
Proceeds from treasury shares re-issued	-	-	-	2.5	-	2.5
Proceeds from shares issued under the Sharesave Scheme	0.2	1.4	-	-	-	1.6
Equity issuance related costs	-	(2.3)	-	-	-	(2.3)
	5.4	94.2	-	(119.4)	(16.2)	(36.0)
At 30 September 2015	167.8	212.8	144.2	581.5	294.8	1,401.1

	Share capital (note 10) £m	Share premium account (note 11) £m	Capital redemption reserve £m	Retained earnings and other reserves £m	Perpetual capital securities (note 12) £m	Total equity £m
	Unaudited					
At 1 April 2016	167.8	213.3	144.2	667.5	294.8	1,487.6
Profit for the period	-	-	-	72.9	16.2	89.1
Other comprehensive loss for the period	-	-	-	(67.4)	-	(67.4)
Total comprehensive income for the period	-	-	-	5.5	16.2	21.7
Transactions with equity shareholders						
Dividends paid	-	-	-	(138.5)	-	(138.5)
Adjustment for shares issued under the scrip dividend alternative	0.3	(0.3)	-	6.9	-	6.9
Distributions due to perpetual capital security holders	-	-	-	-	(20.3)	(20.3)
Current tax relief on distributions to perpetual capital security holders	-	-	-	-	4.1	4.1
Adjustment in respect of share-based Payments	-	-	-	1.8	-	1.8
Own shares acquired by the Pennon Employee Share Trust in respect of share options granted	0.1	1.2	-	(2.6)	-	(1.3)
Proceeds from shares issued under the Sharesave Scheme	0.2	2.6	-	-	-	2.8
Proceeds from shares issued under the Executive Share Option Scheme	-	0.1	-	-	-	0.1
	0.6	3.6	-	(132.4)	(16.2)	(144.4)
At 30 September 2016	**168.4**	**216.9**	**144.2**	**540.6**	**294.8**	**1,364.9**

The notes on pages 36 to 50 form part of this condensed half year financial information.

PENNON GROUP PLC

Consolidated statement of cash flows for the half year ended 30 September 2016

	Note	**Unaudited** **Half year ended 30 September 2016 £m**	Half year ended 30 September 2015 £m
Cash flows from operating activities			
Cash generated from operations	13	**243.3**	206.4
Interest paid		**(35.1)**	(41.4)
Tax paid		**-**	(9.5)
Net cash generated from operating activities		**208.2**	155.5
Cash flows from investing activities			
Interest received		**1.8**	4.5
Loan repayments received from joint ventures		**4.0**	19.5
Acquisitions, net of cash acquired		**-**	(90.0)
Purchase of property, plant and equipment		**(158.2)**	(141.4)
Proceeds from sale of property, plant and equipment		**3.2**	2.7
Net cash used in investing activities		**(149.2)**	(204.7)
Cash flows from financing activities			
Proceeds from issuance of ordinary shares		**4.2**	99.6
Proceeds from treasury shares re-issued	10	**-**	2.5
Release/(deposit) of restricted funds		**7.5**	(14.9)
Purchase of ordinary shares by the Pennon Employee Share Trust		**(2.6)**	(1.1)
Proceeds from new borrowing		**130.0**	130.0
Repayment of borrowings		**(23.0)**	(95.1)
Finance lease sale and leaseback		**0.2**	0.9
Finance lease principal repayments		**(10.9)**	(15.0)
Dividends paid		**(131.6)**	(37.7)
Net cash (used)/received from financing Activities		**(26.2)**	69.2
Net increase in cash and cash equivalents		**32.8**	20.0
Cash and cash equivalents at beginning of period	14	**405.7**	574.8
Cash and cash equivalents at end of period	14	**438.5**	594.8

The notes on pages 36 to 50 form part of this condensed half year financial information.

PENNON GROUP PLC

Notes to the condensed half year financial information

1. General information

Pennon Group Plc is a company registered in the United Kingdom under the Companies Act 2006. The address of the registered office is given on page 50. Pennon Group's business is operated through two main subsidiaries. South West Water Limited includes the merged water companies of South West Water and Bournemouth Water, holding the water and wastewater services appointments for Devon, Cornwall and parts of Dorset and Somerset and the water appointments for parts of Dorset, Hampshire and Wiltshire. Viridor Limited's business is waste, recycling and recovery.

This condensed half year financial information was approved by the Board of Directors on 24 November 2016.

The financial information for the period ended 30 September 2016 does not constitute statutory accounts within the meaning of section 435 of the Companies Act 2006. The statutory accounts for 31 March 2016 were approved by the Board of Directors on 24 May 2016 and have been delivered to the Registrar of Companies. The independent auditor's report on these financial statements was unqualified, and did not contain a statement under section 498 of the Companies Act 2006.

2. Basis of preparation

This condensed half year financial information has been prepared in accordance with the Disclosure and Transparency Rules of the Financial Services Authority and with IAS 34 "Interim financial reporting" as adopted by the European Union (EU). This condensed half year financial information should be read in conjunction with the Pennon Group Plc Annual Report and Accounts for the year ended 31 March 2016, which were prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the EU.

Having made enquiries, the Directors consider that the Company and its subsidiary undertakings have adequate resources to continue in business for the foreseeable future, and that it is therefore appropriate to adopt the going concern basis in preparing the condensed half year financial information.

This condensed half year financial information has been reviewed but not audited by the independent auditor pursuant to the Auditing Practices Board guidance on the "Review of Interim Financial Information".

The preparation of the half year financial information requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets and liabilities, income and expense. Actual results may differ from these estimates. The significant judgements made by management in applying the Group's accounting policies and the key sources of estimation uncertainty are consistent with those that applied to the consolidated financial statements for the year ended 31 March 2016, with the exception of changes in estimates that are required in determining the half year provision of income taxes.

3. Accounting policies

The accounting policies adopted in this condensed half year financial information are consistent with those applied and set out in the Pennon Group Plc Annual Report and Accounts for the year ended 31 March 2016 and are in accordance with all IFRSs and interpretations of the IFRS Interpretations Committee expected to be applicable for the year ended 31 March 2017 in issue which have been adopted by the EU.

New standards or interpretations which were mandatory for the first time in the year beginning 1 April 2016 did not have a material impact on the net assets or results of the Group.

The tax charge for September 2016 and September 2015 has been derived by applying the anticipated effective annual rate to the first half year profit before tax.

PENNON GROUP PLC

Notes to the condensed half year financial information (continued)

4. Segmental information

Operating segments are reported in a manner consistent with internal reporting provided to the Chief Operating Decision-Maker, which has been identified as the Pennon Group Plc Board.

The water business comprises the regulated water and wastewater services undertaken by South West Water and the regulated water services undertaken by Bournemouth Water. The waste management business is the waste recycling and recovery services provided by Viridor Limited.

	Unaudited	
	Half year ended 30 September 2016 £m	Half year ended 30 September 2015 £m
Revenue		
Water	**287.9**	279.3
Waste management	**397.9**	410.1
Other	**6.1**	6.1
Less intra-segment trading	**(6.4)**	(6.4)
	685.5	689.1
Segment result		
Operating profit before depreciation, amortisation and non-underlying items (EBITDA)		
Water	**183.0**	173.6
Waste management	**63.3**	61.0
Other	**(0.9)**	(2.9)
	245.4	231.7
Operating profit before non-underlying items		
Water	**127.2**	117.7
Waste management	**27.7**	20.5
Other	**(1.0)**	(2.9)
	153.9	135.3
Profit before tax and non-underlying items		
Water	**97.0**	87.0
Waste management	**23.1**	12.9
Other	**8.0**	6.9
	128.1	106.8
Profit before tax		
Water	**96.5**	87.0
Waste management	**12.9**	12.9
Other	**(7.0)**	6.9
	102.4	106.8

Intra-segment transactions between and to other segments are under normal commercial terms and conditions. Intra-segment revenue or interest receivable of one segment is a cost or interest payable of another.

Factors such as seasonal weather patterns can affect sales volumes, income and costs in both the water and waste management segments.

PENNON GROUP PLC

Notes to the condensed half year financial information (continued)

4. Segmental information (continued)

Geographic analysis of revenue based on location of customers

	Unaudited	
	Half year ended 30 September 2016 £m	Half year ended 30 September 2015 £m
UK	**663.5**	664.2
Rest of European Union	**3.9**	4.5
China	**14.6**	12.2
Rest of World	**3.5**	8.2
	685.5	689.1

The Group's country of domicile is the United Kingdom and is the country in which it generates the majority of its revenue. The Group's non-current assets are located in the United Kingdom.

5. Non-underlying items

Non-underlying items are those that in the Directors' view are required to be separately disclosed by virtue of their size, nature or incidence to enable a full understanding of the Group's financial performance.

	Unaudited	
	Half year ended 30 September 2016 £m	Half year ended 30 September 2015 £m
Operating costs		
Shared services restructuring cost (a)	**(10.7)**	-
Total net operating costs	**(10.7)**	-
Remeasurement of fair value movement in derivatives (b)	**(15.0)**	-
Deferred tax change in rate (c)	**20.1**	-
Tax charge arising on non-underlying items	**(2.7)**	-
Net non-underlying charge	**(8.3)**	-

(a) During the period a one-off charge of £10.7m was made relating to restructuring costs associated with the Group-wide Shared Services Review. The £10.7m charge consists of a £9.5m non-cash charge to other operating expenses relating to a rationalisation of systems leading to an asset de-recognition, and a £1.1m charge to manpower costs and a £0.1m charge to other operating costs in relation to restructuring provisions.

(b) In the period a credit of £24.4m was recognised relating to non-cash derivative fair value movements associated with derivatives that are not designated as being party to an accounting hedge relationship.

In addition, a charge of £39.4m was made to recognise the movement in the fair value of another derivative arrangement relating to a change in legislation, which impacts the derivative's future cash flows.

(c) Following the enactment during the period the rate of corporation tax reduced from 18% to 17% from April 2020, resulting in a one-off credit of £20.1m being recognised in the income statement. In addition a charge of £4.1m has been recognised in the statement of comprehensive income.

PENNON GROUP PLC

Notes to the condensed half year financial information (continued)

6. **Net finance costs**

	Unaudited					
	Half year ended 30 September 2016			Half year ended 30 September 2015		
	Finance cost £m	**Finance income £m**	**Total £m**	Finance cost £m	Finance income £m	Total £m
Cost of servicing debt						
Bank borrowings and overdrafts	**(24.2)**	**-**	**(24.2)**	(25.4)	-	(25.4)
Interest element of finance lease rentals	**(16.2)**	**-**	**(16.2)**	(17.4)	-	(17.4)
Other finance costs	**(2.2)**	**-**	**(2.2)**	(2.0)	-	(2.0)
Interest receivable	**-**	**1.8**	**1.8**	-	3.8	3.8
Interest receivable on shareholder loans to joint ventures	**-**	**5.0**	**5.0**	-	5.7	5.7
	(42.6)	**6.8**	**(35.8)**	(44.8)	9.5	(35.3)
Notional interest						
Interest receivable on service concession arrangements	**-**	**8.8**	**8.8**	-	8.3	8.3
Retirement benefit obligations	**(0.6)**	**-**	**(0.6)**	(1.2)	-	(1.2)
Unwinding of discounts on provisions	**(5.1)**	**-**	**(5.1)**	(5.5)	-	(5.5)
	(5.7)	**8.8**	**3.1**	(6.7)	8.3	1.6
Net gains on derivative financial instruments arising from the combination of non-derivative instruments	**-**	**4.1**	**4.1**	-	4.2	4.2
Net finance costs before non-underlying items	**(48.3)**	**19.7**	**(28.6)**	(51.5)	22.0	(29.5)
Non-underlying items (note 5)						
Fair value remeasurement of non-designated derivative financial instruments	**(39.4)**	**24.4**	**(15.0)**	**-**	**-**	-
Net finance costs after non-underlying items	**(87.7)**	**44.1**	**(43.6)**	(51.5)	22.0	(29.5)

PENNON GROUP PLC

Notes to the condensed half year financial information (continued)

7. **Taxation**

	Unaudited			
	Before non-underlying items half year ended 30 September 2016 £m	**Non-underlying items half year ended 30 September 2016 (note 5) £m**	**Total half year ended 30 September 2016 £m**	Half year ended 30 September 2015 £m
Analysis of charge :				
Current tax charge	**22.8**	**(1.3)**	**21.5**	3.8
Deferred tax charge/(credit)	**7.9**	**(16.1)**	**(8.2)**	18.1
Tax charge for the year	**30.7**	**(17.4)**	**13.3**	21.9

UK corporation tax is calculated at 20% (H1 2015/16 20%) of the estimated assessable profit for the year. The tax charge for September 2016 and September 2015 has been derived by applying the anticipated effective annual tax rate to the first half year profit before tax.

Tax on amounts included in the consolidated statement of comprehensive income, or directly in equity, is included in those statements respectively.

The effective tax rate for the period before the impact of non-underlying items was 24% (H1 2015/16 21%).

PENNON GROUP PLC

Notes to the condensed half year financial information (continued)

8. **Earnings per share**

Basic earnings per share are calculated by dividing the earnings attributable to ordinary shareholders by the weighted average number of ordinary shares outstanding during the period, excluding those held in the employee share trust which are treated as cancelled. For diluted earnings per share the weighted average number of ordinary shares is adjusted to include all dilutive potential ordinary shares.

The weighted average number of shares and earnings used in the calculations were:

	Unaudited	
	Half year ended 30 September 2016	Half year ended 30 September 2015
Number of shares (millions)		
For basic earnings per share	**412.5**	409.9
Effect of dilutive potential ordinary shares from share options	**2.1**	1.6
For diluted earnings per share	**414.6**	411.5

Basic and diluted earnings per ordinary share

Adjusted earnings per share are presented to provide a more useful comparison on business trends and performance. Non-underlying items are adjusted for by virtue of their size, nature or incidence to enable a full understanding of the Group's financial performance (as described in note 5). The annual perpetual capital return is recognised in full at the half year, so is proportionately adjusted to allow a more useful comparison at the half year.

Earnings per share have been calculated:

	Unaudited					
	Half year ended 30 September 2016			Half year ended 30 September 2015		
		Earnings per ordinary share			Earnings per ordinary share	
	Profit after tax £m	**Basic p**	**Diluted p**	Profit after tax £m	Basic p	Diluted p
Statutory earnings	**72.9**	**17.7**	**17.6**	68.7	16.8	16.7
Deferred tax charge before non-underlying items (note 7)	**7.9**	**1.9**	**1.9**	18.1	4.4	4.4
Non-underlying items (net of tax) (note 5)	**8.3**	**2.0**	**1.9**	-	-	-
Proportionate impact of perpetual capital returns (note 12)	**8.1**	**2.0**	**2.0**	8.1	2.0	2.0
Adjusted earnings	**97.2**	**23.6**	**23.4**	94.9	23.2	23.1

PENNON GROUP PLC

Notes to the condensed half year financial information (continued)

9. Dividends to ordinary shareholders

Amounts recognised as distributions to ordinary shareholders in the period :

	Unaudited	
	Half year ended 30 September 2016 £m	Half year ended 30 September 2015 £m
Interim dividend paid for the year ended 31 March 2016 : 10.46p (2015 9.98p) per share	**43.1**	39.8
Final dividend approved for the year ended 31 March 2016 : 23.12p (2015 21.82p) per share	**95.4**	89.7
	138.5	129.5

Proposed interim dividend

	Unaudited	
	Half year ended 30 September 2016 £m	Half year ended 30 September 2015 £m
Proposed interim dividend for the year ended 31 March 2017 : 11.09p (2016 10.46p) per share	**45.9**	43.1

The proposed interim dividend of 11.09p per share will be paid on 4 April 2017 to shareholders on the register on 3 February 2017.

The proposed interim dividend has not been included as a liability in this condensed half year financial information.

PENNON GROUP PLC

Notes to the condensed half year financial information (continued)

10. **Share capital**

Allotted, called up and fully paid

1 April 2015 to 30 September 2015	Unaudited		
	Number of shares		
	Treasury shares	Ordinary shares	£m
At 1 April 2015 ordinary shares of 40.7p each	389,515	398,720,708	162.4
Shares issued in respect of the equity issuance	-	12,084,337	4.9
Shares issued under the scrip dividend alternative	-	236,033	0.1
Shares re-issued under the Company's Executive Share Option Scheme	(8,305)	8,305	-
For consideration of £1.1m, shares re-issued to the Pennon Employee Share Trust	(143,538)	143,538	-
For consideration of £1.4m, shares re-issued under the Company's Sharesave Scheme	(227,316)	227,316	-
For consideration of £1.6m, shares issued in respect of the Company's Sharesave Scheme	-	280,090	0.2
At 30 September 2015 ordinary shares in issue of 40.7p each	10,356	411,700,327	167.6
Shares to be issued under the scrip dividend alternative	-	524,593	0.2
	10,356	412,224,920	167.8

1 April 2016 to 30 September 2016	Unaudited		
	Number of shares		
	Treasury shares	Ordinary shares	£m
At 1 April 2016 ordinary shares of 40.7p each	10,356	412,340,597	167.8
Shares issued under the scrip dividend alternative	-	771,563	0.3
Shares re-issued under the Company's Executive Share Option Scheme	(1,913)	1,913	-
For consideration of £1.3m, shares issued to the Pennon Employee Share Trust	-	143,479	0.1
For consideration of £0.1m, shares issued under the Company's Executive Share Option Scheme	-	24,457	-
For consideration of £2.8m, shares issued in respect of the Company's Sharesave Scheme	-	524,905	0.2
At 30 September 2016 ordinary shares in issue of 40.7p each	**8,443**	**413,806,914**	**168.4**

Shares held as treasury shares may be sold, re-issued for any of the Company's share schemes, or cancelled.

The weighted average market price of the Company's shares at the date of exercise of Sharesave Scheme options during the half year was 887p (H1 2015/16 767p).

PENNON GROUP PLC

Notes to the condensed half year financial information (continued)

11. Share premium account

	Unaudited £m
1 April 2015 to September 2015	
At 1 April 2015	118.6
Equity placing	95.4
Adjustment for shares issued under the scrip dividend alternative	(0.3)
Shares issued under the Sharesave Scheme	1.4
Equity issuance related costs	(2.3)
At 30 September 2015	212.8
1 April 2016 to 30 September 2016	
At 1 April 2016	213.3
Adjustment for shares issued under the scrip dividend alternative	(0.3)
Shares issued under the Sharesave Scheme	2.6
Shares issued under the Executive Share Option Scheme	0.1
Shares issued to the Pennon Employee Share Trust	1.2
At 30 September 2016	**216.9**

12. Perpetual capital securities

	Unaudited Half year ended 30 September 2016 £m	Year ended 31 March 2016 £m
GBP 300m 6.75% perpetual subordinated capital securities	**294.8**	294.8

On 8 March 2013 the Company issued £300m perpetual capital securities. They have no fixed redemption date but the Company may, at its sole discretion, redeem all, but not part, of these securities at their principal amount on 8 March 2018 or any subsequent periodic return payment date after this.

The Company has the option to defer periodic returns on any relevant payment date, as long as a dividend on the Ordinary Shares has not been paid or declared in the previous 12 months. Deferred periodic returns shall be satisfied only on redemption or payment of dividend on Ordinary Shares, all of which only occur at the sole discretion of the Company.

As the Company paid a dividend on 1 April 2016 the periodic return of £20.3m scheduled 8 March 2017 is payable and consequently has been recognised as a liability at 30 September 2016.

PENNON GROUP PLC

Notes to the condensed half year financial information (continued)

13. **Cash flow from operating activities**

Reconciliation of profit to net cash inflow from operating activities:

	Unaudited	
	Half year ended 30 September 2016 £m	Half year ended 30 September 2015 £m
Cash generated from operations		
Profit for the period	**89.1**	84.9
Adjustments for:		
Share-based payments	**1.8**	2.4
Profit on disposal of property, plant and equipment	**(2.0)**	(4.1)
Depreciation charge	**90.1**	94.6
Amortisation of intangible assets	**1.4**	1.8
Non-underlying restructuring costs	**10.7**	-
Non-underlying movement in derivatives	**15.0**	-
Share of post-tax profit from joint ventures	**(2.8)**	(1.0)
Finance income	**(19.7)**	(22.0)
Finance costs	**48.3**	51.5
Taxation charge	**13.3**	21.9
Changes in working capital :		
Increase in inventories	**(2.8)**	(5.0)
(Increase)/ decrease in trade and other receivables	**(2.3)**	2.3
Increase in service concession arrangements receivable	**(13.2)**	(13.4)
Increase in trade and other payables	**27.3**	0.5
Increase in retirement benefit obligations	**1.0**	0.9
Decrease in provisions	**(11.9)**	(8.9)
Cash generated from operations	**243.3**	206.4

	Unaudited	
Total interest paid	**Half year ended 30 September 2016 £m**	Half year ended 30 September 2015 £m
Interest paid in operating activities	**35.1**	41.4
Interest paid in investing activities	**6.1**	4.0
Total interest paid	**41.2**	45.4

PENNON GROUP PLC

Notes to the condensed half year financial information (continued)

14. **Net borrowings**

	Unaudited Half year ended 30 September 2016 £m	Year ended 31 March 2016 £m
Cash and cash deposits	**657.5**	632.2
Borrowings – current		
Bank and other loans	**(24.9)**	-
Other current borrowings	**(41.1)**	(39.0)
Finance lease obligations	**(26.2)**	(26.0)
Total current borrowings	**(92.2)**	(65.0)
Borrowings – non-current		
Bank and other loans	**(1,484.9)**	(1,502.5)
Other non-current borrowings	**(339.4)**	(234.5)
Finance lease obligations	**(1,307.1)**	(1,314.6)
Total non-current borrowings	**(3,131.4)**	(3,051.6)
Total net borrowings	**(2,566.1)**	(2,484.4)

For the purposes of the cash flow statement cash and cash equivalents comprise:

	Unaudited Half year ended 30 September 2016 £m	Year ended 31 March 2016 £m
Cash and cash deposits as above	**657.5**	632.2
Less : deposits with a maturity of three months or more (restricted funds)	**(219.0)**	(226.5)
	438.5	405.7

Restricted funds are available for access, subject to being replaced by an equivalent valued security.

PENNON GROUP PLC

Notes to the condensed half year financial information (continued)

15. **Fair value disclosure for financial instruments**

Fair value of financial instruments carried at amortised cost

Financial assets and liabilities which are not carried at an amount which approximates to their fair value are:

	Unaudited Half year ended 30 September 2016		Year ended 31 March 2016	
	Book value £m	**Fair value £m**	Book value £m	Fair value £m
Non-current borrowings :				
Bank and other loans	**(1,484.9)**	**(1,694.5)**	(1,502.5)	(1,566.2)
Other non-current borrowings	**(339.4)**	**(300.5)**	(234.5)	(209.3)
Finance lease obligations	**(1,307.1)**	**(1,188.0)**	(1,314.6)	(1,163.0)
Total non-current borrowings	**(3,131.4)**	**(3,183.0)**	(3,051.6)	(2,938.5)
Other non-current assets	**279.7**	**348.4**	267.8	334.9

Compared to 31 March 2016 balances the difference between the book value and fair value of the Group's non-current borrowings and assets relates to a decrease in the underlying interest rates used to calculate the fair value.

Valuation hierarchy of financial instruments carried at fair value

The Group uses the following hierarchy for determining the fair value of financial instruments by valuation technique:

- quoted prices (unadjusted) in active markets for identical assets or liabilities (level 1)
- inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices) (level 2)
- inputs for the asset or liability that are not based on observable market data (that is, unobservable inputs) (level 3).

The fair value of financial instruments not traded in an active market (level 2, for example over-the-counter derivatives) is determined by using valuation techniques. A variety of methods and assumptions are used based on market conditions existing at each balance sheet date. Quoted market prices or dealer quotes for similar instruments are used for long-term debt. Other techniques, such as estimated discounted cash flows, are used to determine fair value for the remaining financial instruments. The fair value of interest rate swaps is calculated as the present value of the estimated future cash flows.

PENNON GROUP PLC

Notes to the condensed half year financial information (continued)

15. **Fair value disclosure for financial instruments (continued)**

Valuation hierarchy of financial instruments carried at fair value (continued)

The Group's financial instruments are valued principally using level 2 measures:

	Unaudited Half year ended 30 September 2016 £m	Year ended 31 March 2016 £m
Level 2 inputs		
Assets		
Derivatives used for cash flow hedging	**18.0**	3.4
Derivatives used for fair value hedging	**-**	1.8
Derivatives not in a hedge accounting relationship	**85.7**	67.0
Total assets	**103.7**	72.2
Liabilities		
Derivatives used for cash flow hedging	**53.6**	46.9
Derivatives used for fair value hedging	**-**	-
Derivatives not in a hedge accounting relationship	**4.6**	4.8
Total liabilities	**58.2**	51.7

Financial instruments valued using level 3 measures are valued by the counterparty using cash flows discounted at prevailing mid-market rates. The fair value of such financial instruments is not significantly sensitive to unobservable inputs.

Level 3 inputs		
Liabilities		
Derivatives deemed held for trading	**39.5**	4.2

The fair value of level 3 inputs is determined using the Black-Scholes valuation model with reference to prevailing mid-market rates and a propriety Nomura index.

The table below shows the summary of changes in the fair value of the Group's level 3 financial instruments:

	Unaudited Half year ended 30 September 2016 £m	Year ended 31 March 2016 £m
Opening liability	**(4.2)**	(3.6)
(Losses) and gains recognised in net finance costs	**(35.3)**	8.4
Settlement of recognised gains	**-**	(9.0)
Closing liability	**(39.5)**	(4.2)

PENNON GROUP PLC

Notes to be condensed half year financial information (continued)

16. **Retirement benefit obligations**

Defined benefit schemes

The principal actuarial assumptions were: the rate used to discount schemes' liabilities and expected return on scheme assets of 2.35% (March 2016 3.30%) and the inflation assumption of 3.0% (March 2016 2.9%).

	Unaudited Half year ended 30 September 2016			Year ended 31 March 2016		
	Present value of obligation £m	**Fair value of plan assets £m**	**Total £m**	Present value of obligation £m	Fair value of plan assets £m	Total £m
At 1 April	**(833.6)**	**792.7**	**(40.9)**	(752.3)	692.7	(59.6)
Arising on acquisition	**-**	**-**	**-**	(86.6)	88.5	1.9
Amounts recognised in the income statement	**(20.8)**	**13.0**	**(7.8)**	(39.9)	25.5	(14.4)
Remeasurements through other comprehensive income	**(168.5)**	**95.4**	**(73.1)**	17.1	(19.7)	(2.6)
Contributions	**13.7**	**(7.5)**	**6.2**	28.1	5.7	33.8
	(1,009.2)	**893.6**	**(115.6)**	(833.6)	792.7	(40.9)

The deficit has increased during the period due to the post-Brexit fall in bond yields, increasing the valuation of liabilities. Over half of the increase in the valuation of liabilities has been offset by increases in asset values.

17. **Capital expenditure**

	Unaudited Half year ended 30 September 2016 £m	Year ended 31 March 2016 £m
Property, plant and equipment		
Additions	**173.9**	284.2
Net book value of disposals	**10.7**	11.3
Capital commitments		
Contracted but not provided	**355.7**	374.4

Notes to the condensed half year financial information (continued)

18. **Contingent liabilities**

	Unaudited Half year ended 30 September 2016 £m	Year ended 31 March 2016 £m
Performance bonds	**187.5**	159.7
Other	**4.0**	4.0
	191.5	163.7

Performance bonds are entered into in the normal course of business. No liability is expected to arise in respect of the bonds.

The Group is subject to litigation from time to time as a result of its activities, including a prosecution from the Health and Safety Executive in relation to the fatality of an employee at Falmouth wastewater treatment works in 2013. The Group establishes provisions in connection with litigation where it has a present legal or constructive obligation as a result of a past event and where it is more likely than not an outflow of resources will be required to settle the obligation and the amount can be reliably estimated.

19. **Related party transactions**

The Group's significant related parties are its joint ventures in Lakeside Energy from Waste Holdings Limited and Viridor Laing (Greater Manchester) Holdings Limited and its associate INEOS Runcorn (TPS) Holdings Limited, for which disclosures were made in the Pennon Group Plc Annual Report and Accounts for the year ended 31 March 2016.

There were no material changes during the half year to September 2016 in the nature of transactions with these related parties.

Pennon Group Plc
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EX2 7HR
pennon-group.co.uk

Registered in England No 2366640

PENNON GROUP PLC

DIRECTORS' RESPONSIBILITIES STATEMENT

The Directors named below confirm on behalf of the Board of Directors that this unaudited condensed half year financial information has been prepared in accordance with IAS 34 "Interim financial reporting" as adopted by the European Union and to the best of their knowledge the interim management report herein includes a fair review of the information required by DTR 4.2.4, DTR 4.2.7R and DTR 4.2.8R of the Disclosure and Transparency Rules, being an indication of important events that have occurred during the period and their impact on the unaudited condensed half year financial information; a description of the principal risks and uncertainties for the remaining six months of the current financial year; and the disclosure requirements in respect of material related party transactions.

The Directors are responsible for the maintenance and integrity of the Company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial information may differ from legislation in other jurisdictions.

The Directors of Pennon Group Plc at the date of the signing of this announcement and statement are:

Sir John Parker
Martin Angle
Gill Rider
Neil Cooper
Chris Loughlin
Susan Davy

For and on behalf of the Board of Directors who approved this half year report on 24 November 2016.

C Loughlin
Group Chief Executive Officer

S J Davy
Chief Financial Officer

PENNON GROUP PLC

INDEPENDENT REVIEW REPORT TO PENNON GROUP PLC

Introduction

We have been engaged by the Company to review the condensed consolidated set of financial statements in the half-yearly financial report for the six months ended 30 September 2016 which comprises the Consolidated income statement, the Consolidated statement of comprehensive income, the Consolidated balance sheet, the Consolidated statement of changes in equity, the Consolidated statement of cash flows and related notes. We have read the other information contained in the half yearly financial report and considered whether it contains any apparent misstatements or material inconsistencies with the information in the condensed set of financial statements.

This report is made solely to the company in accordance with guidance contained in International Standard on Review Engagements 2410 (UK and Ireland) "Review of Interim Financial Information Performed by the Independent Auditor of the Entity" issued by the Auditing Practices Board. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company, for our work, for this report, or for the conclusions we have formed.

Directors' Responsibilities

The half-yearly financial report is the responsibility of, and has been approved by, the directors. The directors are responsible for preparing the half-yearly financial report in accordance with the Disclosure and Transparency Rules of the United Kingdom's Financial Conduct Authority.

As disclosed in note 2, the annual financial statements of the Group are prepared in accordance with IFRSs as adopted by the European Union. The condensed set of financial statements included in this half-yearly financial report has been prepared in accordance with International Accounting Standard 34, "Interim Financial Reporting", as adopted by the European Union.

Our Responsibility

Our responsibility is to express to the Company a conclusion on the condensed set of financial statements in the half-yearly financial report based on our review.

Scope of Review

We conducted our review in accordance with International Standard on Review Engagements (UK and Ireland) 2410, "Review of Interim Financial Information Performed by the Independent Auditor of the Entity" issued by the Auditing Practices Board for use in the United Kingdom. A review of interim financial information consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing (UK and Ireland) and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the condensed consolidated set of financial statements in the half-yearly financial report for the six months ended 30 September 2016 is not prepared, in all material respects, in accordance with International Accounting Standard 34 as adopted by the European Union and the Disclosure and Transparency Rules of the United Kingdom's Financial Conduct Authority.

Ernst & Young LLP
Reading
24 November 2016