



Interim Results 2004

For the half year ended 30 September 2004

www.pennon-group.co.uk

Pennon Group Plc

Financial Highlights

- Operating profit up 11.0% to £78.4m ⁽¹⁾
 - South West Water up 6.9% to £65.3m
 - Viridor Waste up 30.6% to £14.5m before goodwill
- Profit before tax up 11.0% to £47.4m ⁽¹⁾
- Earnings per share (before deferred tax) up 9.9% to 34.3p ⁽¹⁾
- Interim dividend per share up 4.5% to 13.8p
- Final Determination received by South West Water

⁽¹⁾ Before exceptional item in 2004/05 of £2.0m for costs incurred relating to abortive acquisition

Pennon Group Plc

Operational Highlights

South West Water

- Remains on track to outperform the current regulatory contract
- Ofwat confirmed 2003/04 OPA improvement of 45 points and enhanced efficiency banding

Viridor Waste

- Continued strong growth in profits from landfill and power generation
- Thames Waste acquisition and West Sussex PFI performing in line with expectations



Pennon Group Plc



Pennon Group Plc

Pennon Group Plc

Summary Financial Results

For the half year ended
30 September

	2004 £m	2003 £m	Change %	2003/04 £m
Group turnover	282.2	234.8	20.2	471.3
Group operating profit ⁽¹⁾	78.4	70.6	11.0	136.3
Group profit before tax ⁽¹⁾	47.4	42.7	11.0	78.8
Earnings per share ⁽²⁾	34.3	31.2	9.9	57.7

- *Strong financial performance. Last year's H2 boosted by recognition of high Summer demand in SWW*

⁽¹⁾ *Before exceptional item in 2004/05 of £2.0m for costs incurred relating to abortive acquisition (2003/04 £6.5m)*

⁽²⁾ *Before exceptional item and deferred tax*

Pennon Group Plc

Cash Flow

For the half year
ended
30 September

	2004	2003	2003/04
	£m	£m	£m
Cash inflow from operations	135.0	103.8	215.1
Net interest paid	(22.5)	(9.6)	(41.3)
Dividends and tax paid	(10.6)	(15.6)	(47.1)
Capital expenditure	(81.0)	(94.9)	(178.6)
Acquisitions	(28.5)	(20.0)	(20.0)
Net cash outflow	(7.6)	(36.3)	(71.9)
Shares issued and purchased	0.7	1.2	1.5
Non-cash movements	(8.0)	(13.2)	(15.1)
Increase in net debt	(14.9)	(48.3)	(85.5)

- *Modest increase in net debt - £14.9m*

Pennon Group Plc

Net Debt

	As at 30 September 2004 £m	2003 £m	As at 31 March 2004 £m
Loans and finance leases			
- over one year	1,278.1	1,187.7	1,234.8
- under one year	107.2	74.3	107.0
	<u>1,385.3</u>	<u>1,262.0</u>	<u>1341.8</u>
<u>Less: investments and cash</u>	<u>(296.3)</u>	<u>(225.1)</u>	<u>(267.7)</u>
Net debt	<u>1,089.0</u>	<u>1,036.9</u>	<u>1,074.1</u>
Net gearing	118%	114%	119%

- Significant drawdowns from loans of £55m and finance leases of £26m
- Gearing stable

Pennon Group Plc

Net Interest Payable

	For the half year ended 30 September		
	2004 £m	2003 £m	2003/04 £m
Interest payable	(37.1)	(32.0)	(66.6)
Interest receivable	6.1	4.2	9.4
Net interest payable	<u>(31.0)</u>	<u>(27.8)</u>	<u>(57.2)</u>
Average rate of interest	5.7%	5.5%	5.5%
Net interest cover ⁽¹⁾	2.5 times	2.5 times	2.4 times

- *Little increase in average interest rate – benefit of swaps strategy*

⁽¹⁾ *Before exceptional item*

Pennon Group Plc

Depreciation

	For the half year ended 30 September		
	2004 £m	2003 £m	2003/04 £m
South West Water			
- infrastructure assets	7.5	7.1	14.2
- other assets	25.2	24.1	48.6
	<u>32.7</u>	<u>31.2</u>	<u>62.8</u>
Viridor Waste	14.0	10.4	20.5
Other	-	-	(0.1)
	<u>46.7</u>	<u>41.6</u>	<u>83.2</u>

Pennon Group Plc

Taxation

	For the half year ended 30 September		
	2004 £m	2003 £m	2003/04 £m
UK corporation tax	4.6	4.2	7.5
Deferred tax	4.5	0.7	3.3
	<u>9.1</u>	<u>4.9</u>	<u>10.8</u>

- *Deferred tax charge very sensitive to long term interest rates used for discounting*

Pennon Group Plc

Pensions

- Indicative net deficit at 30 September 2004 similar to 31 March 2004 - £54m
- Represents c 5% of market capitalisation
- Triennial actuarial valuation in progress
 - expected to result in annual additional costs of c £6m
 - including additional charge of c £3m under SSAP24 reflected in H1

Pennon Group Plc

IFRS

- Ongoing preparation for adoption of IFRS for 2005/06
- Significant changes from:
 - deferred tax
 - pensions
 - fixed asset accounting (“renewals”)
 - goodwill
- Overall reduction to net assets and increase in earnings volatility

- *Does not affect underlying cashflow*

Pennon Group Plc

Dividends

- Progressive dividend policy
- Interim dividend per share increased by 4.5% to 13.8p
- Dividend cover (before exceptional item and deferred tax): 2.4x (H1 2003/04: 2.3x)
- Scrip dividend alternative



South West Water

Financial Performance Summary

For the half year ended
30 September

	2004 £m	2003 £m	Change %	2003/04 £m
Turnover	157.6	146.0	7.9	291.8
Operating profit	65.3	61.1	6.9	118.9

South West Water Turnover

Increase of £11.6m (7.9%) in half year. Reflects impact of:

	£m
- tariff increase	10.5
- meter option switchers	(3.3)
- new connections	1.1
- demand	(0.5)
- other	3.8
	<hr/>
	11.6
	<hr/>

- Strong H1 performance. Last year's H2 boosted by recognition of high Summer demand

• Number of meter switchers	14,000
• Number of new customers	3,600

South West Water *Operating Costs*

For the half year
ended 30 September

	2004 £m	2003 £m	Change %
Total operating costs	92.3	84.9	8.7
Increase in operating costs due to:	£m		
- inflation	1.6		
- new works (including depreciation)	2.8		
- other (pensions, cost of sales)	4.6		
- efficiency savings	(1.6)		
	<u>7.4</u>		

South West Water Efficiency Savings

- Analysis:

	£m
• Manpower	0.2
• Power costs	0.3
• Contracted services	0.5
• Other (including raw materials, procurement and rates)	0.6
	<hr/>
	1.6
	<hr/>

- Improved efficiency banding
- Cumulative K3 saving of £20.0m per annum (£47.6m per annum since 1995)

South West Water

Operational Performance Summary

- Highest ever drinking water and river water quality
- Original “Clean Sweep” now complete – remaining UWWTD schemes underway
- Remains an industry leader in managing leakage
- Secure raw water resources
- Continued progress on service standards requiring capital investment
- 45 point OPA improvement in 2003/04 – one of the largest gains in the sector
- Continued high performance on customer “Levels of Service Indicators”
- Refocus of capital programme

South West Water Capital Programme

- Capital programme since privatisation totals just over £2bn (over 1,000 schemes): delivered to target and beating budget
- Capital expenditure half year to 30 September 2004 – £68.0m (2003 - £69.8m)
 - £95m Torbay scheme commissioned
 - Almost 300km water mains replaced/refurbished (44% higher than H1 2003/04)
- Regulatory contract K3:
 - Ofwat provision £725m (May 1999 prices)
 - targeting outperformance of 10%
 - remain on track to achieve

South West Water Regulatory Asset Value

Year end	2003 £m	2004 £m	2005 £m
At 2002/03 prices ⁽¹⁾	1620	1706	1847 ⁽²⁾
Actual/Predicted outturn prices including COPI indexation ⁽³⁾	1642	1770	1952

- Strong growth in RAV 2003-05 outstripping anticipated growth in net debt

⁽¹⁾ Source: Ofwat

⁽²⁾ Previously reported as 1784 by Ofwat

⁽³⁾ Source: South West Water

South West Water *Final Determination*

- A reduced waste water environmental improvement programme
- A bigger water mains rehabilitation programme to meet DWI requirements by 2010
- Increased levels of capital maintenance expenditure
- Asset investment to meet demand growth including two new towns
- Meeting customer concerns through targeted programmes to deal with odours at sewage treatment works and sewage flooding
- Higher running costs, including business rates, pensions, energy prices and corporation tax changes
- 113,000 optional meters by 2009-10

South West Water

Final Determination

- K price increases of 12.5%, 9.8%, 9.8%, 1.7%, 1.4% for 2005-2010; an average of 6.9% over the five years
- A capital programme of £762m at 2002/03 prices (similar to AMP3)
- Average annual operating expenditure efficiency improvements of 2.5% (water) and 2.0% (sewerage)
- Capital maintenance efficiency improvements of 6% (water) and 11% (sewerage), including frontier shift
- Capital enhancement efficiency improvement of 7% (water) and 18% (sewerage), including frontier shift
- Overall package extremely challenging
- Restructuring underway
 - c £5m exceptional restructuring costs in H2

South West Water

Final Determination

Capital Expenditure Projections (£M)⁽¹⁾

	AMP3	AMP4 Final Determination
Water Service	317	485
Sewerage Service	453	277
Total	770	762

⁽¹⁾ 2002/03 prices

South West Water Regulatory Asset Value

Year end	2006 £m	2007 £m	2008 £m	2009 £m	2010 £m
At 2002/03 prices ⁽¹⁾	1929	1994	2042	2095	2136
Actual/Predicted outturn prices ⁽²⁾	2094	2218	2329	2449	2560

- Strong growth in RAV 2006-10 reaching £2.56bn by March 2010

(1) Source: Ofwat

(2) Source: South West Water

South West Water

Ofwat response to issues raised by SWW post Draft Determination

- Level of risk
 - additional notified items covering EA charges and FRED29
 - COPI allowance
 - higher provision for power costs and pensions
- Level of operating efficiencies:

(per annum)	Water	Sewerage
Draft Determination	3.0%	2.6%
Final Determination	2.5%	2.0%

- Capital maintenance allowance
 - little increase
 - BUT
 - reduced efficiency target
- Overall package still extremely challenging



Viridor

W A S T E

Viridor Waste

Financial Performance Summary

	For the half year ended			2003/04
	30 September			
	2004	2003	Change	2003/04
	£m	£m	%	£m
Turnover ⁽¹⁾	126.7	90.7	39.7	183.1
EBITDA ⁽²⁾	28.5	21.5	32.6	43.2
Operating profit				
- before goodwill	14.5	11.1	30.6	22.7
- after goodwill	12.7	10.0	27.0	20.2
Operating margin % (before goodwill and excluding landfill tax)	15.0%	16.8%		16.9%

- Continued strong growth in turnover, EBITDA and operating profit

(1) Including landfill tax

(2) EBITDAP H1 2004/05 - £30.0m (H1 2003/04 - £22.8m)

Viridor Waste

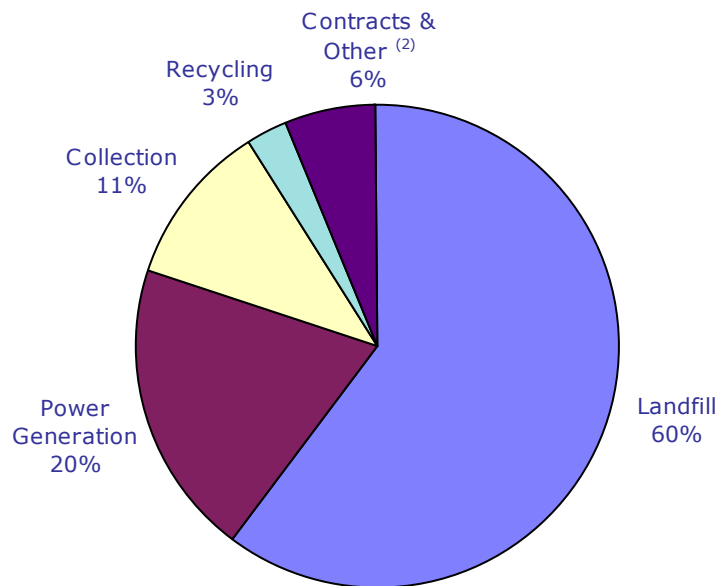
Financial Highlights

- At beginning of year projected moderate growth in operating profit before goodwill
 - after strong growth in each of the previous three years
- H1 Turnover up 40% or £36.0m (£30.7m excluding landfill tax)
- EBITDA up 33%
- Operating profit before goodwill up 31% to £14.5m
 - up 11% excluding this year's and full effect of last year's acquisitions and additional pensions charge
- Operating margin before goodwill down from 17% to 15% as mix of business changes (including Thames liquids and sludge contracts)
- Capex £18.0m (H1 2003/04 £15.7m)

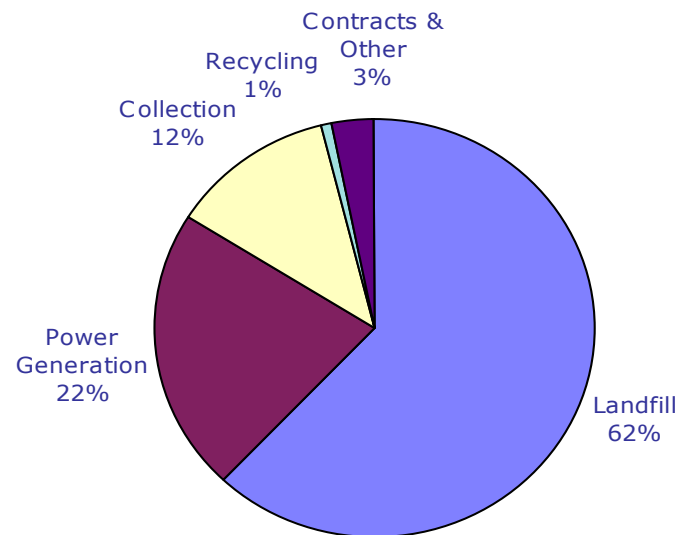
Viridor Waste

Profit Contribution by Segment (1)

Half year ended 30 September 2004



Half year ended 30 September 2003



(1) Contribution before goodwill and central overheads

(2) Including West Sussex PFI

Viridor Waste

Operational and Business Highlights - Landfill

- Landfill volumes increased by 20% to 2.3m tonnes compared to H1 2003/04
 - 12% increase excluding acquisitions
 - aided by particularly high inputs preceding the ending of hazardous waste disposal to non-hazardous landfills in July
- Gate fees increased by 5%
 - continuing to outstrip cost increases
- Current landfill capacity 80m m³ (reflecting usage of 2.7m m³ in H1)
- Not currently pursuing opportunity for dedicated hazardous waste landfill
 - long-term market demand unclear
 - aftercare in perpetuity
 - but six Viridor Waste sites now accepting stabilised non-reactive hazardous waste or asbestos

Viridor Waste

Operational and Business Highlights – Power Generation

- Output increased by 25% to 160,000 MWH
 - 9% increase excluding acquisitions
 - ROCs 53%; NFFO 47%
 - average price £50 per MWH
- Capacity increased by a further 2MW to 47MW
 - additional 3MW under construction
 - compared to 28 MW March 2002
 - Government target of 10% of electricity from renewables by 2010 and 15% by 2015 and aspiration of 20% by 2020 vs under 4% at present

Viridor Waste

Operational & Business Highlights

– Acquisition of Thames Waste Management

- Acquired for £30.7m (£28.5m net of cash in business) on 6 April 2004
- Since acquisition has won five year £20m contract for sludge handling with Southern Water
 - in addition to sludge handling for Thames Water
- 4m m³ consented void within M25
- 5MW power generation
- Five liquid treatment plants
- Projected to be earnings enhancing before goodwill this year
 - trading in line with expectations

Viridor Waste

Operational & Business Highlights

– Major Contracts

- Council integrated contracts will assume greater importance as part of Government's developing waste strategy
 - note landfill diversion targets/Landfill Allowance Trading Scheme (LATS)
- 25 year £450m integrated waste contract with West Sussex County Council commenced on 1 April 2004
 - 12 household waste recycling sites, five transfer stations and MRF
 - £25m capex in early years
 - trading in line with expectations
- Three year £10m integrated waste contract with the Borough of Poole Council commenced on 1 September 2004

Viridor Waste

Operational & Business Highlights

– New Technologies

- Continue to explore new technologies in partnership with our customers
- £2.3m in-vessel composting facility opened at Beddington landfill near Croydon in partnership with Sutton, Croydon and Merton Councils
 - substantial grant assistance from London Recycling Fund
 - potential extension into mechanical biological treatment (MBT)
- Two further £1.5m in-vessel composting plants under construction with financial assistance from DEFRA
 - at Heathfield in partnership with Devon County Council
 - at Lackford in partnership with Suffolk County Council



Pennon Group Plc



Pennon Group Plc

Summary

- Strategy clearly focused on water, sewerage and waste management
- South West Water
 - remains on track to outperform the regulatory contract to 2005
 - strong growth in RAV up to 2005, outstripping anticipated growth in net debt
 - determined to meet the challenge of K4
- Viridor Waste delivering strong growth by
 - capitalising on landfill asset base
 - exploiting landfill gas power generation opportunities
 - continuing to pursue profitable opportunities in line with the Government's developing waste strategy
- Board accepts Ofwat's Final Determination
- Board confirms continuation of progressive dividend policy