

31 May 2022

Full Year Results 2021/22

Bringing water to life

Driving sustainable growth

Susan Davy, Group Chief Executive, commented:

2021/22 has been another year of resilient performance for Pennon.

We're building momentum, executing our strategy and driving sustainable growth. At the same time, we are doing more for customers than ever before as well as delivering the step change we all want for our rivers and seas, for the Great South West, and for generations to come.

At Pennon, we believe every customer should benefit from what we do. That's why in February, we announced average bills in the South West would fall, lower now than 10 years ago, supporting the cost of living crisis.

We've also announced plans to share an additional c.£20 million of outperformance with every household in the South West, part of our unique WaterShare+ scheme, putting customers in control, choosing either to take £20 off their bill or investing in shares in Pennon Group, building on the 1 in 16 households who have already done so, in 2020.

At the same time, we're investing more where it matters most. With our largest ever environmental programme in 15 years, we are accelerating plans to make a step change in river and sea health, building on our track record of 100% coastal bathing water quality, with WaterFit, delivering a tangible difference to communities and customers in the region over the next 3 years, and with no impact on bills.

We can do all this and more, because of our relentless approach to being as efficient as possible, delivering double base RORE, reinvesting outperformance where it counts, with a robust balance sheet and an optimised financing portfolio.

We also couldn't achieve any of this without the pioneering spirit of our c.3000 employees, who see opportunities when others see obstacles, and show extraordinary care for customers, communities and each other.

Purpose-led business

- Living our values – trusted, responsible, collaborative and progressive
- Talented people delivering for customers, communities and the environment – c.3,000 colleagues serving a population of c.3.5 million
- South West Water bill cut for 2022/23 – bills lower than they were 10 years ago
- Financially supporting all our customers

Robust, resilient financial and operational performance

- Largest ever water business capital investment programme – c.£240 million in 2021/22
- South West Water – sector-leading RORE – 9.2%¹
 - c.80%² of South West Water ODIs[^] on track – delivering net reward in 2021/22
 - Sector-leading effective interest rate[^] of 3.4%
 - Continued focus on totex efficiency – supporting lower bills and enabling headroom for re-investment
- Bristol Water financial results – ahead of acquisition expectations
 - c.75%² of Bristol Water ODIs[^] on track – delivering net reward in 2021/22
 - RORE – 6.3%¹, delivering above allowed base returns
- Cumulative K7 Group outperformance of c.£150 million¹ to date – Group RORE¹ of c.8.9%
- Pennon Water Services³ – c.£19 million new contract wins, growing a sustainable national platform for business retail
- Finance portfolio strategically positioned – optimum level of index-linked debt exposure – benefiting gearing and providing headroom for growth

Investing for sustainable growth – for the benefit of all

- c.£425 million acquisition of Bristol Water – merger cleared on 7 March 2022 at Phase 1, synergies of c.£50 million identified over remainder of K7⁴ – targeting doubling of base returns by 2025
- c.£150 million additional and accelerated investment in K7
 - c.£45 million totex reinvestment to deliver a step change for coastal and river water quality – WaterFit
 - c.£20 million accelerated second issuance of WaterShare+ return to customers
 - c.£82 million accelerated and additional spend on Green Recovery, including pilots into river water quality
- Responsible gearing across the water business – 61.4%⁵

[^] Measures with this symbol are defined in the Alternative Performance Measures (APMs) as outlined on pages 60 to 64.

¹ Based on Ofwat's K7 approach to RORE, including total tax impacts and using actual average inflation for totex and financing. Fast track reward for South West Water of 10bps per annum applied over years one to five of K7

² On track or within regulatory tolerances

³ 80:20 Joint venture with South Staffordshire Group

⁴ 2020-2025 regulatory period

⁵ Post Pennon deployment of c.£55 million into the water business, notionally allocated to Bristol Water – deployment in progress

- Pennon Water Services delivering profit before tax for the first time since market opening
- Delivering Group RCV⁶ growth of >40% over K7

Shareholder returns

- Share buy-back programme – c.£200 million complete, c.£200 million to deploy
- Shareholder dividend in line with policy – growth of CPIH + 2%

FINANCIAL PERFORMANCE

| Underlying [^] | 2021/22 | 2020/21 | Change |
|--------------------------------------------------------------------------------------------------------|----------------|------------------|----------------|
| Revenue | £792.3m | £644.6m | +22.9% |
| EBITDA [^] | £383.9m | £334.7m | +14.7% |
| Operating profit | £237.2m | £215.3m | +10.2% |
| Profit before tax | £143.5m | £157.0m | (8.6%) |
| Non-underlying items before tax ⁷ | (£15.8m) | (£24.9m) | - |
| Profit before tax | £127.7m | £132.1m | (3.3%) |
| Underlying tax | (£13.9m) | (£29.6m) | +53.0% |
| Non-underlying tax | (£98.2m) | £4.8m | - |
| Profit for the year | £15.6m | £1,762.0m | (99.1%) |
| Earnings per share | | | |
| - Adjusted EPS [^] – continuing operations (adjusted for share consolidation) ⁸ | 50.2p | 47.8p | +5.0% |
| - Statutory EPS | 4.9p | 418.5p | (98.8%) |
| Dividend per share ⁹ - dividend policy | 38.53p | 35.61p | +8.2% |
| - <i>Interim dividend per share</i> | <i>11.70p</i> | <i>11.15p</i> | <i>+4.9%</i> |
| - <i>Final dividend per share</i> | <i>26.83p</i> | <i>24.46p</i> | <i>+9.6%</i> |

Resilient financial performance

- Results in line with management expectations
- +22.9% underlying revenue[^], with Bristol Water contributing £104.4 million
- +6.7% organic¹⁰ underlying revenue[^] primarily due to a recovery in non-household demand both in and out of region, and contract wins from Pennon Water Services
- (1.2%) organic¹⁰ underlying EBITDA[^] impacted by higher costs to serve driven by high levels of demand and cost pressures from macro-economic factors
- +14.7% underlying EBITDA[^] growth with contribution from Bristol Water from 3 June 2021

⁶ Regulatory Capital Value

⁷ Non-underlying items are adjusted for by virtue of their size, nature or incidence to enable a full understanding of financial performance

⁸ Adjusted earnings per share for 2021/22 and 2020/21 rebased to reflect impact of share consolidation. This calculation is outlined in the Alternative Performance Measures on pages 60 to 64

⁹ Dividend policy of CPIH + 2%. The CPIH rate used is 6.2% as of 31 March 2022. Base 2020/21 uplift for share consolidation and return of capital (from 21.74 pence to 32.61 pence). 2020/21 comparative full year dividend includes additional 3.0 pence increase to the dividend base as announced at the Full Year Results in June 2021

¹⁰ References to organic movements throughout this commentary refer to the performance of the business excluding the contribution from Bristol Water from 3 June 2021

- (8.6%) decrease in underlying profit before tax[^] with contribution from underlying EBITDA[^] growth being more than offset by increased interest charges on index-linked debt
- (3.3%) decrease in profit before tax
- +5.0% increase in adjusted earnings per share[^] (adjusted for share consolidation)⁸
- Earnings per share of 4.9 pence reflecting non-underlying impacts including deferred tax charge of £99.5 million in 2021/22 relating to the future change in tax rate (2020/21 earnings per share of 418.5 pence including the £1.7 billion profit on disposal)
- Sector-leading dividend growth of 8.2% with full year dividend per share up (CPIH +2%) to 38.53 pence.

A full reconciliation to the statutory reported results is included in item (i) in the Alternative Performance Measures on pages 60 to 64 of this announcement.

Presentation of results

A presentation of these results hosted by Susan Davy, Group Chief Executive and Paul Boote, Group Finance Director, will take place at London Stock Exchange, 10 Paternoster Sq, London, EC4M 7LS at 09:00am (GMT), today, 31 May 2022.

The presentation will be available as live webcast and can be accessed here: <https://www.pennon-group.co.uk/investor-information>

The presentation will be immediately followed by a live Q&A which will also be available via conference call facility. Details are included below:

| | |
|--------------------------------|------------------|
| United Kingdom: | 0800 640 6441 |
| United Kingdom (Local): | 020 3936 2999 |
| All other locations: | +44 20 3936 2999 |
| Conference passcode: | 623854 |

For further information, please contact:

| | | |
|-------------------|----------------------------|---------------|
| Paul Boote | Group Finance Director | 01392 443 168 |
| Jennifer Cooke | Head of Investor Relations | |
| James Murgatroyd | Finsbury Glover Hering | 020 7251 3801 |
| Harry Worthington | | |

OPERATIONAL PERFORMANCE

Delivering for customers, communities and the environment across the Great South West

Performance across the Group continues to be operationally resilient, delivering against South West Water and Bristol Water's business plan commitments, and driving growth at Pennon Water Services, realising benefits for all stakeholders.

In June 2021 we announced the acquisition of Bristol Water, increasing the Group's RCV by c.16%. The merger of Bristol Water with South West Water was reviewed by the Competition and Markets Authority (CMA), in line with standard practice. Throughout this review process, we worked collaboratively with Ofwat and the CMA to demonstrate the benefits for customers, communities, and shareholders arising from the merger. During the period from June 2021 to the point at which the CMA provided merger clearance at Phase 1 on 7 March 2022, South West Water and Bristol Water operated independently of each other, in line with CMA requirements.

The integration of the water businesses is now underway, with the focus of sharing best practice across the Group.

Bringing together the best of the best

The acquisition of Bristol Water increases the population served across the Group to over 3.5 million, with services delivered by a team of c.3,000 talented colleagues. Bristol Water embodies many of Pennon's values, our approach to stakeholder engagement and collaboration, providing a solid foundation for the integration.

As we did with Bournemouth Water, we are retaining the local presence, operations and valuable Bristol Water brand which is very relevant for customers and communities given Bristol Water has just celebrated its 175th anniversary, building on that trusted heritage.

The merger and integration of South West Water and Bristol Water unlocks specific benefits for all stakeholders. We have embarked on a 24-month integration programme, deploying our proven integration blueprint which is focused on:

- creating common systems and processes
- unlocking economies of scale
- driving supply chain efficiencies
- sharing environmental best practice
- delivering even better customer service.

There are three streams of integration, moving across three phases: corporate and shared services, operations, and customer services. We are targeting more efficient central governance and support structures, alongside combining operational and customer service excellence.

We have identified a full run rate of synergies of c.£20 million per annum by 2025, with c.£50 million targeted cumulatively over the remainder of K7. The scale of which is broadly comparable to the synergies delivered through the Bournemouth Water acquisition. Financing outperformance will be realised over a longer horizon as Bristol debt is refinanced. As was the case with Bournemouth Water, the benefits are multiple and we are focused on ensuring we can unlock service improvements alongside efficiency performance.

A greater stake and a say for customers in the Great South West

Building on the successful launch of our WaterShare+ scheme in 2020 which saw one in 16 households in the region become shareholders, we are delighted to be accelerating the next issuance of our unique WaterShare+ scheme in 2022/23¹¹. c.£20 million of outperformance will be used to underpin our commitment not just to South West Water and Bournemouth Water customers but now also Bristol Water customers – enhancing the community contract already in place with them.

Sustainability at the heart of our business

We are committed to being a responsible business for all our stakeholders, achieving improved environmental, social and governance (ESG) performance. Demonstrating our role in society is crucial in maximising the value we create for stakeholders, and we are proud that our ongoing commitment to do the right thing, in the right way continues to deliver sustainable results. Our commitment to maintaining the highest standards is demonstrated through our strong and improving ESG performance metrics.

We are also partnering across 11 innovation projects and underpinning this, is our £20 million joint venture with the University of Exeter, where we're collaborating on the first purpose-built, trans-disciplinary research centre in the water sector, focused on the most pressing challenges that impact upon the provision of safe and resilient water and wastewater services in the UK and overseas.

Our existing environmental plans to 2025 are already delivering significant benefits for the environment. We are well underway with the delivery of our c.£1.4 billion capital programme in K7 across the Group – our largest environmental investment programme in 15 years. This includes our Green Recovery and Net Zero 2030 plans, delivering nature-based solutions and pilots to shape future investment plans, along with accelerating renewable energy generation to c.50% by

¹¹ Subject to shareholder approval at the Pennon AGM on 21 July 2022

2030. Alongside this, WaterFit will see us reinvest c.£45 million totex efficiencies achieved to date in K7 to deliver a step change for river and coastal water quality.

We continue to build on the success of our pioneering Sustainable Financing Framework, having raised c.£300 million through the Framework since 31 March 2021. We were also pleased to have achieved Fair Tax accreditation again this year, recognising our responsible approach to tax.

At Pennon, we believe our people are our best asset and are delighted to have been recognised as the winner in Britain's Most Admired Companies (Utilities) for the second year running. This award demonstrates our commitment to engaging employees in our strategy and the important role they play in delivering it. We are also delighted that for the second year running we have officially been accredited as a Great Place To Work. The survey measures effectiveness in a range of categories including innovation, maximising human potential, values, leadership effectiveness and wellbeing and we are pleased to have achieved our highest ever participation rate of 85%.

We are proud to be a member of 'The 5% Club' – investing in the next generation through embracing an 'earn and learn' culture and committing to having at least 5% of our employees on structured graduate or apprenticeship programmes, a target that we are currently exceeding. Our graduate programme is well underway, with a new intake of 28 graduates during the year, who represent our most diverse intake ever, and we are on track to recruit 100 graduates over K7. We continue to create new apprenticeships and having added 209 apprenticeships since 2020, we are ahead of schedule in reaching our 2025 target of 500. We are also proud to support the #10000blackinterns initiative and the Change The Race Ratio, as well as having increased gender diversity across the Group with >30% female employees.

Supporting our customers

South West Water's New Deal business plan 2020-25 was developed with customers, for customers. In helping to shape our business plan, customers told us they want a resilient and reliable service, and a fair and affordable bill. Through Covid-19, many of our customers saw significant additional pressures on their finances, and teamed with the current rising inflationary environment, our commitment to support customers has never been more important.

We have worked hard to deliver quality services at an efficient cost, so that bills remain as low as possible. During the year we announced that bills for 2022/23 would fall, meaning that whilst the majority of utilities are increasing prices, our average bill will be reducing at this critical time. South West Water's bills are lower in real terms than they were 10 years ago thanks to our continued focus on driving efficiency through innovation. Alongside this, the acquisition of Bristol Water will afford future bill reductions for Bristol Water customers.

Alongside ensuring our bills remain as low as possible, our innovative WaterCare programme, introduced in 2007, continues to offer support to customers through a number of initiatives including direct account reviews and benefit entitlement checks. This has been achieved through a range of affordability support measures including a programme of physical and virtual home visits to help customers ensure they are receiving all eligible benefits, meaning they are financially better off. In addition, we have been working in partnership with organisations such as social housing providers and carer organisations to ensure that our schemes are promoted and easy for our customers to access.

In 2021/22, there was a c.4% increase in customers benefiting from one or more of South West Water's affordability initiatives, bringing the total to c.70,000. These initiatives include discounts to bills or a level of bill certainty to suit customers' circumstances. We are targeting a further increase in 2022/23 as we work to address water poverty for our customers by 2025, in line with South West Water's Board Pledge.

For our Bristol Water customers, we offer three discounted tariffs to make sure customers who find it hard to pay their water charges are given the help they need, with over 21,000 customers receiving assistance through these measures, an increase of c.4% on the previous year. In addition to the social tariff schemes, almost 4,000 households are currently benefiting from the 'Restart' scheme to help clear their water bill debt. During 2021, Bristol Water introduced 'Covid Assist' which provides support to customers who have been unexpectedly thrown into severe financial hardship. These customers can receive help with their bill for 6 months before applying for support on a longer-term basis if needed. Bristol Water's work with debt advice partners continues to be key to promoting the help available to customers.

As a result of these initiatives, since the start of this regulatory period we have unlocked almost £22 million of support for customers across the Group.

At Bristol Water an additional c.8,000 households have been included on the Priority Services Register (PSR) during the year, taking the number registered to c.21,000. Encouragingly, 89% of Bristol Water's vulnerable customers rated the service they receive through the PSR as 'very satisfied' or 'satisfied' compared to the 2021/22 target of 85%. This measure is in line with the progress made against Bristol Water's published Vulnerability Action Plan, which is reviewed by the Bristol Water Challenge Panel.

Striving for service excellence

During the year, South West Water saw a c.60% reduction in total complaints, maintaining our position as an upper quartile company and reflects customer experience improvements implemented along with shortening resolution timescales.

Bristol Water has more than halved the total number of complaints during the year. Complaint resolution and handling is a key focus of Bristol Water's customer experience strategy, and root cause information feeds directly into future improvements to prevent repeat complaints.

Customer satisfaction as measured by Ofwat's Customer Measure of Experience (C-MeX) presents a good opportunity for us to share best practice across the Group. At South West Water this is an area where we're focusing our improvement efforts, being ranked 12th in 2021/22. Improved customer communications, using new channels convenient to our customers and a new education campaign form part of our plan to advance performance in this area.

Bristol Water continues to deliver strong C-Mex performance, ranking 6th in the industry – continuing its strong performance from the previous year. We have managed a variety of projects to achieve this performance, which will continue into 2022/23, including the 'In their shoes' campaign, which has been embedded within the culture of our customer facing operational teams. During the latter part of the year, Bristol Water increased the focus on messages to help customers with their bill, which included the launch of the two year 'Money Back Guarantee' aimed at providing confidence to customers to trial a meter for two years.

Our D-MeX performance, measuring satisfaction from developer customers such as house builders for both South West Water and Bristol Water is forecast to be close to the average for the industry, presenting an opportunity for targeted improvements including greater stakeholder engagement through face-to-face and virtual workshops and events.

R-MeX is a relatively new survey which measures retailer satisfaction in the business market with wholesaler services. In the most recent survey, the performance of both South West Water and Bristol Water is robust, with both above the current average for the industry.

Playing our part in the community

South West Water's revamped school's education programme is aimed at developing and delivering classroom material to local schools. This programme is focused on teaching school children the importance of water conservation and environmental protection, illustrating the part they can play through being careful with what is discarded through the wastewater network. Through this programme we have directly taught c.5,000 pupils about where our clean water comes from and how wastewater is treated.

In the coming year we are extending our reach by working with our partners, including South West Lakes Trust, and our ambition in this space is to engage with more and more pupils outside the school term. We're also creating new partnerships to support our ambition to drive behavioural change across the region.

We continue to support communities with funding available for community groups through both South West Water and Bristol Water, including South West Water's Neighbourhood Fund and Water Saving Community Fund, and Bristol Water's Community Fund, administered by the Quartet Community Foundation, supporting a range of initiatives across the Bristol region.

Bristol Water's local community satisfaction target recognises the importance of working together with local stakeholders to jointly tackle the issues which the city faces. This means challenging ourselves on the way that we work to deliver a safe and reliable supply to customers, so that we can maximise additional economic, environmental and social value. This approach is underpinned by Bristol Water's Social Contract, which provides the framework and governance process for the delivery of this wider public value.

Clean safe, reliable drinking water

Across the Group, we are committed to ensuring the continuous supply of clean, safe and reliable drinking water, whilst protecting the natural resources within the Great South West. Our dedicated teams and ongoing investments ensure that we are able to respond to challenges, such as those posed by the Covid-19 pandemic and severe weather – such as Storm Eunice in February 2022.

Investing to secure resilience, now and into the future

At South West Water, in 2021 we celebrated a silver jubilee – the 25th consecutive year without water restrictions. Bournemouth Water's track record of no water restrictions was also successfully maintained. Despite high demand over the year and hot weather over the summer we successfully managed our water resources, taking advantage of the wetter periods over the winter. This enabled us to replenish water storage and as we enter the summer period our water resources are in a robust position with reservoir storage at c.93% at 31 March 2022.

We continue to look for strategic value enhancing opportunities in this area having recently procured a site for development of a new reservoir on Bodmin Moor, Devon.

At Bristol Water, the drought risk measure did not achieve its target for the year due to the ongoing higher than forecast distribution input and unplanned outages. However, Bristol Water's water resources remain in a robust position with reservoir storage at the end of March 2022 at c.93%.

Water quality

The Compliance Risk Index (CRI) score as reported by the Drinking Water Inspectorate (DWI) measures water quality compliance. Performance across the Group, which missed 2021/22 targets, was impacted by one-off events in 2021/22, however underlying performance remains strong. Continued investment in research and implementation of advanced treatment technologies, including ceramic membranes and granular activated carbon is designed to ensure compliance measures improve in future years.

Further enhanced maintenance and resilience improvements are being delivered across all our water treatment works as part of our site MOT programme to ensure we proactively intervene before failures occur.

Leakage

We recognise that the prevention of water being lost through leakage from our pipes and assets is a key issue for all customers and is something we work continuously to reduce. Across the Group in 2021/22 leakage levels reduced by c.7%.

At South West Water, the specific investments made since the start of the regulatory period, coupled with the launch of our targeted action plan are delivering results. Improved leakage performance for the year has resulted in us achieving our 3-year average target and represents a c.8% reduction on prior year performance. Whilst we know there's still more to do to find, fix and prevent leaks on our network, we're encouraged by the progress we've made to date, and continue to focus on delivering further improvements to achieve a 15% reduction over the K7 period.

Bristol Water maintained its strong leakage performance during the year, reflected in a 5% reduction on prior year performance. A focus on customer leaks along with out-of-hours work has played a significant part in driving stubborn leakage areas down. Bristol's current leakage strategy, delivering sector-leading performance, is expected to continue for the remainder of K7.

Mains repairs

Decreasing the number of mains failures is vital to ensuring we maintain a continuous supply of water to our customers.

The work to optimise the operation and control of our network by pressure management and other 'network calming' activities, along with targeted replacement of sections of water mains with higher failure rates has led to a significant reduction in the number of mains failures across the year, and across the Group. We are pleased to have significantly reduced the number of reactive repairs across the Group, delivering a c.30% reduction across South West Water and Bristol Water.

Unplanned outages

Water treatment unplanned outage is a new measure for the K7 regulatory period and provides a means of assessing asset health (primarily for non-infrastructure, above ground assets), for water abstraction and water treatment activities. It tracks the temporary loss of production capacity across all water treatment works, resulting from unplanned breakdowns and asset failure. The Group is performing well in this area, with both South West Water and Bristol Water outperforming the industry wide target.

South West Water's performance in 2021/22 has remained strong and is founded on effective investment and maintenance regimes, ensuring that unplanned failures are minimised. This in turn minimises the risk of any production outages resulting in service impacts for our customers.

At Bristol Water, we continue to aim to fix all outages within the working day however, due to some extreme weather events, such as storm Eunice, and supply chain issues in obtaining replacement parts, there has been an increase in unplanned outage over 2021/22, though performance still remains favourable to the industry-wide target.

Minimising customer supply interruptions

As a Group, we understand the inconvenience that supply interruptions can cause.

At South West Water, during 2021/22 performance was impacted by two large events, including one in Gunnislake, Cornwall and a significant third-party incident¹², and reflects the way in which performance against this target can be impacted by one-off issues. On an underlying basis South West Water's core performance remains robust with our strategy of a dedicated, in-house supply continuity and alternative water supply team making long term improvements to customers, reducing the number and duration of supply interruption events.

Bristol Water have made a number of changes in their approach to supply interruptions over the past three years to improve performance. The impact of these changes is now being seen, with Bristol Water outperforming their 2021/22 target.

Protecting the environment – robust wastewater delivery

Our wastewater services, delivered by South West Water, continue to drive improvements through innovation by constantly seeking out new ideas, pioneering and piloting new technologies with a focus on nature-based solutions, where possible, and by enhancing governance and working in partnership with others.

Reducing flooding incidents

During 2021/22 the number of internal sewer flooding cases decreased year on year by c.40% in comparison to the prior year. This is a significant outperformance against target and places us as one of the best performers in the industry on this measure. External sewer flooding events also decreased, with a 6% year on year reduction – maintaining our strongest performance yet, supported by the use of artificial intelligence, such as Meniscus, enabling proactive interventions based on predictive analytics.

¹² In late August 2021 a third-party utility company, performing work unconnected with South West Water, damaged mains supply pipes at Carland Cross in Cornwall, causing a localised loss of supply. Any impact from this event in terms of ODI mechanism remains under evaluation.

We have a multi-faceted approach to improve our performance on sewer flooding with key activities including the installation of sewer-depth monitors at key points within the network to alert us to potential issues, enhanced data collection and analysis, and HYBACS technology to help peak network demand. This informs our forward plans for identifying repeat flooding risk areas and locations requiring further sewer cleansing and defect remediation.

Sewer Collapses

The number of sewer collapses reduced by c.30% compared to the same period last year and represents an area of excellence, with our performance already exceeding the 2025 target. The downward trend in the number of collapses reflects a relentless drive to investigate, clean, and repair sewers. We are using artificial intelligence to produce automated sewer condition surveys, and to detect and code faults accurately, resulting in faster proactive repairs at a lower cost.

Pollution incident reduction plan delivering results

South West Water's Pollutions Incident Reduction Plan, launched in September 2020, continues to deliver results. This level of improvement has continued into 2021¹³, with a one third reduction in pollution incidents recorded compared to the previous year, reflecting our best ever performance in 10 years.

2021/22 saw the completion of the first phase of 210 'hotspot' interventions where issues identified at sites with multiple previous issues were fixed during the year. A second phase has been identified for resolution in 2022 which, in addition to the other planned maintenance and enhancements to assets, will support our trajectory to improve overall performance and target continued reductions in pollution incidents.

In addition, we continue to collaborate with others in the industry to share best practice and operational insights and are enhancing our root cause analysis to deliver greater insight into identifying risks. Alongside this we are helping customers to understand how their behaviour impacts on our assets and ultimately their local environment.

We recognise that there is still more to do in this area as our targets become more stringent, impacting our relative EPA performance. The investments and interventions we are making support our trajectory to improve our overall position, achieving a 4-star EPA rating by 2024. Our steadfast focus remains in this area as we work to deliver a meaningful step change in performance.

Enhancing the environment in the Great South West

Since the publication of South West Water's Final Determination, there has been a marked shift in the focus on the environment from customers, the media, Government and other stakeholders.

¹³ Calendar year measure

During 2021 we saw COP26 in Glasgow and the G7 meeting in Cornwall, with climate change at the forefront of discussions.

Improving river and coastal water quality has taken centre stage, as water-based recreation, such as wild swimming and paddle boarding, have become more popular, and the pandemic has strengthened the bond our customers want to have with more open green and blue spaces, now and for generations to come.

WaterFit – protecting rivers and seas together

A key concern and priority of our customers is protecting and enhancing the beautiful environment in the Great South West and we are determined to play our part in improving river and coastal water quality. Our new investment programme, 'WaterFit' is focused on protecting rivers and seas together, bringing together existing plans to deliver multiple benefits, as well as going further, faster - piloting and proving the case for future investment in preparation for the next regulatory period, PR24.

WaterFit will see us nurturing healthy rivers and seas, reducing our impact on rivers by one third by 2025¹⁴, and maintaining our excellent bathing water quality standards all year round. We are also developing plans to target zero harm on river quality by 2030. Our WaterFit plans have been built around six pledges underpinned by a range of specific targets, including targeting changes on around 200 treatment works, pumping stations and storm overflows, increasing capacity across our infrastructure by the equivalent of around 20 Olympic swimming pools, and reducing spills from storm overflows to an average of 20 per year, per overflow. c.£45 million of additional investment for WaterFit will be funded through totex efficiencies delivered to date during the K7 regulatory period, with the achievement of our existing environmental ODIs continuing to be a priority.

Delivering in our catchments

Our pioneering catchment management approach has now been in place for over 15 years and continues to be fundamental to helping unlock environmental challenges across the region. To date we have improved over 95,000 hectares including c.300 hectares of peatland, and we undertake catchment management across c.80% of our region. These activities lead to reduced ammonia and phosphate run-off thereby improving overall river quality. We're also well advanced with our plans to plant 250,000 trees by 2025, more than doubling our original target of 100,000, which we achieved four years early. We planted c.50,000 trees this year bringing the total to date to c.150,000.

Record quality levels recorded at our bathing waters

In the South West we have over 860 miles of coastline to protect, representing over one third of the UK's bathing waters. This is something we, and our customers, have always valued and prioritised,

¹⁴ Reducing the rivers where we are responsible for not achieving good ecological status from c.19% to c.12%

working tirelessly across the region to improve bathing water quality, which now for the first time ever, has achieved 100% water quality, as measured by the Environment Agency.

We have advanced investment to deliver six bathing water enhancements ahead of schedule – bringing the total delivered to 2022 to eight schemes. We are particularly pleased that Combe Martin retained bathing water designation as a result of our collaborative mixed investment approach and interventions including nature-based solutions, restoring, protecting and enhancing land to reduce pollution levels running off into our seas.

Improvements on the Isles of Scilly

South West Water commenced operating the water and sewerage services on the Isles of Scilly in April 2020, at the very start of the Covid-19 pandemic.

During 2021/22 investments have been delivered on the islands that include improved communication and control systems on key assets, and an enhanced water sampling programme which provides improved water quality data that will be used to design the new water treatment systems the islands require.

Recognising the importance of water efficiency, we completed the rollout of our smart metering programme with c.90% of customers now metered. This forms part of a focus on remote operations and communities. During the year we improved water treatment for all customers on St Mary's, along with the completion of a programme of tank cleansing. We have also bolstered our teams, recruiting locally to strengthen the island based team that effectively manage these critical services.

All specified targets agreed with the DWI and the Environment Agency have been achieved, in addition to extra commitments made to the DWI based on further water quality data that has been gathered since April 2020.

The programme now moves to the next stage of detailed design regarding replacement treatment processes that provide improved resilience and reduced environmental impacts.

Green Recovery – piloting for success

Our c.£82 million Green Recovery initiative, developed with customers and stakeholders, has been designed to deliver benefits for customers, society and the environment.

As part of our Green Recovery initiative, we are extending storm overflow monitors¹⁵ so that all c.1,600 overflows on our network will be monitored by December 2023 (c.80% installed to date) giving us important data on the number and duration of spills across the entire network. Alongside this we are also trialling sewer separation which allows us to assess the sustainability of this activity

¹⁵ Event Duration Monitors (EDMs)

in reducing storm overflows during heavy rainfall, ultimately helping to inform where to target investment in this regulatory period and the next.

Our inland river bathing water pilots on the Rivers Dart and Tavy are progressing. These pilots will enable us to test the implications, costs and benefits of achieving bathing water designation and deliver specific asset enhancements where necessary to achieve these aims. We are engaging with stakeholders in the area and have commenced the installation of monitors to measure water quality.

Four schemes are now underway focused on the removal of phosphorous and ammonia, including investment in additional storm storage, in line with our targeted programme.

Recognising that there are many contributing factors to river water quality including farming and industry, we are taking the lead in supporting all those who might be a source of river water pollution. We are also on track to reduce the impact of our own assets and processes by one third by 2025.

Net Zero 2030

Our Net Zero 2030 journey is underway across the Group, with investment focused on delivering reduced carbon emissions and increasing renewable energy generation. As we target Net Zero by 2030, we are enhancing our understanding of carbon in our business and processes, so that we can optimise our assets and embed carbon into our decisions.

South West Water's Net Zero plan is driven by a combination of activities, structured through three key pillars – bringing wider benefits to the South West.

- Sustainable living – reducing emissions through operational practices, including our on-site water usage, increasing energy efficiency and using lower carbon fuel sources
- Championing renewables – investment is underway to support the achievement of 50% renewable energy generation at our sites by 2030. During the year we accelerated plans to roll out additional solar photo-voltaic (PV) panels across many of our sites, including our flagship water treatment works, Mayflower. These investments will help to double our renewable generation capacity to over 10%
- Reversing carbon emissions – working in partnership to deliver natural carbon sequestration through peatland restoration and tree planting. We are making good progress towards our target of restoring 1,000 hectares of peatland.

Bristol Water's Net Zero 2030 strategy is built around four pathways to reduce our carbon footprint.

- More efficient use of water – continuing to reduce leakage from our pipes and encouraging customers to use less water, offsetting the increase from a growing population in our area
- More efficient operations – further reducing the amount of energy used to supply our customers by optimising the design and operation of our systems

- Switch to low or zero carbon sources of energy – switching to renewable energy sources
- Remove carbon from the atmosphere – carbon offsets and sequestration.

Customer and shareholder returns

RORE outperformance underpins the Group's sustainable dividend policy whilst enabling the reinvestment of efficiencies and keeping customer bills low.

South West Water's strong operational and financial performance has contributed to a sector-leading RORE of 9.2%¹⁶ with outperformance in all areas in 2021/22.

Bristol Water has delivered a RORE of 6.8%¹⁶, also delivering outperformance in all areas in 2021/22. The identified synergies across the Group of c.£50 million over the remainder of K7 will result in a doubling of base returns for Bristol Water.

Group RORE of c.8.9%¹⁶ reflects c.£150 million¹⁷ of cumulative outperformance to date.

Outcome Delivery Incentives[^]

In 2021/22 South West Water achieved c.80%¹⁸ of its ODIs across a broad range of challenging bespoke, common and comparative measures – in line with performance in 2020/21.

Ten ODIs continue to represent areas of excellence having achieved their 2025 target early, with a further 25 outperforming their 2021/22 target or on track.

We have delivered a significant step change in pollutions performance in line with our Pollutions Incident Reduction Plan, reducing wastewater pollution incidents by over a third, and whilst still an area of focus the financial penalty is substantially reduced from 2020/21.

Overall, financial ODI performance for South West Water for 2021/22 has improved significantly from the prior year, resulting in a net reward of c.£0.6 million (2020/21 net penalty of c.£10.4¹⁹ million), reflecting an annual equivalent RORE[^] outperformance of 0.1%.

Bristol Water achieved c.75%¹⁸ of its ODIs, with three ODIs representing areas of excellence and a further 19 outperforming or on track with their 2021/22 target.

Bristol Water has also delivered net financial reward based on their ODI performance for 2021/22, delivering c.£0.4 million net reward (2020/21 net penalty of c.£1.8 million), reflecting an annual equivalent RORE[^] outperformance of 0.1%.

¹⁶ Based on Ofwat's K7 approach to RORE, including total tax impacts and using actual average inflation for totex and financing

¹⁷ Outperformance reflects c.£94 million totex efficiency, c.£67 million financing outperformance, net of c.£11 million ODI net penalty and c.£1 million tax. WaterShare equivalent total outperformance c.£190 million to date.

¹⁸ On track or within regulatory tolerances

¹⁹ Reflects final outturn of prior year ODI performance, consistent with Ofwat reporting

Financing

Our efficient financing strategy continues to drive outperformance with South West Water's effective interest rate[^] at 3.4% (2020/21 2.5%), lower than Ofwat's nominal cost of debt. While recent increases in inflation are driving an increase in finance costs of index-linked debt, we continue to outperform the cost of debt allowances through our flexible financing strategy and the company's diverse debt portfolio, with a relatively lower level of index-linked debt compared to the industry average.

Bristol Water's level of index-linked debt is in line with the industry average at around 50%. With an effective interest rate[^] of 5.6%, this has still delivered financing outperformance in the year.

Total expenditure savings (Totex[^])

South West Water's overall cumulative net efficiency savings in the regulatory period to date are c.£87 million²⁰. Whilst the elevated inflationary environment is placing pressure on costs, we continue to focus on efficient totex delivery, supported by our pioneering approach to innovation across the Group.

Bristol Water has delivered totex outperformance of c.£7 million²¹ on a cumulative basis. The c.£50 million synergies identified across the Group following the acquisition of Bristol Water over K7 will contribute to a doubling of base returns.

Reflecting the above, overall totex for the water represents a c.10% efficiency, net of increased expenditure on wastewater pollutions and leakage, reflecting efficiencies and advancements across the Group.

Return on Regulated Equity

The table below summarises the 2021/22 and cumulative RORE[^] position for both South West Water and Bristol Water.

²⁰ Based on Ofwat's approach to RORE using average actual inflation (2020/21 – 0.8%, 2021/22 – 3.7%)

| | Ofwat RORE ²¹ | | WaterShare RORE ²² | |
|---------------------------|--------------------------|---------------|-------------------------------|---------------|
| | 2021/22 | | 2021/22 | |
| | South West Water | Bristol Water | South West Water | Bristol Water |
| Base return | 3.9% | 4.4% | 3.9% | 4.4% |
| Totex | 0.8% | 0.7% | 0.8% | 0.8% |
| ODI | 0.1% | 0.1% | 0.1% | 0.1% |
| Tax | 0.5% | (0.1%) | N/A | N/A |
| Financing | 3.9% | 1.7% | 3.9% | 2.1% |
| Total RORE | 9.2% | 6.8% | 8.7% | 7.4% |
| <i>K7 cumulative RORE</i> | <i>7.9%</i> | <i>4.9%</i> | <i>8.2%</i> | <i>6.3%</i> |

Growing a sustainable national platform for business retail

Pennon Water Services³, with a market share of c.6% continues to deliver on its growth ambitions, winning c.£19 million of new contracts during 2021/22. Pennon Water Services' strategy is to engage proactively with its customer base, and to continue to win new, quality contracts.

Through a simple, transparent and competitive service offering, Pennon Water Services attracted businesses of all sizes and sectors during the year, including Essar Oil and Bourne Leisure, along with strategic water users such as GSK and Rolls Royce, recognising the value from their relationship with Pennon Water Services by renewing their retail contracts.

The business focus upon securing contracts from high volume strategic water using sectors, such as manufacturing, supported Pennon Water Services' resilience through the Covid-19 pandemic as these sectors continued to operate in line or in some cases above pre-pandemic levels of consumption. Overall non-household demand which had been impacted due to Covid restrictions on customer's operations in some sectors, has returned to near pre-Covid levels across the majority of sectors.

Pennon Water Services customers continued to recognise the value and support provided by giving the business a high rating through the independent review site Trustpilot, being rated as excellent - 4.8/5, reflecting efforts to refine and improve customer service.

Through our acquisition of Bristol Water we gained a 30% share in water2business – led by a strong team who are also focused on delivering an outstanding customer experience, currently with a Trustpilot score of 4.9/5. Serving c.160,000 customers, and with a c.6% market share,

²¹ Based on Ofwat's K7 approach to RORE, including total tax impacts and using actual average inflation for totex and financing

²² Watershare RORE - financing outperformance is based on the outturn effective interest rate translated into a real rate using a forecast average inflation assumption of 3.1% CPIH. Base RORE for South West Water includes fast track reward of 10bps applied over years one to five of K7

water2business' offers tailored water and wastewater management helping customers improve efficiency and deliver savings.

Well positioned for the future

At Pennon we have the headroom and capacity to respond with agility when it matters most. We have always focused on having an agile and efficient financing strategy and with the water company net debt/RCV gearing at 61.4%, and forecast to fall further over K7, we are well placed for investment.

We also continue to drive efficiency and performance across financing and totex. The financing at Pennon and the combined water business is the most efficient in the sector and South West Water's effective interest rate is consistently one of the lowest in the industry and significantly below Ofwat's allowed nominal cost of debt. This outperformance provides headroom for optionality, for reinvestment or sharing of benefits with customers, lowering their bills at a time when they most need it most.

Now that the Bristol Water integration is underway, our approach is all about taking the best of the best whether performance, process, talent or efficiency. The synergies that we have identified will enable us to realise efficiency savings across the Group of c.£50 million to 2025, leading to a doubling of base returns for Bristol Water.

Supporting our plans for organic growth, we are reinvesting where we see the opportunity. Having delivered cumulative outperformance of c.£150 million²³ across the Group so far in K7, we are reinvesting and accelerating new projects as well as sharing benefits with customers.

Our long-term plans for PR24 and beyond are being developed to maximise public value – adaptive plans focused on service, society and the environment, built to recognise the uncertainties of climate change and population growth.

Pennon's agility and innovative approach to driving efficiency has positioned the Group well, adopting a twin-track approach, pursuing both organic and acquisitive growth. A key parameter of measuring growth is our Regulatory Capital Value – with this being the basis of future revenues and central to our gearing and debt position. Over K7 we expect RCV to have increased by over 40% from a combination of organic and acquisition led growth, broadly split 50:50 between the two, along with the impact of the higher inflationary environment.

²³ Based on Ofwat's K7 approach to RORE, including total tax impacts and using actual average inflation for totex and financing. Fast track reward for South West Water of 10bps per annum applied over years one to five of K7

FINANCIAL PERFORMANCE

During this financial year, we have implemented our commitments to return value to our shareholders and stakeholders following the sale of Viridor, having paid a special dividend of c.£1.5 billion, commenced a share buy-back programme of up to c.£400 million, and making further contributions to our principal pension scheme. We have extended our investment in UK water with the acquisition of Bristol Water and have committed further investment to fund the water business in support of our Green Recovery initiative.

Bristol Water has contributed to the financial results since 3 June 2021, with financial performance ahead of management expectations. The Competition and Markets Authority cleared the non-household aspect of the acquisition in November 2021, with full clearance for the merger of the wholesale water businesses granted on 7 March 2022.

| Underlying[^] | 2021/22 | 2020/21 | Change |
|--------------------------------------------------------------------------------------------------------|--------------------------|--------------------------|----------------|
| Revenue | £792.3m | £644.6m | +22.9% |
| Operating costs | (£408.4m) | (£309.9m) | (31.8%) |
| EBITDA [^] | £383.9m | £334.7m | +14.7% |
| Depreciation and amortisation | (£146.7m) | (£119.4m) | (22.9%) |
| Operating profit | £237.2m | £215.3m | +10.2% |
| Net interest charge | (£93.7m) | (£58.3m) | (60.7%) |
| Profit before tax | £143.5m | £157.0m | (8.6%) |
| Non-underlying items before tax ⁷ | (£15.8m) | (£24.9m) | - |
| Profit before tax | £127.7m | £132.1m | (3.3%) |
| Underlying tax | (£13.9m) | (£29.6m) | +53.0% |
| Non-underlying tax | (£98.2m) | £4.8m | - |
| Discontinued operations | - | £1,654.7m | - |
| Profit for the year | £15.6m | £1,762.0m | (99.1%) |
| Earnings per share | | | |
| - Adjusted EPS [^] – continuing operations (adjusted for share consolidation) ⁸ | 50.2p | 47.8p | +5.0% |
| - Statutory EPS | 4.9p | 418.5p | (98.8%) |
| Dividend per share ⁹ – dividend policy | 38.53p | 35.61p | +8.2% |
| Capital investment | £240.9m | £205.2m | +17.4% |
| - South West Water | £203.4m | £168.2m | +20.9% |
| - Bristol Water | £37.0m | - | - |
| - Other | £0.5m | £0.3m | +66.7% |
| | 31 March 2022 | 31 March 2021 | |
| Total Group net (debt)/cash | (£2,682.9m) | £64.3m | |

Robust financial performance

Financial performance across the Group has been robust with a strong contribution from the newly acquired Bristol Water, with performance in line with management expectations.

The Group's revenue has increased from £624.1 million to £792.3 million, with the prior period including a £20.5 million WaterShare+ non-underlying reduction to revenue. The Group's underlying revenue[^] has increased from £644.6 million to £792.3 million, an increase of c.23%, with Bristol Water contributing £104.4 million of the increase in the year ended 31 March 2022.

Organically¹⁰, underlying revenues[^] have increased by 6.7%. The Covid-19 pandemic led to a substantial population increase in the South West with continued higher levels of household demand. Alongside this, as restrictions eased, businesses have increased activity, resulting in increased water usage both in and out of our region, as well as growth in developer services activities.

Cost pressures from the macro-economic environment, alongside the increased demand, which includes the impact of a sustained population increase in the region, have resulted in higher costs to serve.

In the Bristol Water region, demand levels have been relatively stable year-on-year with revenues benefitting from higher regulatory allowances in its business plan as determined by the CMA.

Pennon Water Services continues to deliver further revenue growth with contract wins contributing £17.5 million of additional revenue in 2021/22 compared to 2020/21.

Cash collections throughout the Group have remained robust during the financial year. Underlying credit loss charges for 2021/22 of £3.1 million for South West Water (0.5% of revenue) are in line with previous levels (2020/21 0.5%). Bristol Water recognised an expected credit loss charge of £1.9 million (1.8% of revenue) for the ten month period since acquisition, in line with recent experience for the business. For Pennon Water Services, the expected credit loss charge of £0.5 million (0.3% of revenue) is lower than the previous year (2020/21 of 0.6% of revenue). This reflects the significant focus on cash collection and the quality of the customer base as revenues have recovered from the pandemic. Across all Group businesses, the potential impact of significant increases in the cost of living on affordability has been considered, noting the existing toolkit of measures we have in place to help customers most in need in difficult times.

Overall, underlying EBITDA[^] has increased by 14.7% from £334.7 million to £383.9 million including a contribution of £53.3 million from Bristol Water. Organically¹⁰, underlying EBITDA[^] has reduced marginally by 1.2% with cost pressures from macro-economic conditions and higher costs to serve offsetting higher revenues.

Group underlying profit before tax[^] decreased by 8.6% to £143.5 million compared with the prior year of £157.0 million. This outturn reflects the underlying EBITDA[^] growth, supported by the Bristol Water contribution, being more than offset by increased interest charges on index-linked debt driven by the continuing high inflationary environment.

As flagged in our half year results 2021/22 presentation, the results for the Group are H1 weighted with the significantly higher levels of inflation impacting finance costs on index-linked debt in the last six months. Whilst long-term protection from the increasing inflationary environment is provided through inflation linked revenues and RCV growth, along with regulatory true-ups²⁴, we continue to expect financing costs to be impacted in the near term. Whilst the Group benefits from a lower proportion of index-linked debt compared to the water industry average, 29% of Pennon's regulated water businesses' gross debt of £2.8 billion is index linked, meaning a 1% increase in inflation results in an additional c.£8 million of financing costs.

SOUTH WEST WATER

| South West Water underlying ²⁵ | 2021/22 | 2020/21 | Change |
|-------------------------------------------|-----------|-----------|---------|
| Revenue ²⁶ | £583.4m | £563.0m | +3.6% |
| Operating Costs | (£251.9m) | (£222.4m) | (13.3%) |
| EBITDA [^] | £331.5m | £340.6m | (2.7%) |
| Depreciation and amortisation | (£117.0m) | (£118.3m) | (1.1%) |
| Operating profit | £214.5m | £222.3m | (3.5%) |
| Net interest charge | (£77.9m) | (£57.7m) | (35.0%) |
| Profit before tax | £136.6m | £164.6m | (17.0%) |

South West Water's underlying revenue for 2021/22 of £583.4 million has increased by 3.6% (£20.4 million) compared with the prior year (2020/21 £563.0 million). This increase reflects the continued recovery of the non-household market and developer services activity to near pre-Covid levels, in addition to maintained elevated demand by household customers.

Underlying operating costs of £251.9 million increased by £29.5 million (2020/21 £222.4 million) principally reflecting:

- Inflationary and other cost pressures on wholesale energy of c.£5.1 million, c.£2.0 million on wages, c.£0.8 million on chemicals (linked to energy markets), and £4.6 million on other cost lines including higher insurance costs
- Increased production volumes arising from the recovery of non-household demand driving increased power and chemical consumption of c.£4 million

²⁴ Including revenue and RCV adjustments to reflect changes of totex allowances linked to changes in pay and wage indices (ASHE – average survey of hours and earnings), the true up for higher tax rates, changes in iboxx indices trueing up the cost of new debt, true ups for changes in volume related to bioresources, developer activity, land sales and customer numbers

²⁵ Measures presented are before non-underlying items

²⁶ Includes wholesale revenue for non-household customers

- Additional operating costs of c.£5 million to enhance and accelerate our key areas of operational focus of pollutions and leakage and reflecting additional regulatory requirements such as ‘farming rules for water’
- Higher developer activity such as government road schemes of c.£5 million associated with higher developer revenue
- Other operating costs of c.£5 million, partially offset by ongoing efficiency initiatives and property sales.

South West Water’s underlying EBITDA[^] and underlying operating profit reduced by 2.7% and 3.5%, respectively, reflecting the higher revenue from higher overall demand more than offset by higher operating costs.

Net interest costs of £77.9 million are £20.2 million higher than the prior year (2020/21 £57.7 million) due to the impact of higher inflation on index-linked debt. The Group’s efficient funding mix (which includes a relative low proportion of index-linked debt) and hedging strategy minimises these market effects with active management of our portfolio continuing to deliver a sector leading effective interest rate[^] of 3.4% (2020/21 2.5%). South West Water has c.£750 million of interest rate swaps in place to manage its fixed, floating and index-linked ratios.

South West Water’s capital expenditure this financial year was £203.4 million (2020/21 £168.2 million), with the split between clean water investment and wastewater investment being largely balanced at £102.1 million and £101.3 million, respectively. This c.20% increase reflects the expected profile in the regulatory period with major capital schemes to replace the first of two water treatment works in the Bournemouth region progressing well, in addition to advanced expenditure on bathing water schemes and other environmental projects.

BRISTOL WATER

| Bristol Water underlying²⁵ | 2021/22 |
|----------------------------------------------|----------------|
| Revenue ²⁶ | £104.4m |
| Operating Costs | (£51.1m) |
| EBITDA [^] | £53.3m |
| Depreciation and amortisation | (£24.0m) |
| Operating profit | £29.3m |
| Net interest charge | (£20.1m) |
| Profit before tax | £9.2m |

Bristol Water has contributed to the Group’s financial results since its acquisition on 3 June 2021. The business has contributed underlying revenue[^] of £104.4 million, underlying EBITDA[^] of £53.3

million and underlying profit before tax[^] of £9.2 million since that date, before any adjustments to depreciation and interest costs from the acquisition fair value exercise. In the period since acquisition, the business has performed ahead of acquisition expectations, with results having an H1 weighting, primarily due to the inflationary impact on its index-linked debt. The impact of inflation in the second half of the year on Bristol Water's financing costs has been more marked with c.50% of Bristol Water's debt being index-linked.

Bristol Water has delivered increased revenues of c.4% in the financial year to 31 March 2022, compared to the same 12 month period last year. Overall demand in the Bristol region has remained relatively stable with reductions in household demand being offset by the recovery in the non-household market. Revenues have also benefitted from higher regulatory allowances in its business plan determined by the CMA.

Bristol Water's capital programme totalled £37.0 million for the ten month period since acquisition and includes resilience focused investment across the network and initiatives to further improve supply interruptions performance.

PENNON WATER SERVICES

| Pennon Water Services underlying²⁵ | 2021/22 | 2020/21 | Change |
|------------------------------------------------------|------------------|-----------------|----------------|
| Revenue | £195.3m | £162.8m | +20.0% |
| <i>Water segment wholesale elimination</i> | <i>(£90.9m)</i> | <i>(£81.6m)</i> | <i>+11.4%</i> |
| <i>Revenue excluding elimination</i> | <i>£104.4m</i> | <i>£81.2m</i> | <i>+28.6%</i> |
| Operating Costs ²⁷ | (£191.9m) | (£161.4m) | (18.9%) |
| <i>Water segment wholesale elimination</i> | <i>£90.9m</i> | <i>£81.6m</i> | <i>(11.4%)</i> |
| <i>Operating costs excluding elimination</i> | <i>(£101.0m)</i> | <i>(£79.8m)</i> | <i>(26.6%)</i> |
| EBITDA [^] | £3.4m | £1.4m | +142.9% |
| Depreciation and amortisation | (£0.8m) | (£0.7m) | (14.3%) |
| Operating profit | £2.6m | £0.7m | +271.4% |
| Net interest charge | (£1.6m) | (£1.7m) | +5.9% |
| Profit / (loss) before tax | £1.0m | (£1.0m) | +200.0% |

Pennon Water Services has performed strongly this financial year through its disciplined approach to winning new business and benefitting from business customers' Covid recovery throughout the year.

Non-household demand has returned to near pre-Covid levels, with the recovery predominantly in the hospitality, tourism and manufacturing sectors. Growth rates in the second half of the year have moderated from the growth rates seen in the first half of 2021/22.

²⁷ Includes wholesale costs for non-household customers

The overall impact on underlying revenues[^] for Pennon Water Services, including the impact of new contract wins is an increase of c.20% compared to the prior year. New business wins have contributed £17.5 million of additional revenue compared to last year. Underlying operating costs have grown in line with improving revenues and the business has more than doubled its underlying EBITDA[^]. This strong performance has resulted in the business reporting a profit before tax of £1.0 million (2020/21 loss before tax £1.0 million).

The business continues to maintain its focus on targeting high quality, sustainable customers who will benefit from the value-added services that form part of Pennon Water Services' differentiated service proposition, with new annualised contract wins of c.£19 million secured during the year.

Group net finance costs

Net finance costs for the Group of £93.7 million are £35.4 million higher than last year (2020/21 £58.3 million), driven by the current high levels of inflation. The Group has benefitted from the efficient financing that has been achieved through our diverse mix of fixed, floating and index-linked debt, including Pennon's relatively lower exposure to index-linked instruments in comparison to the water industry average.

The Group continues to secure funding for South West Water through its Sustainable Financing Framework and has efficiently secured funding, both fixed or hedged, to ensure c.60% of its interest rate risk is mitigated in line with the Group Treasury policy with a further c.27% index linked which remains below Ofwat's notional assumption of 33%.

Bristol Water has a mix of fixed, floating and index-linked debt, of which c.50% is index-linked. At 31 March 2022 Bristol Water's gross debt stood at £419 million excluding fair value adjustments arising on acquisition. We will seek to refinance Bristol Water's debt in line with the Group's efficient financing strategy over a longer time period as debt matures.

The diverse portfolio of debt in the water business remains in line with Ofwat's notional water company assumptions.

Profit before tax

Group underlying profit before tax[^] is £143.5 million compared with the prior year of £157.0 million. This outturn reflects the underlying EBITDA[^] growth, supported by Bristol Water's ten month contribution, being more than offset by increased interest charges on index-linked debt.

Non-underlying items and acquisition accounting

Non-underlying items for 2021/22 total a charge before tax of £15.8 million (2020/21 charge of £24.9 million). The Directors believe excluding non-underlying items provides a more useful comparison of business trends and performance.

The total non-underlying charge consists of expenses in connection with the acquisition of Bristol Water and the related merger review by the CMA and integration costs.

The total non-underlying tax charge is £98.2 million (2020/21 £4.8 million credit), including a credit of £1.3 million in connection with the items noted above and a £99.5 million non-underlying deferred tax charge, recognised for the change in future tax rate which was substantively enacted during this financial year.

As part of the requirements of acquisition accounting, we have determined the fair values of the acquired balance sheet of Bristol Water. These provisional values were reported in the Group's half year results to 30 September 2021 with some changes being required to the acquired tax balances. The most material areas of adjustment relate to the fair value of acquired property, plant and equipment, including the network infrastructure, and the fair value of Bristol Water's debt portfolio.

Goodwill arising from the acquisition of £116.1 million has been recorded in the Group consolidated balance sheet and is attributed to the synergies expected to be derived from the combination and the value of the workforce which cannot be recognised as an intangible asset. The consequent adjustments to depreciation and interest costs arising from the fair value exercise are reflected within 'Other' in our segmental reporting.

Responsible approach to tax

The overall tax charge for the Group is £112.1 million (2020/21 £24.8 million). On an underlying[^] basis, the net tax charge for 2021/22 for the Group of £13.8 million (2020/21 £29.6 million) consists of:

- Current tax charge of £5.0 million, reflecting an effective tax rate of 3.5% (2020/21 £23.0 million, 14.6%). This reduction is primarily as a result of the introduction of capital allowance super-deductions (c.£15 million of additional capital allowances), along with tax relief on pension payments made during the year and in recent years
- Deferred tax charge of £8.9 million (2020/21 £6.6 million) primarily reflects capital allowances across the Group in excess of depreciation charged together with relief on pension contributions. The increase mainly relates to super-deductions.

The UK tax rate increases to 25% from 1 April 2023, and as such most deferred tax items will crystallise at a higher rate. This change gives rise to a non-underlying deferred tax charge of £99.5 million.

Earnings per share

The Group has recorded statutory earnings per share of 4.9 pence for the year ended 31 March 2022. This includes non-underlying items before tax of £15.8 million and a net non-underlying tax charge of £98.2 million. Statutory earnings per share of 418.5 pence in 2020/21 included the significant profit on disposal of Viridor of c.£1.7 billion.

The comparability of the Group's earnings per share is distorted by the significant one-off transactions that have been identified as non-underlying and the profit on the sale of Viridor reported in the last financial year. Furthermore, the average number of shares used to derive the earnings per share reflects the share consolidation in July 2021, reducing the share count from 422.1 million to 281.4 million.

To facilitate comparison of performance, our adjusted earnings per share excludes the impact of deferred tax charges and non-underlying items. We have also adjusted the number of shares in issue to reflect the share consolidation as if it took place at the start of both this, and the last, financial year to aid comparability. For the Group, we have generated adjusted earnings per share[^] (adjusted for share consolidation)⁸ for 2021/22 of 50.2 pence compared to 47.8 pence in 2020/21, on a comparable basis. This represents an increase of 5.0%, reflecting the contribution from Bristol Water and the lower current tax charge from super-deductions.

Sustainable net debt position

Cash generation has remained robust throughout 2021/22. We closely monitor cash collections throughout the year as the volatility in the wider economy and the potential impact of significant rises in the cost of living increases risk in this area. The Group's total operational cash inflows and other movements[^] for 2021/22 were £364.7 million (2020/21 £316.0 million) including a £47.1 million contribution from Bristol Water.

These cashflows adequately support our effective finance structures with net interest paid of £72.0 million (2020/21 £66.3 million) and capital payments of £227.6 million (2020/21 £157.6 million).

Net cash interest payments for the total Group have increased compared to the previous year. c.£36 million of the income statement finance costs relate to indexation, which is non-cash and accretes to the carrying value of the respective debt instruments. Bristol Water has contributed an additional cash interest cost of c.£12 million, which is partially offset by the reduced interest charges at a Pennon company level following the repayment of Viridor related debt during the previous financial year.

The acquisition of Bristol Water resulted in total cash outflows of £421.2 million²⁸ including transaction costs and stamp duty, net of £12.8 million cash acquired. The Group's net debt is further increased by £391.4 million book value of Bristol Water's net debt and subsequent fair value adjustments of £134.8 million at the point of acquisition.

Other significant movements in net debt in 2021/22 include the special dividend of £1,498.5 million, £27.9 million contributions to the Group's principal pension scheme and the four tranches of the share buy-back programme completed up to 31 March 2022, with the total cash outflow of £202 million. The restructuring of the Group's borrowings is now substantially complete, and the current levels of net debt represent a sustainable position for the Group.

Following the above, and the payment of our interim and final dividends for 2020/21, the Group's net debt at 31 March 2022 was £2,682.9 million (31 March 2021 net cash £64.3 million). This includes fair value adjustments on acquired debt of £168.6 million²⁹ resulting from the Bournemouth Water and Bristol Water acquisitions, which are released over the life of the related debt instruments. The Group's net debt position excluding these adjustments is £2,514.3 million.

Agile and efficient financing

The water business' cost of finance, with an effective rate[^] of 3.7% remains among the lowest in the industry, continuing to benefit from the use of finance leasing as the main source of funding in the portfolio which provides long maturities at fixed margins, secured at the inception of each lease.

The water business net debt is a mix of fixed / swapped (£1,401 million, 53%), floating (£426 million, 16%) and index-linked borrowings (£812 million, 31%). The debt has a maturity of up to 35 years with a weighted average maturity of c.15 years. New debt has been fixed to align to iBoxx indices in line with Ofwat's approach to allowed cost of debt. Where appropriate, derivatives are used to fix the rate on floating rate debt.

The gross debt position of the water business is a mix of fixed / swapped 53%, floating 18% and index-linked 29% as at 31 March 2022, which reflects our diverse debt portfolio and compares to an industry average³⁰ of fixed / swapped 43%, floating 8% and index linked 49%.

South West Water's gross debt has reduced by £192 million to £2,429 million (2020/21 £2,621 million). This is mainly due to the repayment and restructuring of the lease portfolio to ensure its continued efficient and effective management with a further c.£150 million planned to be repaid in

²⁸ Reflecting £425.1 million on acquisition, £8.9 million cash outflow for expenses in connection with the acquisition of Bristol Water, offset by £12.8 million cash acquired

²⁹ Carrying value of fair value acquisition adjustments to net debt at 31 March 2022 - £39.9 million Bournemouth Water, £128.7 million Bristol Water

³⁰ UK water position as at 31 March 2021

September 2022. The lease portfolio will continue to deliver long term benefits as part of our diverse range of facilities as we look to further develop our exposure to other products going forward.

During the year, the Group completed the transition to SONIA as its risk-free rate following the cessation of LIBOR in December 2021, the Group has followed the protocols set out for the transition and amended the financial instruments to ensure the continued practice of hedge accounting for our facilities and associated derivatives.

The water business index-linked debt remains below the Ofwat's notional assumption of 33%. Given the current volatility within the market and the divergence in the wedge from the assumed position, the water business remains at a comparative advantage through the regulatory transition from RPI to CPIH and in light of the current market conditions.

As announced in June 2021, Pennon planned to deploy c.£100 million investment into the water business and, as at 31 March 2022 the first deployment of £45 million has been made into South West Water. Including this planned investment, at 31 March 2022, the water business debt to RCV³¹ ratio stood at 61.4%^{32,5} (31 March 2021 64.8%). At the same date and on the same basis, gearing at South West Water was 61.7%³², which is expected to fall during this regulatory period with a trajectory towards Ofwat's notional structure of 60% by 2025. Bristol Water gearing at 31 March 2022 was 59.8%⁵. The debt to RCV ratios at 31 March 2022 for the water business and Bristol Water stood at 62.7% and 69.2%, respectively, before the remaining investment being made.

Responsible and sustainable balance sheet

The Group has a strong liquidity and funding position with £816 million of cash and committed facilities as at 31 March 2022. This consists of cash of £519 million (including £168 million of restricted funds representing deposits with lessors against lease obligations) and £297 million of undrawn facilities. £307 million of the cash holdings are held at the Pennon company level.

Following the continued success of our Sustainable Financing Framework, in September 2021 we issued our updated framework to incorporate the latest sustainable principles; in particular in respect of sustainability linked loans and bonds. The Group was the first UK corporate to issue sustainability linked loans in 2018 and the new principles have helped to develop this market further. Since March 2021, the Group has signed c.£300 million of new and renewed facilities across Pennon and South West Water.

The Group's measure of return on capital employed has been distorted at the year end 31 March 2021 and 31 March 2022 with the Group being in a net cash position at 31 March 2021, which distorts

³¹ RCV as published in South West Water's Final Determination (2020-25), recognising the omission of data not included by Ofwat in relation to IFRS16: *Leases*

³² Based on RCV at 31 March 2022 and South West Water Group net debt. Regulatory South West Water Limited gearing is 63.6% at 31 March 2022 (67.0% at 31 March 2021)

the average capital employed. South West Water's return on capital employed[^] at 31 March 2022 of 8.6% has reduced marginally in comparison to the same period last year (2021: 9.1%) reflecting the planned increased levels of capital investment at this phase of our regulatory plan.

Pensions

At 31 March 2021, the Group reported a surplus on retirement benefit obligations of £8.8 million relating to the Group's principal pension scheme, Pennon Group Pension Scheme (PGPS). At 31 March 2022, the surplus on retirement obligations of £66.3 million constitutes a surplus on PGPS of £59.5 million and a surplus of £6.8 million in respect of Bristol Water's defined benefit pension obligations.

The surplus on PGPS has increased by £50.7 million with the significant elements of the increase being:

- £23.0 million of additional contributions to the scheme being part of our package of returning capital to our investors and stakeholders
- £24.9 million increase in surplus from favourable movements in financial and other actuarial assumptions.

In total, following the Viridor disposal, the Group has contributed £59.0 million over and above the agreed deficit recovery payments from the 2019 actuarial valuation. As at 31 March 2022, PGPS is approximately 105% funded against its technical provisions and no further deficit recovery contributions are outstanding from the 2019 actuarial valuation. The 2022 triennial valuation is underway.

Bristol Water's pension surplus relates to the Bristol Water Section of the Water Companies Pension Scheme (WCPS). The liabilities of the scheme are fully insured, securing the pension promises made to the benefit of members through a bulk annuity policy. Changes in actuarial assumptions have little impact on the surplus recognised as the change in liabilities is materially matched by the change in asset values through the bulk annuity policy. The surplus recognised on acquisition reflects the fair value of the surplus to Pennon and is restricted by a tax deduction of 35% under UK tax legislation.

Recognising shareholder support

The Group continues to deliver on its commitments to customers, shareholders and stakeholders as our investments drive tangible, positive and sustainable results. Over half of Pennon's shareholders are UK pension funds, savings, charities and individuals with almost half of the Group's employees, now including Bristol Water, also being shareholders.

In July 2021, shareholders approved the payment of a £1.5 billion special dividend to shareholders as part of Pennon's recognition of shareholder support following the sale of Viridor in July 2020. The

special dividend represented £3.55 per existing ordinary share and was paid in July 2021 from the retained earnings arising from the Viridor disposal.

To maintain comparability of the Company's share price before and after the special dividend, a share consolidation accompanied the special dividend. This consolidated the Ordinary share capital on the basis of two New Ordinary Shares for every three Existing Ordinary Shares. The effect of the share consolidation was that the existing shares were replaced by the new shares, reducing the number of shares in issue and reflecting the amount of cash to be returned to shareholders, thus being economically neutral.

In July 2021 the Group commenced a share buy-back programme of up to £400 million, with the first four tranches totalling c.£200 million being completed prior to 31 March 2022. Further phases are expected to commence imminently and over the period to 30 September 2022, subject to our continued review of further growth opportunities in UK water, in line with our established financial disciplines.

Following the share consolidation, share buy-back and acquisition of Bristol Water, the dividend per share was rebased, with the interim and final dividend for 2020/21 being rebased to 11.15 pence and 24.46 pence respectively, resulting in a total dividend for 2020/21 of 35.61 pence⁹.

The Board has recommended a final dividend of 26.83 pence per share for the year ended 31 March 2022. Together with the interim dividend of 11.70 pence per share paid on 5 April 2022 this gives a total dividend for the year of 38.53 pence. This represents an increase of 8.2% (CPIH + 2%) on the adjusted base for 2020/21. Pennon offers shareholders the opportunity to invest their dividend in a Dividend Reinvestment Plan (DRIP).

Pennon's sector-leading dividend policy of growth of CPIH +2% reflects the Board's confidence in the Group's sustainable growth strategy and is underpinned by continued RORE[^] outperformance in South West Water.

Proposed dividends totalling £102.0 million are covered 1.4 times[^] by net profit (before non-underlying items and deferred tax) (2020/21 1.9 times). Dividends are charged against retained earnings in the year in which they are paid.

Macro-economic outlook

The global economy continues to be volatile reflecting the global geopolitical situation, including the ongoing war in Ukraine, compounding existing global economic difficulties regarding the recovery from the impacts of the Covid-19 pandemic. The impacts on the supply chain, rising power prices and overall higher levels of inflation are impacting all businesses. Our 2022/23 pay increases across

the business have been agreed at between 3% and 5%, and we are continuing to target efficiencies across the Group, having delivered c.£110 million³³ during K7 to date

We recognise the pressure that inflationary pricing increases may pose to our customers, and customer bill affordability is a key consideration for us. Our broad range of affordability measures ensures we are able to support those in need of support, and we are pleased that for the coming year bills will continue to be lower than they were 10 years ago, driven by our continued focus on delivering improvements efficiently and effectively.

In the near-term we expect our earnings to be impacted by the higher inflationary environment, in particular from higher interest and power costs.

Looking at our cost base, power costs represent 20% of our underlying operating costs at c.£56 million of the regulated water business in 2021/22, of which c.£28 million relates to wholesale power prices. Over the past year energy prices have been volatile and have risen sharply. For 2022/23 we have de risked around two thirds of our power needs. Given where power prices currently are, with day-ahead pricing of around £100 MW/h and the Winter season at £230 M/Wh we expect our power costs to rise between 50 and 75%³⁴. For 2023/24 and 2024/25 have de-risked around 40% of our power needs locking in rates around 10% above the 2021/22 outturn.

Our energy risk policies involve constant monitoring of forward power prices and we will continue to manage our exposure to pricing volatility in this area. As part of our target to achieve net zero carbon emissions by 2030, we have identified renewable energy generation investment opportunities which will decrease our reliance on wholesale power markets. We are underway with installing our first phase of new solar PV which will help to more than double the Group's self-generation capacity to >10%.

Like all companies we are seeing supply chain inflation pressures in particular for chemicals, transport costs and construction materials such as steel and concrete. However, we are well placed as we start from an efficient cost base which has generated c.£110 million of totex efficiencies in K7 to date.

However, in the longer term the elevated inflationary environment provides the Group with additional growth in long-term sustainable value, with revenues and RCV linked to November and March outturn inflation, respectively. The elevated inflationary environment in this regulatory period is forecast to increase RCV by a further c.10% over K7, bringing total RCV growth in K7 to >40%, more than offsetting the near-term headwinds.

³³ Combined water business position

³⁴ Based on indicative pricing in late May 2022

Technical Guidance – 2022/23

| Pennon Group | | FY 2021/22 | Change |
|--------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------|---------------|
| Revenue | <ul style="list-style-type: none"> • Full year revenue contribution from Bristol Water • Pennon Water Services growth through contract wins and continued non-household demand recovery • Offset by impact of lower customer bills | £792.3m | ▲ |
| Net debt | <ul style="list-style-type: none"> • Expected deployment of share buy-back c.£200 million • Continued capital investment across the Group • Accretion on index-linked debt | £2,682.9m | ▲ |
| Current tax | <ul style="list-style-type: none"> • 2021/22 effective rate reflects additional pension contributions made during the year • Continued super-deductions anticipated in 2022/23 | 3.5% | ▲ |
| Water business | | FY 2021/22 | Change |
| Operating costs | <ul style="list-style-type: none"> • Operating cost increases due to market impact of inflation, including power • Full year impact of Bristol Water | £303.0m | ▲ |
| Net interest | <ul style="list-style-type: none"> • Efficient financing impacted by inflationary increases in charges related to index-linked debt • Full year impact of Bristol Water | £98.0m | ▲ |
| Capex | <ul style="list-style-type: none"> • Capital expenditure reflects K7 existing profile of investment, with anticipated peak in 2022/23 | £240.4m | ▲ |
| RORE [^] (Ofwat K7 cumulative) | <ul style="list-style-type: none"> • Continued doubling of base returns for South West Water – targeting improved net reward on ODIs, maintaining cumulative totex efficiency to date, increasing level of financing outperformance through inflationary environment | 7.9% | - |
| | <ul style="list-style-type: none"> • Bristol RORE anticipated to be improved as synergies are realised | 4.9% | - |
| RCV | <ul style="list-style-type: none"> • Increase in line with K7 business plan levels of investment and inflationary impact | £4.2bn | ▲ |
| Pennon Water Services | | FY 2021/22 | Change |
| Operating costs | <ul style="list-style-type: none"> • Non-household recovery and contract wins leading to higher wholesale supply charges • Impact of increased inflationary environment | £191.9m | ▲ |
| Underlying EBITDA [^] | <ul style="list-style-type: none"> • Impact of increased non-household demand on margins • Focus on continued cost efficiency with strong collections | £3.4m | ▲ |

Board Matters

Upon our acquisition of Bristol Water Holdings UK Limited and its subsidiaries, including Bristol Water plc, on 3 June 2021, Paul Boote, Iain Evans and Neil Cooper were appointed as directors of Bristol Water plc and the other companies in the Bristol Water Group. Following the CMA's acceptance of Pennon's undertakings in lieu and grant of merger clearance on 7 March 2022, Susan Davy was appointed as a director of Bristol Water plc on 9 March 2022 and the other Bristol Water Group companies on 4 April 2022, and Gill Rider, Claire Ighodaro and Jon Butterworth were appointed directors of Bristol Water plc on 2 April 2022.

Susan Davy

Group Chief Executive

30 May 2022

Financial Timetable

| | |
|-------------------|---------------------------------------------|
| June 2022 | Annual Report and Accounts published |
| 21 July 2022 | Annual General Meeting |
| 22 July 2022* | Ordinary shares quoted ex-dividend |
| 22 July 2022* | Record date for final dividend |
| 11 August 2022* | Final date for receipt of DRIP applications |
| 5 September 2022* | Final Dividend payment date |
| 30 September 2022 | Trading Statement |
| 30 November 2022 | Half Year Results 2022/23 |
| 26 January 2023 | Ordinary shares quoted ex-dividend |
| 27 January 2023 | Record date for interim dividend |
| 10 March 2023 | Final date for receipt of DRIP applications |
| 31 March 2023 | Trading Statement |
| 1 June 2023 | Full Year Results 2022/23 |

* Subject to obtaining shareholder approval at the 2022 Annual General Meeting.

PRINCIPAL RISKS AND UNCERTAINTIES

Principal Risks

The Board continues to regularly consider and review the principal risks of the Group within the context of its risk appetite. This includes the impact of changes to the external macro-economic, legal and regulatory environment within which the Group operates.

The Board have reviewed the Group's principal risks and consider them to be consistent with those reported within the 2021/22 Half Year Results:

Law, Regulation and Finance

1. Changes in Government Policy
2. Regulatory frameworks
3. Non-compliance with laws and regulations
4. Inability to secure sufficient finance and funding, within our debt covenants, to meet ongoing commitments
5. Non-compliance or occurrence of avoidable health and safety incidents
6. Failure to pay all pension obligations as they fall due & increased costs to the Group should the defined benefit pension scheme deficit increase

Market and Economic Conditions

7. Non-recovery of customer debt
8. Macro-economic near-term risks impacting on inflation, interest rates and power prices

Operating Performance

9. The Group's operations and assets are impacted as a result of climate change and extreme weather events
10. Failure of operational water treatment assets and processes resulting in an inability to produce or supply clean drinking water
11. Failure of operational wastewater assets and processes resulting in an inability to remove and treat wastewater and potential environmental impacts, including pollutions
12. Failure to maintain excellent service or effectively engage with our customers and wider stakeholders
13. Insufficient skills and resources to meet the current and future business needs and deliver the Group's strategic priorities
14. Non-delivery of Regulatory Outcomes and performance commitments

Business Systems and Capital Investment

15. Inefficient or ineffective delivery of capital projects
16. Inadequate technological security results in a breach of the Group's assets, systems and data
17. Failure to fully realise the strategic value arising from the acquisition of Bristol Water.

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, changes in Government policy; regulatory and legal reform; compliance with laws and regulations; maintaining sufficient finance and funding to meet ongoing commitments; non-compliance or occurrence of avoidable health and safety incidents; tax compliance and contribution; failure to pay all pension obligations as they fall due and increased costs to the Group should the defined benefit pension scheme deficit increase; non-recovery of customer debt; poor operating performance due to extreme weather or climate change; macro-economic risks impacting commodity and power prices and other matters; poor customer service and/or increased competition leading to loss of customer base; business interruption or significant operational failure/incidents; difficulty in recruitment, retention and development of skills; non-delivery of regulatory outcomes and performance commitments; failure or increased cost of capital projects/exposure to contract failures; failure of information technology systems, management and protection, including cyber risks; and all other risks in the Pennon Group Annual Report to be published in June 2022. Such forward looking statements should therefore be construed in light of all risks, uncertainties and other factors, including without limitation those identified above, 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 year ended 31 March 2022

| | Notes | Before non- underlying items 2022 £m | Non- underlying items (note 4) 2022 £m | Total 2022 £m | Before non- underlying items 2021 £m | Non- underlying items (note 4) 2021 £m | Total 2021 £m |
|-------------------------------------------------------------------------|-------|--------------------------------------------------|-------------------------------------------------------|---------------------|--------------------------------------------------|-------------------------------------------------------|---------------------|
| Continuing operations | | | | | | | |
| Revenue | 3 | 792.3 | - | 792.3 | 644.6 | (20.5) | 624.1 |
| Operating costs | | | | | | | |
| Employment costs | | (90.4) | (1.7) | (92.1) | (75.0) | (4.4) | (79.4) |
| Raw materials and consumables used | | (22.9) | - | (22.9) | (18.1) | - | (18.1) |
| Other operating expenses | | (295.1) | (14.1) | (309.2) | (216.8) | - | (216.8) |
| Earnings before interest, tax, depreciation and amortisation | 3 | 383.9 | (15.8) | 368.1 | 334.7 | (24.9) | 309.8 |
| Depreciation and amortisation | | (146.7) | - | (146.7) | (119.4) | - | (119.4) |
| Operating Profit | 3 | 237.2 | (15.8) | 221.4 | 215.3 | (24.9) | 190.4 |
| Finance income | 5 | 2.6 | - | 2.6 | 4.2 | - | 4.2 |
| Finance costs | 5 | (96.3) | - | (96.3) | (62.5) | - | (62.5) |
| Net finance costs | 5 | (93.7) | - | (93.7) | (58.3) | - | (58.3) |
| Profit before tax | 3 | 143.5 | (15.8) | 127.7 | 157.0 | (24.9) | 132.1 |
| Taxation | 6 | (13.9) | (98.2) | (112.1) | (29.6) | 4.8 | (24.8) |
| Profit for the year from continuing operations | | 129.6 | (114.0) | 15.6 | 127.4 | (20.1) | 107.3 |
| Discontinued operations | | | | | | | |
| Profit for the year from discontinued operations | 14 | - | - | - | 35.5 | 1,619.2 | 1,654.7 |
| Profit for the year | | 129.6 | (114.0) | 15.6 | 162.9 | 1,599.1 | 1,762.0 |
| Attributable to: | | | | | | | |
| Ordinary shareholders of the parent | | | | 15.4 | | | 1,762.2 |
| Non-controlling interests | | | | 0.2 | | | (0.2) |
| Earnings per ordinary share (pence per share) | 7 | | | | | | |
| From continuing operations | | | | | | | |
| - Basic | | | | 4.9 | | | 25.5 |
| - Diluted | | | | 4.9 | | | 25.4 |
| From continuing and discontinued operations | | | | | | | |
| - Basic | | | | 4.9 | | | 418.5 |
| - Diluted | | | | 4.9 | | | 416.9 |

PENNON GROUP PLC

Consolidated statement of comprehensive income for the year ended 31 March 2022

| | Before non- underlying items 2022 £m | Non- underlying items (note 4) 2022 £m | Total 2022 £m | Before non- underlying items 2021 £m | Non- underlying items (note 4) 2021 £m | Total 2021 £m |
|----------------------------------------------------------------------|--------------------------------------------------|-------------------------------------------------------|---------------------|--------------------------------------------------|-------------------------------------------------------|---------------------|
| Profit for the year | 129.6 | (114.0) | 15.6 | 162.9 | 1,599.1 | 1,762.0 |
| Other comprehensive income / (loss) | | | | | | |
| <i>Items that will not be reclassified to profit or loss</i> | | | | | | |
| Remeasurement of defined benefit obligations | 24.9 | - | 24.9 | (28.8) | - | (28.8) |
| Income tax on items that will not be reclassified | 2.4 | - | 2.4 | 5.5 | - | 5.5 |
| Total items that will not be reclassified to profit or loss | 27.3 | | 27.3 | (23.3) | - | (23.3) |
| <i>Items that may be reclassified subsequently to profit or loss</i> | | | | | | |
| Cash flow hedges | 40.6 | - | 40.6 | 13.5 | - | 13.5 |
| Income tax on items that may be reclassified | (6.5) | - | (6.5) | (2.4) | - | (2.4) |
| Total items that may be reclassified subsequently to profit or loss | 34.1 | - | 34.1 | 11.1 | - | 11.1 |
| Other comprehensive income / (loss) for the year net of tax | 61.4 | - | 61.4 | (12.2) | - | (12.2) |
| Total comprehensive income for the year | 191.0 | (114.0) | 77.0 | 150.7 | 1,599.1 | 1,749.8 |
| Total comprehensive income attributable to: | | | | | | |
| Ordinary shareholders of the parent | | | 76.8 | | | 1,750.0 |
| Non-controlling interests | | | 0.2 | | | (0.2) |

PENNON GROUP PLC
Consolidated balance sheet at 31 March 2022

| | Notes | 2022 £m | 2021 £m |
|-----------------------------------------------------------------------|-------|------------------|------------------|
| ASSETS | | | |
| Non-current assets | | | |
| Goodwill | | 158.4 | 42.3 |
| Other intangible assets | | 13.9 | 1.2 |
| Property, plant and equipment | | 4,264.0 | 3,221.0 |
| Derivative financial instruments | | 14.8 | 3.8 |
| Other non-current assets | | 9.6 | - |
| Retirement benefit obligations | | 66.3 | 8.8 |
| | | 4,527.0 | 3,277.1 |
| Current assets | | | |
| Inventories | | 7.7 | 5.4 |
| Trade and other receivables | | 270.9 | 216.8 |
| Current tax receivable | | 1.5 | 0.1 |
| Derivative financial instruments | | 5.6 | 1.3 |
| Cash and cash deposits | 12 | 519.0 | 2,919.3 |
| | | 804.7 | 3,142.9 |
| LIABILITIES | | | |
| Current liabilities | | | |
| Borrowings | 12 | (240.2) | (88.3) |
| Financial liabilities at fair value through profit | | (2.5) | (2.8) |
| Derivative financial instruments | | - | (6.3) |
| Trade and other payables | | (171.5) | (126.1) |
| Provisions | | (1.0) | (0.3) |
| | | (415.2) | (223.8) |
| Liabilities associated with assets classified as held for sale | | | |
| | | | - |
| Net current assets | | 389.5 | 2,919.1 |
| Non-current liabilities | | | |
| Borrowings | 12 | (2,961.7) | (2,766.7) |
| Other non-current liabilities | | (137.2) | (128.3) |
| Financial liabilities at fair value through profit | | (36.1) | (39.4) |
| Derivative financial instruments | | - | (17.4) |
| Deferred tax liabilities | | (506.9) | (259.6) |
| | | (3,641.9) | (3,211.4) |
| Net assets | | 1,274.6 | 2,984.8 |
| Shareholders' equity | | | |
| Share capital | 9 | 161.7 | 171.8 |
| Share premium account | | 235.5 | 232.1 |
| Capital redemption reserve | | 154.7 | 144.2 |
| Retained earnings and other reserves | | 722.6 | 2,436.8 |
| Total shareholders' equity | | 1,274.5 | 2,984.9 |
| Non-controlling interests | | 0.1 | (0.1) |
| Total equity | | 1,274.6 | 2,984.8 |

PENNON GROUP PLC

Consolidated statement of changes in equity for the year ended 31 March 2022

| | Share capital (note 9) £m | Share premium account £m | Capital redemption reserve £m | Retained earnings and other reserves £m | Non- controlling interests £m | Perpetual capital securities £m | Total equity £m |
|-----------------------------------------------------------------------------------------------|---------------------------------|--------------------------------|----------------------------------------|-----------------------------------------------------|----------------------------------------|------------------------------------------|--------------------|
| At 1 April 2020 | 171.3 | 227.0 | 144.2 | 872.8 | 0.1 | 296.7 | 1,712.1 |
| Profit for the year | - | - | - | 1,762.2 | (0.2) | - | 1,762.0 |
| Other comprehensive income for the year | - | - | - | (12.2) | - | - | (12.2) |
| Total comprehensive income for the year | - | - | - | 1,750.0 | (0.2) | - | 1,749.8 |
| <i>Transactions with equity shareholders:</i> | | | | | | | |
| Dividends paid | - | - | - | (184.3) | - | - | (184.3) |
| Adjustments in respect of share-based payments (net of tax) | - | - | - | 2.2 | - | - | 2.2 |
| Redemption of perpetual capital securities | - | - | - | (3.3) | - | (296.7) | (300.0) |
| Own shares acquired by the Pennon Employee Share Trust in respect of share options granted | - | - | - | (1.2) | - | - | (1.2) |
| Deferred tax recognised directly in equity | - | - | - | 0.6 | - | - | 0.6 |
| Proceeds from shares issued under the Sharesave Scheme | 0.5 | 5.1 | - | - | - | - | 5.6 |
| Total transactions with equity shareholders | 0.5 | 5.1 | - | (186.0) | - | (296.7) | (477.1) |
| At 31 March 2021 | 171.8 | 232.1 | 144.2 | 2,436.8 | (0.1) | - | 2,984.8 |
| Profit for the year | - | - | - | 15.4 | 0.2 | - | 15.6 |
| Other comprehensive income for the year | - | - | - | 61.4 | - | - | 61.4 |
| Total comprehensive income for the year | - | - | - | 76.8 | 0.2 | - | 77.0 |
| <i>Transactions with equity shareholders:</i> | | | | | | | |
| Dividends paid | - | - | - | (1,590.3) | - | - | (1,590.3) |
| Shares purchased for cancellation (including related expenses) | - | - | - | (201.7) | - | - | (201.7) |
| Shares cancelled (note 9) | (10.5) | - | 10.5 | - | - | - | - |
| Adjustments in respect of share-based payments (net of tax) | - | - | - | 2.2 | - | - | 2.2 |
| Own shares acquired by the Pennon Employee Share Trust in respect of share options granted | - | - | - | (1.2) | - | - | (1.2) |
| Proceeds from shares issued under the Sharesave Scheme | 0.4 | 3.4 | - | - | - | - | 3.8 |
| Total transactions with equity shareholders | (10.1) | 3.4 | 10.5 | (1,791.0) | - | - | (1,787.2) |
| At 31 March 2022 | 161.7 | 235.5 | 154.7 | 722.6 | 0.1 | - | 1,274.6 |

PENNON GROUP PLC

Consolidated statement of cash flows for the year ended 31 March 2022

| | Notes | 2022 £m | 2021 £m |
|----------------------------------------------------------------------------------|-------|------------------|------------------|
| Cash flows from operating activities | | | |
| Cash generated from operations | 10 | 334.2 | 298.1 |
| Interest paid | | (74.6) | (80.2) |
| Tax paid | | (7.3) | (7.4) |
| Net cash generated from operating activities | | <u>252.3</u> | <u>210.5</u> |
| Cash flows from investing activities | | | |
| Interest received | | 2.6 | 4.3 |
| Loan repayments received from joint ventures | | - | 4.0 |
| Purchase of property, plant and equipment | | (225.6) | (190.1) |
| Purchase of intangible assets | | (3.4) | (0.2) |
| Acquisition of subsidiaries, net of cash acquired | | (421.2) | - |
| Proceeds on disposal of subsidiaries, net of cash disposed and transaction costs | | 9.2 | 3,628.5 |
| Proceeds from sale of property, plant and equipment | | 1.4 | 0.4 |
| Movement of restricted deposits | | 89.1 | (23.6) |
| Net cash (used in) / received from investing activities | | <u>(547.9)</u> | <u>3,423.3</u> |
| Cash flows from financing activities | | | |
| Proceeds from issuance of ordinary shares | | 3.8 | 5.6 |
| Purchase of ordinary shares by the Pennon Employee Share Trust | | (1.2) | (1.2) |
| Proceeds from new borrowing | | 61.0 | 330.0 |
| Repayment of borrowings | | (49.4) | (1,265.4) |
| Cash inflows from lease financing arrangements | 10 | 15.0 | 15.0 |
| Lease principal repayments (including recoverable VAT paid) | | (258.9) | (28.4) |
| Dividends paid | 8 | (1,590.3) | (184.3) |
| Repurchase of own shares and associated fees | | (201.7) | - |
| Perpetual capital securities periodic return | | - | (8.6) |
| Redemption of perpetual capital securities | | - | (300.0) |
| Net cash used in financing activities | | <u>(2,021.7)</u> | <u>(1,437.3)</u> |
| Net (decrease) / increase in cash and cash equivalents | | (2,317.3) | 2,196.5 |
| Cash and cash equivalents at beginning of year | 11 | 2,668.5 | 472.0 |
| Cash and cash equivalents at end of year | 11 | <u>351.2</u> | <u>2,668.5</u> |

PENNON GROUP PLC

Notes

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 59. Pennon Group's continuing business is operated through three principal subsidiaries. South West Water Limited includes the integrated water companies of South West Water and Bournemouth Water, providing water and wastewater services in Devon, Cornwall and parts of Dorset and Somerset and water only services in parts of Dorset, Hampshire and Wiltshire. Pennon Group is also the majority shareholder of Pennon Water Services Limited, a company providing water and wastewater retail services to non-household customer accounts across Great Britain.

On 2 June 2021, the Company approved the acquisition of the Bristol Water Holdings UK Limited ('Bristol Water'), which was completed on 3 June 2021. Bristol Water comprises Bristol Water plc, a regulated water only company serving a population of approximately 1.2 million in the Bristol region, and a 30% share in water2business Limited, a joint venture with Wessex Water. The acquisition was cleared by the Competition and Markets Authority on 7 March 2022, and the Bristol Water is consolidated in Pennon's accounts with effect from midnight on 2 June 2021.

On 8 July 2020, Pennon completed the sale of Viridor Limited, a recycling, energy recovery and waste management business. In accordance with IFRS 5 'Non-current assets held for sale and discontinued operations', the net results for Viridor were presented within discontinued operations in the Group income statement for 2021. The effect of the disposal on the financial position of the Group is detailed in note 14.

The financial information for the years ended 31 March 2022 and 31 March 2021 does not constitute statutory accounts within the meaning of section 434 of the Companies Act 2006. The Annual Report and Accounts for the year ended 31 March 2022, including the financial statements from which this financial information is derived, will be delivered to the Registrar of Companies after the AGM on 21 July 2022. The independent auditor's report on the 2022 financial statements was unqualified and did not contain a statement under section 498 of the Companies Act 2006.

The full financial statements for the year ended 31 March 2021 were approved by the Board of Directors on 2 June 2021 and have been delivered to the Registrar of Companies. The independent auditor's report on those financial statements was unqualified and did not contain a statement under section 498 of the Companies Act 2006. This final results announcement and the results for the year ended 31 March 2022 were approved by the Board of Directors on 30 May 2022.

2. Basis of preparation

The financial information in this announcement has been prepared on the historical cost accounting basis (except for fair value items as set out in the 2021 Annual Report and Accounts) and in accordance with UK-adopted international accounting standards. The accounting policies adopted are consistent with those followed in the preparation of the Group's 2022 Annual Report and Accounts which have not changed significantly from those adopted in the Group's 2021 Annual Report and Accounts (which are available on the Company website www.pennon-group.co.uk).

The going concern basis has been adopted in preparing these financial statements. At 31 March 2022 the Group has access to undrawn committed funds and cash and cash deposits totalling £816 million (£648 million excluding restricted cash). Having considered the Group's strong funding position and prudent financial projections, which take into account a range of possible impacts, as described in this report, the Directors have a reasonable expectation that the Group has adequate resource to continue in operational existence for the period which covers the period from approval of the 2022 financial statements through to 30 June 2023 and that there are no material uncertainties to disclose. For this reason, they continue to adopt the going concern basis in preparing the financial statements.

3. Segmental information

Operating segments are reported in a manner consistent with internal reporting provided to the Chief Operating Decision-Maker (CODM), which has been identified as the Pennon Group plc Board. The earnings measures below are used by the Board in making decisions.

The Group is organised into two operating segments. The water segment comprises the regulated water and wastewater services undertaken by South West Water and the regulated water services undertaken by Bristol Water. The non-household retail business reflects the services provided by Pennon Water Services.

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Notes (continued)

3. Segmental information (continued)

Separate disclosures for Bristol Water Group on a stand-alone basis are also provided below as additional information.

The profit recognised on disposal of the Viridor business is provided in note 14.

| | 2022 | 2021 |
|---------------------------------------------------------------------------------------------------------------|---------------|--------|
| | £m | £m |
| Revenue | | |
| Water | 687.8 | 563.0 |
| Non-household retail | 195.3 | 162.8 |
| Other | 8.5 | 5.6 |
| Less intra-segment trading | (99.3) | (86.8) |
| Total underlying revenue | 792.3 | 644.6 |
| Water non-underlying revenue (note 4) | - | (20.5) |
| | 792.3 | 624.1 |
| | | |
| Operating profit/(loss) before depreciation, amortisation and non-underlying items (underlying EBITDA) | | |
| Water | 385.0 | 340.6 |
| Non-household retail | 3.4 | 1.4 |
| Other | (4.5) | (7.3) |
| | 383.9 | 334.7 |
| | | |
| Operating profit/(loss) before non-underlying items | | |
| Water | 244.0 | 222.3 |
| Non-household retail | | 0.7 |
| Other | (9.4) | (7.7) |
| | 237.2 | 215.3 |
| | | |
| Profit/(loss) before tax before non-underlying items | | |
| Water | 146.0 | 164.6 |
| Non-household retail | 1.0 | (1.0) |
| Other | (3.5) | (6.6) |
| | 143.5 | 157.0 |
| | | |
| Profit/(loss) before tax | | |
| Water | 144.0 | 140.6 |
| Non-household retail | 1.0 | (1.0) |
| Other | (17.3) | (7.5) |
| | 127.7 | 132.1 |

Intra-segment trading between different segments is under normal market based commercial terms and conditions. Intra-segment revenue of the other segment is at cost.

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Notes (continued)

3. Segmental information (continued)

All revenue is generated in the United Kingdom. The grouping of revenue streams by how they are affected by economic factors, as required by IFRS 15, is as follows:

| Year ended 31 March 2022 | Water | Non-household retail | Other | Total |
|---------------------------------|---------------|-----------------------------|--------------|---------------|
| | £m | £m | £m | £m |
| Segment revenue (underlying) | 687.8 | 195.3 | 8.5 | 891.6 |
| Inter-segment revenue | (90.9) | (0.2) | (8.2) | (99.3) |
| Revenue from external customers | 596.9 | 195.1 | 0.3 | 792.3 |
| Significant service lines | | | | |
| Water | 596.9 | - | - | 596.9 |
| Non-household retail | - | 195.1 | - | 195.1 |
| Other | - | - | 0.3 | 0.3 |
| | 596.9 | 195.1 | 0.3 | 792.3 |

| Year ended 31 March 2021 | Water | Non-household retail | Other | Total |
|-------------------------------------------|--------------|-----------------------------|--------------|--------------|
| | £m | £m | £m | £m |
| Segment revenue (underlying) | 563.0 | 162.8 | 5.6 | 731.4 |
| Segment revenue (non-underlying) (note 4) | (20.5) | - | - | (20.5) |
| Inter-segment revenue | (81.6) | (0.4) | (4.8) | (86.8) |
| Revenue from external customers | 460.9 | 162.4 | 0.8 | 624.1 |
| Significant service lines | | | | |
| Water | 460.9 | - | - | 460.9 |
| Non-household retail | - | 162.4 | - | 162.4 |
| Other | - | - | 0.8 | 0.8 |
| | 460.9 | 162.4 | 0.8 | 624.1 |

Amounts included in the Water segment in respect of Bristol Water Group

| | Year ended 31 March 2022 |
|-------------------------------------------------------------------------------------------------|---------------------------------|
| | £m |
| Segment revenue | 104.4 |
| Inter-segment revenue | (0.5) |
| Revenue from external customers | 103.9 |
| Operating profit before depreciation, amortisation and non-underlying items (Underlying EBITDA) | 53.3 |
| Operating profit before non-underlying items | 29.3 |
| Profit before tax before non-underlying items | 9.2 |
| Profit before tax | 9.2 |

PENNON GROUP PLC

Notes (continued)

4. 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 in the year and business trends over time. The presentation of results is consistent with internal performance monitoring.

| | 2022 | 2021 |
|---------------------------------------------------------------------|----------------|--------|
| | £m | £m |
| Revenue | | |
| WaterShare+ ⁽¹⁾ | - | (20.5) |
| Operating Costs | | |
| Bristol Water acquisition costs ⁽²⁾ | (8.9) | - |
| CMA merger review and integration costs ⁽²⁾ | (6.9) | - |
| Pension curtailment charge ⁽³⁾ | - | (4.4) |
| Earnings before interest, tax, depreciation and amortisation | (15.8) | (24.9) |
| Net tax credit arising on non-underlying items above | 1.3 | 4.8 |
| Deferred tax change in rate ⁽⁴⁾ | (99.5) | - |
| Net non-underlying charge | (114.0) | (20.1) |

- (1) In September 2020, the Group offered its WaterShare+ scheme to its customers whereby customers could choose to accept a credit on their bill or take shares in Pennon Group plc. The value of the rebate equated to £20 per customer and the total value of £20.5 million was recognised in full as a non-underlying reduction to revenue in the year ended 31 March 2021. £19.3 million of the WaterShare+ credits were taken as credits on customers' bills, with the balance of £1.2 million being taken as shares in Pennon Group plc. This item was non-underlying in nature given its individual size and its non-recurring nature.
- (2) The Group incurred expenses of £15.8 million in the year ended 31 March 2022. £8.9 million of costs in connection with the acquisition of Bristol Water and £6.9 million on the resulting merger review by the Competition and Markets Authority and other integration costs, £1.7 million of which were employment costs.
- (3) In the year ended 31 March 2021 the Group completed its employee consultation to modernise its ongoing pension arrangements. The outcome of the consultation resulted in a decision to close Pennon's principal defined benefit pension scheme to future accrual with effect from 30 June 2021. This resulted in a curtailment charge of £4.4 million in 2021.
- (4) Following the Chancellor's Budget on 4 March 2021 and subsequent substantial enactment of the Finance Act on 24 May 2021, the UK's main rate of corporation tax will increase to 25% from 1 April 2023. All deferred tax assets and liabilities were therefore reviewed and where they crystallise after 1 April 2023 recalculated to crystallise at 25%, hence giving a non-underlying deferred tax charge of £99.5 million in 2022. This charge is considered non-underlying due to it arising from a material legislative change and its treatment is consistent with that applied in relation to previous changes in corporation tax rates.

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Notes (continued)

5. Net finance costs

| | 2022 Finance costs £m | 2022 Finance income £m | Total £m | Finance costs £m | 2021 Finance income £m | Total £m |
|------------------------------------|--------------------------------|---------------------------------|---------------|------------------------|---------------------------------|---------------|
| Cost of servicing debt | | | | | | |
| Bank borrowings and overdrafts | (73.9) | - | (73.9) | (32.6) | - | (32.6) |
| Interest element of lease payments | (20.3) | - | (20.3) | (25.7) | - | (25.7) |
| Other finance costs | (2.1) | - | (2.1) | (3.5) | - | (3.5) |
| Interest receivable | - | 2.0 | 2.0 | - | 4.2 | 4.2 |
| | (96.3) | 2.0 | (94.3) | (61.8) | 4.2 | (57.6) |
| Notional interest | | | | | | |
| Retirement benefit obligations | - | 0.6 | 0.6 | (0.7) | - | (0.7) |
| Net finance costs | (96.3) | 2.6 | (93.7) | (62.5) | 4.2 | (58.3) |

In addition to the above, finance costs of £1.3 million (2021 £0.9 million) have been capitalised on qualifying assets included in property, plant and equipment.

Other finance costs include £0.9 million (2021 nil) of dividends payable on listed preference shares issued by Bristol Water, which are classified as debt.

Excluded from the amounts above are net finance costs relating to discontinued operations of nil (2021 £89.7 million), consisting of finance income of nil (2021 £6.0 million) and finance costs of nil (2021 £95.7 million) (see note 14).

6. Taxation

| | Before non- underlying items 2022 £m | Non- underlying items (note 4) 2022 £m | Total 2022 £m | Before non- underlying items 2021 £m | Non- underlying items (note 4) 2021 £m | Total 2021 £m |
|-----------------------------------------------------------|--------------------------------------------------|-------------------------------------------------------|---------------------|--------------------------------------------------|-------------------------------------------------------|---------------------|
| Analysis of charge | | | | | | |
| Current tax charge / (credit) | 5.0 | (1.3) | 3.7 | 23.0 | (3.9) | 19.1 |
| Deferred tax - other | 8.9 | - | 8.9 | 6.6 | (0.9) | 5.7 |
| Deferred tax arising on change of rate of corporation tax | - | 99.5 | 99.5 | - | - | - |
| Deferred tax charge / (credit) | 8.9 | 99.5 | 108.4 | 6.6 | (0.9) | 5.7 |
| Tax charge / (credit) for the year | 13.9 | 98.2 | 112.1 | 29.6 | (4.8) | 24.8 |

UK corporation tax is calculated at 19% (2021 19%) of the estimated assessable profit for the year.

UK corporation tax is stated after a credit relating to prior year current tax of £1.7 million (2021 credit of £0.7 million) and a prior year deferred tax charge of £10.2 million (2021 £0.4 million charge). These items arise following discussion with and the subsequent submission of tax computations to HMRC. The largest adjustment relates to qualifying assets acquired in prior years, which are now being recognised.

PENNON GROUP PLC

Notes (continued)

7. 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 year, 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 in issue is adjusted to include all dilutive potential ordinary shares. The weighted average number of shares and earnings used in the calculations were:

| | 2022 | 2021 |
|-----------------------------------------------------------------|--------------|-------|
| Number of shares (millions) | | |
| For basic earnings per share | 312.1 | 421.1 |
| Effect of dilutive potential ordinary shares from share options | 1.7 | 1.6 |
| For diluted earnings per share | 313.8 | 422.7 |

Basic and diluted earnings per ordinary share

Earnings per ordinary share before non-underlying items and deferred tax are presented as the Directors believe this measure provides a more useful year on year comparison of business trends and performance. Deferred tax is excluded as the Directors believe it reflects a distortive effect of changes in corporation tax rates and the level of long-term capital investment. Earnings per share have been calculated as follows:

| Continuing and discontinued operations | 2022 | | | 2021 | | |
|-------------------------------------------------|---------------------------|--------------------|--------------|---------------------------|--------------------|--------------|
| | Profit after tax £m | Earnings per share | | Profit after tax £m | Earnings per share | |
| | | Basic p | Diluted p | | Basic p | Diluted p |
| Statutory earnings | 15.4 | 4.9 | 4.9 | 1,762.2 | 418.5 | 416.9 |
| Deferred tax charge before non-underlying items | 8.9 | 2.9 | 2.8 | 14.2 | 3.4 | 3.4 |
| Non-underlying items (net of tax) | 114.0 | 36.5 | 36.4 | (1,599.1) | (379.8) | (378.4) |
| Adjusted earnings | 138.3 | 44.3 | 44.1 | 177.3 | 42.1 | 41.9 |

| Continuing operations | 2022 | | | 2021 | | |
|-------------------------------------------------|---------------------------|--------------------|--------------|---------------------------|--------------------|--------------|
| | Profit after tax £m | Earnings per share | | Profit after tax £m | Earnings per share | |
| | | Basic p | Diluted p | | Basic p | Diluted p |
| Statutory earnings | 15.4 | 4.9 | 4.9 | 107.5 | 25.5 | 25.4 |
| Deferred tax charge before non-underlying items | 8.9 | 2.9 | 2.8 | 6.6 | 1.6 | 1.6 |
| Non-underlying items (net of tax) | 114.0 | 36.5 | 36.4 | 20.1 | 4.8 | 4.7 |
| Adjusted earnings | 138.3 | 44.3 | 44.1 | 134.2 | 31.9 | 31.7 |

PENNON GROUP PLC

Notes (continued)

8. Dividends

Amounts recognised as distributions to ordinary equity holders in the year:

| | 2022 | 2021 |
|------------------------------------------------------------------------------------------|----------------|-------|
| | £m | £m |
| Interim dividend paid for the year ended 31 March 2021: 6.77p (2020 13.66p) per share | 28.6 | 57.5 |
| Final dividend paid for the year ended 31 March 2021: 14.97p (2020 30.11p) per share | 63.2 | 126.8 |
| Special dividend paid for the year ended 31 March 2021: 355.0p (2020 nil) per share | 1,498.5 | - |
| | 1,590.3 | 184.3 |
| Proposed dividends | | |
| Interim dividend paid for the year ended 31 March 2022: 11.70p (2021 6.77p) per share | 32.4 | 28.6 |
| Final dividend paid for the year ended 31 March 2022: 26.83p (2021 14.97p) per share | 69.6 | 63.2 |
| | 102.0 | 91.8 |

The proposed interim and final dividends have not been included as liabilities in these financial statements.

The proposed interim dividend for 2022 was paid on 5 April 2022 and the proposed final dividend is subject to approval by shareholders at the Annual General Meeting.

9. Share capital

Allotted, called up and fully paid

| | Number of shares | | £m |
|---------------------------------------------------------------------------------------|------------------|--------------------|--------------|
| | Treasury shares | Ordinary shares | |
| At 1 April 2020 ordinary shares of 40.7p each | 8,443 | 421,036,557 | 171.3 |
| For consideration of £5.6 million, shares issued under the Company's Sharesave Scheme | - | 1,083,624 | 0.5 |
| At 31 March 2021 ordinary shares of 40.7p each | 8,443 | 422,120,181 | 171.8 |
| Share consolidation | (2,815) | (140,708,916) | - |
| For consideration of £3.8 million, shares issued under the Company's Sharesave Scheme | - | 582,427 | 0.4 |
| Shares cancelled | - | (17,146,744) | (10.5) |
| At 31 March 2022 ordinary shares of 61.05p each | 5,628 | 264,846,948 | 161.7 |

PENNON GROUP PLC**Notes (continued)****9. Share capital (continued)**

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

On 16 July 2021, the Group paid a special dividend of £1.5 billion to shareholders in relation to the return of capital to shareholders announced on 3 June 2021. In order to maintain the comparability of the Company's share price before and after the special dividend, a share consolidation was approved at the General Meeting held on 28 June 2021. Shareholders received 2 New Ordinary shares of 61.05 pence each for every 3 Existing Ordinary shares of 40.7 pence each.

During the year, the Group announced and began a process to purchase ordinary shares at an aggregate cost of £400 million by September 2022. During the year the Group purchased £199.6 million of ordinary shares from the market at an average ordinary share price of 1,164 pence. The shares acquired under the tender offer were immediately cancelled, creating a capital redemption reserve of £10.5 million. The maximum number of shares that can be repurchased in connection with the Programme is 42,183,689 (being the maximum authority granted by Pennon's shareholders at Pennon's AGM on 22 July 2021).

PENNON GROUP PLC

Notes (continued)

10. Cash flow from operating activities

Reconciliation of profit for the year to cash generated from operations:

| | 2022 | 2021 |
|---------------------------------------------------------------|---------------|-----------|
| | £m | £m |
| Cash generated from operations | | |
| Profit for the year | 15.6 | 1,762.0 |
| Adjustments for: | | |
| Share-based payments | 2.2 | 3.1 |
| Profit on disposal of property, plant and equipment | (1.0) | (0.1) |
| Profit on disposal of discontinued operations | - | (1,682.7) |
| Depreciation charge | 143.3 | 119.2 |
| Amortisation of intangible assets | 3.4 | 0.2 |
| Continuing Group: | | |
| - non-underlying pension items | - | 4.4 |
| - non-underlying Bristol Water acquisition costs | 8.9 | - |
| - non-underlying CMA merger review and integration costs | 6.9 | - |
| Discontinued operations: | | |
| - non-underlying pension items | - | (5.6) |
| - non-underlying restructuring costs and share scheme charges | - | 6.8 |
| - non-underlying debt retirement costs | - | 74.4 |
| Share of post-tax profit from joint ventures | - | (4.3) |
| Finance income (before non-underlying items) | (2.6) | (10.1) |
| Finance costs (before non-underlying items) | 96.3 | 83.7 |
| Taxation charge | 112.1 | 20.5 |
| Changes in working capital: | | |
| Increase in inventories | (0.6) | (4.0) |
| (Increase) / decrease in trade and other receivables | (14.3) | (42.4) |
| Increase in service concession arrangements receivable | - | (3.8) |
| (Decrease) / increase in trade and other payables | (12.2) | 27.4 |
| Decrease in retirement benefit obligations from contributions | (24.2) | (47.3) |
| Increase / (decrease) in provisions | 0.4 | (3.3) |
| Cash generated from operations | 334.2 | 298.1 |
| Cash generated from operations comprises: | | |
| Cash generated from discontinued operations | - | 28.7 |
| Cash generated from the Continuing Group | 334.2 | 269.4 |
| Cash generated from operations | 334.2 | 298.1 |
| Total interest paid | 2022 | 2021 |
| | £m | £m |
| Interest paid in operating activities | 74.6 | 80.2 |
| Interest paid in investing activities | 1.3 | 0.9 |
| Total interest paid | 75.9 | 81.1 |

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Notes (continued)

10. Cash flow from operating activities (continued)

The above includes the entire Group, including cash flows relating to the discontinued operations business. Disaggregated information relating to the discontinued business is provided in note 14.

During the year, the Group completed a number of sale and leaseback transactions in respect of its infrastructure assets as part of its ongoing finance arrangements. Cash proceeds of £15.0 million (2021 £15.0 million) were received and a gain of nil (2021 nil) was recognised. These assets are primarily being leased back over an initial 10-year lease term at market rentals.

11. Net borrowings

| | 2022 £m | 2021 £m |
|---------------------------------------|------------------|------------|
| Cash and cash deposits | 519.0 | 2,919.3 |
| <i>Borrowings – current</i> | | |
| Bank and other current borrowings | (70.0) | (40.1) |
| Lease obligations | (170.2) | (48.2) |
| Total current borrowings | (240.2) | (88.3) |
| <i>Borrowings – non-current</i> | | |
| Bank and other non-current borrowings | (1,907.4) | (1,375.7) |
| Listed preference shares | (12.5) | - |
| Lease obligations | (1,041.8) | (1,391.0) |
| Total non-current borrowings | (2,961.7) | (2,766.7) |
| Total net (borrowings) / cash | (2,682.9) | 64.3 |

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

| | 2022 £m | 2021 £m |
|---------------------------------------------------------------------------|--------------|------------|
| Cash and cash deposits as above | 519.0 | 2,919.3 |
| Less: deposits with a maturity of three months or more (restricted funds) | (167.8) | (250.8) |
| | 351.2 | 2,668.5 |

12. Contingencies

Contingent liabilities

| | 2022 £m | 2021 £m |
|-------------------------------|------------|------------|
| Guarantees: Performance bonds | 9.7 | - |

Guarantees in respect of performance bonds in 2022 relate to changes to the collateral requirements for the non-household retail business with other wholesalers.

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Notes (continued)

12. Contingencies (continued)

Other contractual and litigation uncertainties

Ofwat and the Environment Agency announced an industry-wide investigation into sewage treatment works on 18 November 2021. Since that time, Ofwat announced enforcement actions against certain companies. South West Water was not one of those companies but Ofwat have stated that their industry-wide investigation continues. The Environment Agency investigation is ongoing. The potential outcome of these investigations remains unknown.

The Group establishes provisions in connection with contracts and litigation where it has a present legal or constructive obligation as a result of past events 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. Where it is uncertain that these conditions are met a contingent liability is disclosed unless the likelihood of the obligation arising is remote or the matter is not deemed material.

13. Acquisition of Bristol Water Group

On 2 June 2021, the Company acquired 100% of the issued share capital and voting rights of Bristol Water Holdings UK Limited, the holding company of the Bristol Water Group. Bristol Water Group comprises Bristol Water plc, a regulated water only company and a 30% share in water2business Limited, a joint venture with Wessex Water. The purpose of the acquisition was to grow the Group's core water business by expanding into a geographically contiguous region. The acquisition of the Bristol Water Group was reviewed by the Competition and Markets Authority and given full clearance on 7 March 2022. The Bristol Water Group is consolidated in Pennon's accounts with effect from the completion of acquisition at midnight on 2 June 2021.

The details of the business combination are as follows:

| | £m |
|--------------------------------------------------------------------|--------------|
| Fair value of consideration transferred | |
| Amount settled in cash | <u>419.6</u> |
| Recognised amounts of identifiable net assets | |
| Property, plant and equipment | 944.8 |
| Intangible assets | 12.8 |
| Other non-current assets | 9.9 |
| Inventories | 1.7 |
| Trade and other receivables | 22.3 |
| Cash and cash deposits (including restricted cash of £6.1 million) | 18.9 |
| Current tax liability | (2.2) |
| Borrowings | (545.1) |
| Trade and other payables | (32.3) |
| Provisions | (0.3) |
| Retirement benefit obligations | 7.8 |
| Deferred tax liabilities | (134.8) |
| Identifiable net assets | <u>303.5</u> |
| Goodwill on acquisition | <u>116.1</u> |
| Consideration for equity settled in cash | 419.6 |
| Payment to acquire loan to former parent | 5.5 |
| Cash and cash equivalents acquired (excluding restricted cash) | (12.8) |
| Net cash outflow on acquisition | <u>412.3</u> |
| Acquisition costs paid charged to expenses | 8.9 |
| Net cash paid relating to the acquisition | <u>421.2</u> |

Notes (continued)

13. Acquisition of Bristol Water Group (continued)

Acquisition related costs of £8.9 million are not included as part of the consideration transferred and have been recognised as an expense in the consolidated income statement within other operating expenses.

The fair value of trade and other receivables acquired as part of the business combination amounted to £22.3 million with a gross contractual amount of £38.9 million. At the acquisition date the Group's best estimate of the contractual cash flows expected not to be collected amounted to £16.6 million. As part of the acquisition of Bristol Water, the Group acquired interests in two joint ventures, Bristol Wessex Billing Services Limited ("BWBSL") and water2business Limited ("water2business"). These two interests are accounted for using the equity method. Currently the carrying values of these investments equates to nil representing the relevant share of the net assets of each of these interests.

Fair values on acquisition have been updated from those disclosed at half year results to 30 September 2021, with some changes being required, primarily to the acquired tax balances. This has led to a reduction in the total value of goodwill recognised on acquisition by £2.3 million.

The goodwill that arose on the acquisition can be attributed to synergies expected to be derived from the combination and the value of the workforce which cannot be recognised as an intangible asset. Goodwill has been allocated to the water segment. The goodwill arising is not expected to be tax deductible. From the date of acquisition on 2 June 2021, Bristol Water Group contributed £103.9 million (excluding £0.5 million intercompany revenue as outlined in note 3) and £9.2 million to the Group's revenue and profits before tax respectively. Had the acquisition occurred on 1 April 2021, the contribution to the Group's revenue would have been £124.6 million and the contribution to the Group's profit before tax for the period would have been £11.1 million.

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Notes (continued)
14. Discontinued operations

On 18 March 2020, the Group entered into a formal sale agreement to dispose of Viridor Limited to Planets UK Bidco Limited (Bidco), a newly formed company established by funds advised by Kohlberg Kravis Roberts & Co. L.L.P. (KKR). The Viridor business which represented the entirety of the waste operating segment was classified as a discontinued operation at that date. Consequently, Viridor has not been presented as an operating segment in the segment note. The sale completed on 8 July 2020 and the results of the discontinued operation and the effect of the disposal on the financial position of the Group were as follows:

| | Before non- underlying items 2022 £m | Non- underlying items (see below) 2022 £m | Total 2022 £m | Before non- underlying items (see below) 2021 £m | Non-underlying items 2021 £m | Total 2021 £m |
|-------------------------------------------------------------------------|--------------------------------------------------|----------------------------------------------------------|---------------------|-----------------------------------------------------------------|---------------------------------------|---------------------|
| Discontinued operations | | | | | | |
| Revenue | - | - | - | 192.2 | - | 192.2 |
| Operating costs | | | | | | |
| Employment costs | - | - | - | (34.4) | 0.5 | (33.9) |
| Raw materials and consumables used | - | - | - | (22.4) | - | (22.4) |
| Other operating expenses | - | - | - | (81.1) | (1.7) | (82.8) |
| Earnings before interest, tax, depreciation and amortisation | - | - | - | 54.3 | (1.2) | 53.1 |
| Depreciation and amortisation | - | - | - | - | - | - |
| Operating profit | - | - | - | 54.3 | (1.2) | 53.1 |
| Finance income | - | - | - | 6.0 | - | 6.0 |
| Finance costs | - | - | - | (21.3) | (74.4) | (95.7) |
| Net finance costs | - | - | - | (15.3) | (74.4) | (89.7) |
| Share of post-tax profit from joint ventures | - | - | - | 4.3 | - | 4.3 |
| Profit/(loss) before tax | - | - | - | 43.3 | (75.6) | (32.3) |
| Taxation (charge)/credit | - | - | - | (7.8) | 12.1 | 4.3 |
| Profit/(loss) from operating activities, net of tax | - | - | - | 35.5 | (63.5) | (28.0) |
| Gain on sale of discontinued operation | - | - | - | - | 1,682.7 | 1,682.7 |
| Profit from discontinued operations, net of tax | - | - | - | 35.5 | 1,619.2 | 1,654.7 |
| Attributable to: | | | - | | | - |
| Ordinary shareholders of the parent | | | - | | | 1,654.7 |

Non-underlying items

Non-underlying items in 2021 represent employment costs (restructuring, accelerated share scheme charges and a settlement gain on transfer of pension liabilities), other operating restructuring costs and finance costs relating to debt retirements of £74.4 million, together with the related taxation credit.

| | 2022 £m | 2021 £m |
|-------------------------------------------------------------------------|------------|------------|
| Cash flows used in discontinued operations | | |
| Cash generated from operations | - | 28.7 |
| Interest paid | - | (17.6) |
| Tax paid | - | (4.4) |
| Cash flows from operating activities | - | 6.7 |
| Cash flows from investing activities | - | (24.0) |
| Cash flows from financing activities | - | (79.2) |
| Net cash flows from discontinued operations, net of intercompany | - | (96.5) |

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Notes (continued)

14. Discontinued operations (continued)

Effect of disposal of the financial position of the Group

The net assets relating to the Disposal Group at the date of disposal and the gain on disposal are shown below.

| | 2021 £m |
|------------------------------------------------------------------------|----------------|
| Net assets disposed of and gain on disposal | |
| Goodwill | 340.8 |
| Other intangible assets | 86.9 |
| Property, plant and equipment | 1,619.2 |
| Other non-current assets | 266.7 |
| Investments in joint ventures | 64.4 |
| Inventories | 33.4 |
| Trade and other receivables | 298.7 |
| Current tax asset | 0.6 |
| Cash and cash deposits | 61.7 |
| Total assets | <u>2,772.4</u> |
| Borrowings | (240.7) |
| Trade and other payables | (157.7) |
| Provisions | (236.8) |
| Other non-current liabilities | (12.7) |
| Retirement benefit obligations | 1.5 |
| Deferred tax liabilities | (109.4) |
| Total liabilities | <u>(755.8)</u> |
| Net assets disposed of | <u>2,016.6</u> |
| Consideration received in cash, net of transaction costs | 3,690.2 |
| Deferred consideration | 9.2 |
| Gain on sale before income tax and reclassification of reserves | <u>1,682.8</u> |
| Items previously recognised in equity recycled to the income statement | (0.1) |
| Gain on sale of discontinued operation | <u>1,682.7</u> |
| Net cash inflow arising on disposal | |
| Consideration received in cash, net of transaction costs | 3,690.2 |
| Less cash and cash deposits disposed of | (61.7) |
| | <u>3,628.5</u> |

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Notes (continued)

14. Discontinued operations and non-current assets held for sale (continued)

Deferred consideration

Under the sale agreement deferred consideration may be receivable in future. The fair value of the amount expected to be received at 31 March 2021 has been estimated at £9.2 million and this amount was received in the financial year ended 31 March 2022. The receipt of further deferred consideration remains possible, albeit the likelihood is judged as not probable and has therefore not been recognised in the financial statements.

Taxation on the discontinued operations

The gain on sale of discontinued operations qualified for Substantial Shareholding Exemption and consequently was not subject to corporation tax. The taxation charge from discontinued operations before non-underlying items in 2021 of £7.8 million includes a deferred tax charge of £7.6 million.

Pennon Group plc
Registered office:
Peninsula House
Rydon Lane
Exeter
Devon
EX2 7HR
pennon-group.co.uk

Registered in England: 2366640

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Alternative performance measures

Alternative performance measures (APMs) are financial measures used in this report that are not defined by International Financial Reporting Standards (IFRS). The Directors believe that these APMs assist in providing additional useful information on the underlying trends, performance and position of the Group as well as enhancing the comparability of information between reporting periods.

As the Group defines the APMs they might not be directly comparable to other companies' APMs. They are not intended to be a substitute for, or superior to, IFRS measurements. The following APMs have been added or amended to those presented previously to reflect the changing nature of the Group following the sale of Viridor in July 2020 and the acquisition of Bristol Water in June 2021:

- An APM for 2021/22 has been added for Basic adjusted earnings per share – Continuing Operations (adjusted for share consolidation). To aid comparability, this new APM, which is presented on a basis other than in accordance with IAS 33, includes the full impact of the share consolidation as if it had taken place at the start of the previous financial year and recalculates the resulting Adjusted earnings per share measure.
- The APM for effective interest rate has been expanded to outline the calculation for the effective interest rate of South West Water Limited, Bristol Water Group and together the water business segment. In previous periods South West Water Limited was presented. This change has been made to reflect the acquisition of Bristol Water and the resulting combined effective interest rate of the water business.
- The APM 'Group return on capital employed' has been changed to 'South West Water return on capital employed' due to this metric providing a more meaningful comparison of performance due to the Group holding a net cash position at 31 March 2021.

(i) Underlying earnings

Underlying earnings are presented alongside statutory results as the Directors believe they provide a more useful comparison on business trends and performance. Note 4 in the notes to the financial statements provides more detail on non-underlying items, and a reconciliation of underlying earnings for the current year and the prior year is as follows:

| Underlying earnings reconciliation 31 March 2022 | Underlying £m | Non-underlying items | | Statutory results £m | Earnings per share p |
|-----------------------------------------------------|------------------|-----------------------------------------|----------------------------------------------------|----------------------------|----------------------------|
| | | Deferred tax change of rate £m | Acquisition and merger review costs £m | | |
| EBITDA (see below) | 383.9 | - | (15.8) | 368.1 | |
| Operating profit | 237.2 | - | (15.8) | 221.4 | |
| Profit before tax | 143.5 | - | (15.8) | 127.7 | |
| Taxation | (13.9) | (99.5) | 1.3 | (112.1) | |
| Profit after tax | | | | 15.6 | |
| Non-controlling interests | | | | (0.2) | |
| Profit after tax attributable to shareholders | | | | 15.4 | 4.9 |

| Underlying earnings reconciliation 31 March 2021 | Underlying £m | Non-underlying items | | Statutory results £m | Earnings per share p |
|-----------------------------------------------------|------------------|-----------------------|----------------------------------------|----------------------------|----------------------------|
| | | WaterShare + £m | Pension curtailment charge £m | | |
| EBITDA (see below) | 334.7 | (20.5) | (4.4) | 309.8 | |
| Operating profit | 215.3 | (20.5) | (4.4) | 190.4 | |
| Profit before tax | 157.0 | (20.5) | (4.4) | 132.1 | |
| Taxation | (29.6) | 3.9 | 0.9 | (24.8) | |
| Profit after tax from continuing operations | | | | 107.3 | |
| Profit after tax from discontinued operations | | | | 1,654.7 | |
| Profit after tax | | | | 1,762.0 | |
| Non-controlling interests | | | | 0.2 | |
| Profit after tax attributable to shareholders | | | | 1,762.2 | 418.5 |

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Alternative performance measures (continued)

(ii) Underlying EBITDA

Underlying EBITDA (earnings before interest, tax, depreciation and amortisation and non-underlying items) is used to assess and monitor operational underlying performance.

(iii) Basic adjusted earnings per share – Continuing Operations (adjusted for share consolidation)

| | 2022 | 2021 |
|----------------------------------------------------------------------------------------------------------------------------------------------------------|---------------|---------|
| Basic weighted average number of shares | | |
| Basic weighted average number of shares (millions) (note 8) | 312.1 | 421.1 |
| Adjustment to reflect the post-consolidation share base as if it had been in place from the start of the previous financial year (millions) | (36.6) | (140.4) |
| Adjusted basic weighted average number of shares (adjusted for share consolidation) (millions) | 275.5 | 280.7 |
| Basic adjusted earnings per share from continuing operations before exceptional items and deferred tax (pence) (note 8) | 44.3 | 31.9 |
| Adjustment to reflect the post-consolidation share base as if it had been in place from the start of the previous financial year (pence) | 5.9 | 15.9 |
| Basic adjusted earnings per share from continuing operations before exceptional items and deferred tax (adjusted for share consolidation) (pence) | 50.2 | 47.8 |

(iv) Effective interest rate

A measure of the mean average interest rate payable on net debt, which excludes interest costs not directly associated with net debt. This measure is presented to assess and monitor the relative cost of financing for South West Water Limited, Bristol Water Group and together the water business.

South West Water Limited

A measure of the mean average interest rate payable on South West Water Limited's net debt, which excludes interest costs not directly associated with South West Water Limited net debt. This measure is presented to assess and monitor the relative cost of financing for South West Water Limited.

| | 2022 | 2021 |
|---------------------------------------------------------------------|----------------|---------|
| | £m | £m |
| Net finance costs after non-underlying items | 76.8 | 56.5 |
| Net interest on retirement benefit obligations | 0.4 | (0.4) |
| Capitalised interest | 1.0 | 0.9 |
| Net finance costs for effective interest rate calculation | 78.2 | 57.0 |
| Opening net debt | 2,273.5 | 2,307.2 |
| Closing net debt | 2,305.2 | 2,273.5 |
| Average net debt (opening net debt + closing net debt divided by 2) | 2,289.4 | 2,290.4 |
| Effective interest rate (%) | 3.4 | 2.5 |

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Alternative performance measures (continued)

(iv) Effective interest rate (continued)

Bristol Water Group

A measure of the mean average interest rate payable on Bristol Water Group's net debt, which excludes interest costs not directly associated with Bristol Water Group net debt. This measure is presented to assess and monitor the relative cost of financing for Bristol Water Group and includes full year performance.

| | 2022 |
|-----------------------------------------------------------------------------------------|--------------|
| | £m |
| Net finance costs after non-underlying items (from 3 June 2021) | 20.1 |
| Net interest on retirement benefit obligations (from 3 June 2021) | (0.2) |
| Capitalised interest (from 3 June 2021) | 0.3 |
| Net finance costs for effective interest rate calculation (from 3 June 2021) | 20.2 |
| Net finance costs for effective interest rate calculation (1 April 2021 to 2 June 2021) | 2.4 |
| Net finance costs for effective interest rate calculation | 22.6 |
| Opening net debt ⁽¹⁾ | 395.6 |
| Closing net debt | 405.3 |
| Average net debt (opening net debt + closing net debt divided by 2) | 400.5 |
| Effective interest rate (%) | 5.6 |

(1) Opening net debt of £395.6 million reflects 31 March 2021 Bristol Water Group net debt. On acquisition on 2 June 2021, Bristol Water Group's net debt was £391.4 million. Net debt excludes fair value adjustments.

Water business

A combined measure reflecting the mean average interest rate payable on the water business' net debt, which excludes interest costs not directly associated with water business net debt. This measure is presented to assess and monitor the combined relative cost of financing for the water business.

| | 2022 | 2021 |
|---------------------------------------------------------------------|----------------|---------|
| | £m | £m |
| Net finance costs for effective interest rate calculation | 100.8 | 57.0 |
| Opening net debt (at 31 Mar 2021) | 2,669.1 | 2,307.2 |
| Closing net debt | 2,710.5 | 2,273.5 |
| Average net debt (opening net debt + closing net debt divided by 2) | 2,689.8 | 2,290.4 |
| Effective interest rate (%) | 3.7 | 2.5 |

(v) Underlying interest cover

Underlying net finance costs (excluding pensions net interest cost) divided by operating profit before non-underlying items.

| | 2022 | 2021 |
|---------------------------------------------------------|--------------|-------|
| | £m | £m |
| Net finance costs after non-underlying items | 93.7 | 58.3 |
| Net interest on retirement benefit obligations | 0.6 | (0.7) |
| Net finance costs for interest cover calculation | 94.3 | 57.6 |
| Operating profit before non-underlying items | 237.2 | 215.3 |
| Interest cover (times) | 2.5 | 3.7 |

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Alternative performance measures (continued)

(vi) Group dividend cover

Proposed dividends divided by profit for the year before non-underlying items and deferred tax

| | 2022 | 2021 |
|-----------------------------------------------------------|--------------|-----------|
| | £m | £m |
| Proposed dividends | 102.0 | 91.8 |
| Profit for the year attributable to ordinary shareholders | 15.4 | 1,762.2 |
| Deferred tax charge before non-underlying items | 8.9 | 14.2 |
| Non-underlying items after tax in profit for the year | 114.1 | (1,599.1) |
| Adjusted profit for dividend cover calculations | 134.8 | 177.3 |
| Dividend cover (times) | 1.4 | 1.9 |

(vii) Capital investment

Property, plant and equipment and intangible asset additions. The measure is presented to assess and monitor the total capital investment by the Group.

| | 2022 | 2021 |
|--------------------------------------------|--------------|-------|
| | £m | £m |
| Additions to property, plant and equipment | 237.3 | 168.4 |
| Additions to intangible assets | 3.6 | 0.2 |
| Capital investment | 240.9 | 168.6 |

(viii) Capital payments

Payments for property, plant and equipment (PPE) and intangible asset additions net of proceeds from sale of PPE and intangible assets. The measure is presented to assess and monitor the net cash spend on PPE and intangible assets.

| | 2022 | 2021 |
|---------------------------------------------------------------------------|--------------|--------|
| | £m | £m |
| Cash flow statements: purchase of property, plant and equipment | 225.6 | 190.1 |
| Cash flow statements: purchase of intangible assets | 3.4 | 0.2 |
| Cash flow statements: proceeds from sale of property, plant and equipment | (1.4) | (0.4) |
| Capital payments relating to the Total Group | 227.6 | 189.9 |
| Capital payments relating to discontinued operations | - | (32.3) |
| Capital payments relating to continuing operations | 227.6 | 157.6 |

(ix) South West Water return on capital employed

The total of underlying operating profit divided by capital employed (net debt plus total equity invested). An average value for this metric is part of the long-term incentive plan for Directors.

| | 2022 | 2021 |
|--------------------------------------------------------------------|----------------|---------|
| | £m | £m |
| Underlying operating profit – South West Water | 214.5 | 222.3 |
| Capital employed: | | |
| Net debt | 2,233.8 | 2,198.6 |
| Total equity invested | 295.9 | 250.9 |
| Capital employed for return on capital employed calculation | 2,529.7 | 2,449.5 |
| Return on capital employed (%) | 8.5 | 9.1 |

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Alternative performance measures (continued)

(x) Continuing operations operational cash inflows and other movements

Cash generated from operations before pension contributions and other movements.

| | 2022 | 2021 |
|-------------------------------------------------------------------------------|--------------|--------|
| | £m | £m |
| Cash generated from operations per cash flow statements | 334.2 | 298.1 |
| Remove: cash generated from discontinued operations | - | (28.7) |
| Cash generated from operations from the Continuing Group | 334.2 | 269.4 |
| Other movements ⁽¹⁾ | 2.6 | (3.6) |
| Pension contributions | 27.9 | 50.2 |
| Operational cash inflows and other movements from the Continuing Group | 364.7 | 316.0 |

(1) Other movements reflect operational movements not related to operating cash flows, such as proceeds from share issues and share trust purchases for the employee share schemes.

(xi) Return on Regulated Equity (RoRE)

This is a key regulatory metric which represents the returns to shareholders expressed as a percentage of regulated equity.

Returns are made up of a base return (set by Ofwat, the water business regulator, at c.3.9% for South West Water and c.4.4% for Bristol Water for the period 2020-25) plus totex outperformance, financing outperformance and ODI outperformance. Returns are calculated post tax and post sharing (only a proportion of returns are attributed to shareholders and shown within RoRE). The three different types of return calculated and added to the base return are:

- Totex outperformance – totex is defined below and outperformance is the difference between actual reported results for the regulated business compared to the Final Determination (Ofwat published document at the start of a regulatory period), in a constant price base
- Financing outperformance – is based on the difference between a company's actual effective interest rate compared with Ofwat's allowed cost of debt
- ODI outperformance – the net reward or penalty a company earns based on a number of different key performance indicators, again set in the Final Determination.

Regulated equity is a notional proportion of regulated capital value (RCV which is set by Ofwat at the start of every five-year regulatory period, adjusted for actual inflation). For 2020-25, the notional equity proportion is 40.0%.

References are made to Ofwat RoRE and Watershare RoRE which utilise differing inflation assumptions and the disclosure of tax.

Further information on this metric can be found in South West Water and Bristol Water's annual performance report and regulatory reporting, published in July each year.

(xii) Totex

Operating costs and capital expenditure of the regulated water and wastewater business (based on the Regulated Accounting Guidelines).

(xiii) Outcome Delivery Incentive (ODIs)

ODIs are designed to incentivise companies to deliver improvements to service and outcomes based on customers' priorities and preferences. If a company exceeds these targets a reward can be earned through future higher revenues. If a company fails to meet them, they can incur a penalty through lower future allowed revenues.