

27 November 2018

**Half Year Results 2018/19
for the period ended 30 September 2018**

Delivering for customers, communities and shareholders

Chris Loughlin, Pennon Chief Executive said:

“Momentum for Pennon continues with a strong performance in the first half of 2018/19 across both water and waste. We are delivering on our promises to customers and communities and our investment across the Group is driving tangible and positive results.

In water, we demonstrated our service resilience in extreme weather conditions, with the aftermath of the exceptional cold weather in March followed by the hottest summer on record. Our focus on customers has been reflected in South West Water’s best ever customer service score for this half year. With a relentless focus on efficiency and cost savings, average bills are lower than they were 9 years ago, with a further 11% decrease expected in the next regulatory period 2020-2025 under our new business plan. Customers will be empowered as part of a New Deal giving them a tangible stake and say in South West Water.

The focus for Viridor is UK recycling and residual waste processing and transformation. Waste market dynamics are favourable, with the ‘Blue Planet’ effect spurring action, and we are optimistic that positive changes will be announced in the Government’s Resources & Waste Strategy later this year enabling a UK recycling system fit for the future. The operating fleet of Energy Recovery Facilities (ERFs) is performing well, transforming waste into electricity and heat. Progress continues bringing Viridor’s remaining four ERFs in the portfolio on stream, with three now in operational ramp up and the final facility under construction. We have further consolidated our position through increasing our holding in one of our joint venture ERFs, Runcorn I. The development of Viridor’s ERF portfolio will support Pennon’s earnings growth to 2020 and beyond”.

Financial Highlights

Underlying ¹	H1 2018/19	H1 2017/18	Change
Revenue	£746.7m	£723.9m	+3.1%
EBITDA ²	£274.0m	£253.5m	+8.1%
Adjusted EBITDA ³	£294.7m	£285.8m	+3.1%
Operating profit	£178.5m	£162.4m	+9.9%
Profit before tax (PBT)	£142.5m	£131.1m	+8.7%
Non-underlying items before tax ⁴	(£8.9m)	(£1.3m)	-
Statutory profit before tax	£133.6m	£129.8m	+2.9%
Tax	(£17.6m)	(£17.5m)	(0.6%)
Statutory profit after tax (PAT)	£116.0m	£112.3m	+3.3%
Earnings per share ⁵	30.0p	25.3p	+18.6%
Statutory earnings per share	25.6p	21.8p	+17.4%
Dividend per share ⁶	12.84p	11.97p	+7.3%

Pennon Group

- Pennon is on track to meet management expectations for full year 2018/19
- Underlying PBT up +8.7% following:
 - Higher revenues and EBITDA at South West Water reflecting increased customer demand over the summer
 - Continued cost saving focus, leading to Total Expenditure (Totex) outperformance, at South West Water, a key component to RORE⁷. On track for continued outperformance for 2018/19
 - EBITDA growth of +17.7% at Viridor supported by the build out of new ERFs
 - Momentum in group efficiencies maintained with c.£15 million p.a of the £17 million p.a expected from 2019 already secured
- Statutory PBT up +2.9% to £133.6 million
- Statutory earnings per share growth of +3.8p to 25.6p
- Interim dividend per share up +7.3% to 12.84p
- Cash flow from operations reflecting robust operational performance, whilst significant capital investment continues
- Development of our sustainable financing framework, with £350 million of £480 million secured linked to the sustainable nature of the business, reducing our cost and reflecting our environmental and social credentials

¹ Before non-underlying items. Underlying earnings are presented to provide a more useful comparison on business trends and performance.

² Earnings before interest, tax, depreciation and amortisation (EBITDA)

³ Underlying EBITDA plus share of Joint Venture EBITDA and IFRIC 12 interest receivable

⁴ Non-underlying items are adjusted for by virtue of their size, nature or incidence to enable a full understanding of financial performance

⁵ EPS before deferred tax, non-underlying items and proportionately adjusted for the return on the perpetual capital securities (Note 8)

⁶ The RPI rate used is 3.3% as of September 2018

⁷ RORE - Return on Regulated Equity

South West Water

- Strong performance, demonstrating service resilience through extreme climatic conditions
 - Highest ever Customer Service (SIM) score achieved with South West Water now ranked 2nd overall in England and Wales in H1 2018/19⁸
 - Cumulative Return on Regulated Equity (RORE) at 11.8%⁹ - WaterShare delivering c.£100 million of outperformance for sharing with customers to date
- On track to deliver all our business plan commitments by 2020
 - Cumulative net ODI reward of £9.3 million¹⁰ to H1 2018/19
 - Continued strong focus on efficiency, on track to deliver the c.£300 million Totex outperformance to 2020 – £209 million delivered cumulatively to H1 2018/19
- New Deal launched in our Business Plan to Ofwat for the next five year period 2020-2025 (K7), giving customers a tangible stake and say in the business
 - Operational delivery preparations already underway

Viridor

- Focused on UK recycling and residual waste processing and transformation
- Favourable recycling market dynamics
 - Public perception, 'Blue Planet' effect – driving Government support for recycling
 - Recovery in recycling markets since H2 2017/18 – EBITDA of £7.4 million in H1 2018/19 ahead of £4.4 million achieved in H2 2017/18
- Strong residual waste market opportunities
 - Build out of ERFs supporting strong growth in EBITDA of +17.7%¹¹
 - Operational ERFs outperforming base case. On track for full year availability >90%¹² with planned maintenance weighted to H1
 - The three new ERFs at Glasgow, Beddington and Dunbar are all processing waste. Optimisation is ongoing and operations will ramp up over the next 18 months as has previously occurred at the other ERFs in our portfolio
 - Further consolidated our position through increasing the holding in Viridor's joint venture (TPSCo)¹³ which owns Runcorn I ERF
- Maximising value from landfill energy
 - Robust landfill demand forecast into the medium term.
 - 10 sites open to waste arisings, with volumes and gate fees holding up well
 - Investing in landfill gas for improved longer term yields

⁸ Ranked 2nd Water and Sewerage Company (WASC) for H1 2018/19 quality score based on two waves of Customer Experience Surveys (CES), a key element of SIM (Service Incentive Mechanism)

⁹ See page 20

¹⁰ £9.3 million cumulative net reward reflecting £11.6 million net reward which will be recognised at the end of the regulatory period and £2.3 million net penalty which can be reflected during the regulatory period

¹¹ ERF earnings include contractual compensation in the form of liquidated damages of H1 2018/19 £25.2 million (H1 2017/18 £2.6 million) when construction completed post original contractual completion date, offsetting this is a provision for amounts recognised against the Interserve contractual receivable

¹² Forecast average ERF availability is weighted by site capacity, includes 100% of joint venture availability, excludes Bolton

¹³ TPSCo – INEOS Runcorn (TPS) Holdings Limited which owns Runcorn I ERF

Pennon Water Services

- Pennon Water Services, one of only five associated retailers to have achieved net growth in the new competitive non-household market. Focused on value enhancing contracts and future cost base efficiencies.

Presentation of Results

A presentation for City audiences will be held today, Tuesday 27 November 2018, at 09.00am at the ICAEW (The Auditorium), One Moorgate Place, London, EC2R 6EA.

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

<http://www.pennon-group.co.uk/investor-information>

For further information, please contact:

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About Pennon Group

Pennon is one of the largest environmental infrastructure FTSE 250 groups in the UK with assets of around £6.2 billion and a workforce of around 5,000 people. Around 63% of Pennon's shareholders are UK pensions, savings, charities, individuals and employees, with two thirds of South West Water's employees being shareholders.

The integrated water company of South West Water and Bournemouth Water provides water and wastewater services to a population of c.1.7 million in Cornwall, Devon and parts of Dorset and Somerset and water only services to c.0.5 million in parts of Dorset, Hampshire and Wiltshire.

Since 1989 South West Water has invested around £7 billion to improve water and wastewater services. This investment means that we will supply some of the best quality drinking water in the UK and have achieved record bathing water quality in recent years.

South West Water was awarded enhanced status for its 2015-2020 Business Plan, and has the highest potential returns in the water sector to 2020.

Viridor is a leading UK recycling and residual waste processing and transformation business providing services to more than 150 local authorities and major corporate clients as well as over 32,000 customers across the UK.

Pennon Water Services provides water and wastewater retail services to over 160,000 non-household customer accounts across Great Britain, and is an 80:20 venture with South Staffordshire Plc.

10 year sector-leading dividend policy

Pennon's purpose is bringing resources to life. We aim to protect the environment, provide an outstanding service to customers and communities, while creating value for our shareholders. Pennon is investing significantly in its UK water and waste infrastructure and estimates capital expenditure of c.£1.7 billion between 2015 and 2020, with £1.3 billion invested to date. The Group generates robust operating cash flows, and has a strong liquidity and balance sheet position, underpinning a well established sector leading dividend policy.

South West Water has delivered further benefits for customers through our innovative WaterShare mechanism with around £100 million of benefits achieved since 2015. Customers will continue to benefit from reinvestment in services and lower bills into the next period.

Whilst delivering on our promises to customers and communities for investors Pennon's long established 10 year dividend policy of 4% year-on-year growth above RPI inflation to 2020 results in an expected doubling of dividend over 10 years (2010-2020)¹⁴. This policy reflects the Board's confidence in our sustainable strategy and is underpinned by the highest potential Return on Regulated Equity in the water sector over K6 (2015-2020) and the growth in earnings being delivered by Viridor's ERFs.

For H1 2018/19, the Board has recommended an interim dividend of 12.84p, up 7.3%. The interim dividend will be paid on 4 April 2019 to shareholders on the register on 25 January 2019.

Pennon now offers shareholders the opportunity to invest their dividend in a Dividend Reinvestment Plan (DRIP).

¹⁴ Future dividends growth based on policy of 4% + RPI forecast to 2020

Interim dividend payment information

24 January 2019	Ex-dividend date
25 January 2019	Record date
8 March 2019	Final date for receipt of DRIP applications
4 April 2019	Interim dividend payment date

Upcoming Events

January 2019	Viridor Waste Capital Markets Day
25 March 2019	Trading Statement
4 June 2019	Full Year Results 2018/19
25 July 2019	Annual General Meeting
September 2019	Trading Statement
26 November 2019	Half Year Results 2019/20

PENNON BUSINESS REVIEW

We know that inspiring trust and delivering transparency are fundamental to our strong relationship with customers and communities. Our vision and core values: ‘Trusted, Collaborative, Responsible, Progressive’ emphasise to employees and external stakeholders that we strive to be a trusted and responsible Company delivering high quality resilient services in a safe, reliable and sustainable manner. As a UK-listed Company, Pennon has a transparent corporate structure. Our Board is focused on strong financial control, sound administration and good governance.

Delivering on our promises for customers and communities

We know that delivering a resilient service in South West Water is a key promise to our customers. Despite the periods of extreme weather during 2018 with the ‘freeze and thaw’ in March and the hot dry summer, giving rise to unprecedented demand, we continued to deliver an excellent service to our customers. This has been reflected in our best ever quality service score in H1 2018/19, with South West Water ranked 2nd out of all water and sewerage companies in England and Wales.

South West Water has delivered further benefits for customers through our innovative WaterShare mechanism with around £100 million of benefits achieved since 2015. Customers will continue to benefit from reinvestment in services and lower bills into the next period.

Viridor continues to expand the ERF portfolio with three new facilities Glasgow, Beddington and Dunbar all processing waste with operations due to ramp up over the next 18 months. We continue to work closely with our key customers and partners across our whole portfolio to deliver service in line with expectations.

Delivering strong sustainable financial performance across the Group

Confidence in our financial resilience is driven by robust operating cash flows, a strong liquidity and balance sheet position and a diversified mix of low cost and flexible funding which underpins a sector leading dividend policy.

Pennon through its operating businesses performed well in H1 2018/19 and is on track to be in line with management expectations for 2018/19.

Earnings growth for 2018/19 has been driven by ERF portfolio growth, weather related higher revenue in South West Water, and a strong focus on cost savings, benefitting both customers and shareholders.

The cost savings and synergy targets of c.£17 million p.a. from 2019, identified through our targeted overhead review in 2015/16, are on track with c.£15 million p.a. delivered to date.

South West Water continues to deliver sector leading Totex outperformance and is on track to deliver c.£300 million over the 2015-2020 regulatory period. Together with delivery of net ODI rewards and outperformance in our cost of financing, momentum of delivery has been maintained with a cumulative Return on Regulated Equity (RORE) of 11.8%¹⁵ to H1 2018/19.

The build out of the ERF portfolio is supporting growth in Viridor and the recycling activities have recovered from the challenging position in H2 2017/18. Viridor has continued to focus on cost savings with initiatives delivering indirect cost efficiencies of 17% in real terms since 2015/16.

Balanced business plan for 2020-2025

In September South West Water submitted its business plan for 2020-2025 (K7). As a responsible and transparent water business a fundamental part of our proposals is for a New Deal which signals a new way of doing business for our customers and stakeholders. This approach is focused on empowering our customers by giving them the option of a tangible financial stake and a share in the business and the power to hold us to account, with a say in our business through a Customer AGM.

The initial assessment of the business plan by Ofwat is expected at the end of January 2019. Given customer acceptance of our plan was at 88% preparations are already underway for a fast start in K7, with key supply chain delivery partnerships in place, pilot trials for new water treatment technology completed and preparatory work for taking on the expanded licence area of the Isles of Scilly is in progress.

¹⁵ See page 20

Leading, responsible and sustainable UK waste operator

Viridor is focused on delivering UK recycling and residual waste processing and transformation. We believe there are continued favourable waste market dynamics in both recycling and residual waste.

Whilst the recycling market has been challenging, Viridor has delivered improvements to its recycling performance in H1 2018/19 compared with H2 2017/18, with EBITDA increasing from £4.4 million to £7.4 million. With Government support for recycling and the UK Plastics Pact outlining a roadmap with targets to 2025 we believe there are opportunities for growth. The 'Blue Planet' effect continues to encourage action and we expect positive changes to be announced in the Government's Resources & Waste Strategy when published.

We continue to expect UK residual waste market dynamics to be favourable with demand for ERFs exceeding capacity into the long term. We anticipate the capacity gap to be greater than seven million tonnes (mT) by 2030. Household waste arisings have increased annually since 2012 and expenditure on waste services is up c.16%¹⁶ from 2008/09. The operational ERF portfolio is on track to achieve availability in excess of 90%¹⁷ in 2018/19 with the operational performance of the facilities above management's initial base case expectations which assume a real post tax IRR (internal rate of return) of 8%. EBITDA margin in H1 2018/19 was 60%. Three of the four remaining ERFs are processing waste with operational ramp up over the next 18 months. Construction is progressing well at Avonmouth near Bristol.

We see further opportunities to deliver capacity expansion at existing facilities, having secured planning permissions and permits for additional capacity at Cardiff (75,000 tonnes) and Ardley (27,000 tonnes), as well as an increase in power output at Runcorn II.

We have further consolidated our position through increasing our holding in Viridor's joint venture (TPSCo)¹⁸, which owns Runcorn I ERF, from 37.5% to 75.0% of the economic interest.

We believe our landfill portfolio complements the combustible residual waste strategy, with a requirement for a landfill solution into the medium term.

We also continue to consider further expansion and investment, with development of energy park opportunities across the landfill and ERF portfolio capitalising on the potential of existing grid connections.

Pennon continues to seek and identify further growth opportunities within the UK, assessing the long-term viability of the markets in which we operate and achieving an appropriate risk/reward balance and is confident of delivering sustainable, long-term returns from water and waste.

¹⁶ Source: Tolvik, Defra, SEPA, NRW, MSW and Viridor analysis based on 2016/17 latest local authority data available

¹⁷ Average ERF availability is weighted by site capacity, includes 100% of joint venture availability, excludes Bolton

¹⁸ TPSCo – INEOS Runcorn (TPS) Holdings Limited which owns Runcorn I ERF

Pennon Group

Underlying¹⁹	H1 2018/19	H1 2017/18	Change
Revenue	£746.7m	£723.9m	+3.1%
EBITDA	£274.0m	£253.5m	+8.1%
Adjusted EBITDA ²⁰	£294.7m	£285.8m	+3.1%
Depreciation and amortisation	(£95.5m)	(£91.1m)	(4.8%)
Operating profit	£178.5m	£162.4m	+9.9%
Net interest	(£40.8m)	(£36.6m)	(11.5%)
Share of JV profit after tax	£4.8m	£5.3m	(9.4%)
Profit before tax	£142.5m	£131.1m	+8.7%
Non-underlying items before tax ²¹	(£8.9m)	(£1.3m)	-
Statutory profit before tax	£133.6m	£129.8m	+2.9%
Tax	(£17.6m)	(£17.5m)	(0.6%)
Statutory profit after tax (PAT)	£116.0m	£112.3m	+3.3%
PAT (attributable to holders of hybrid capital)	£8.6m	£21.5m	(60.0%)
PAT (attributable to minority interests)	(£0.1m)	(£0.1m)	-
PAT (attributable to shareholders)	£107.5m	£90.9m	+18.3%
Earnings per share ^{22,23}	30.0p	25.3p	+18.6%
Statutory earnings per share²³	25.6p	21.8p	+17.4%
Dividend per share ²⁴	12.84p	11.97p	+7.3%
Capital investment ²⁵	£200.6m	£222.3m	(9.8%)
South West Water	£68.6m	£97.6m	(29.7%)
Viridor ²⁶	£131.9m	£124.3m	+6.1%
Other	£0.1m	£0.4m	(75.0%)
	30 September	31 March	Change
	2018	2018	
Net debt ²⁷	£3,041.9m	£2,801.5m	+8.6%

¹⁹ Before non-underlying items

²⁰ Underlying EBITDA plus share of Joint Venture EBITDA and IFRIC 12 interest receivable

²¹ Non-underlying items are adjusted for by virtue of their size, nature or incidence to enable a full understanding of the Group's financial performance

²² EPS before deferred tax, non-underlying items and proportionately adjusted for the return due on the perpetual capital securities

²³ Weighted average number of shares for H1 2018/19 of 419.3 million (H1 2017/18 416.6 million)

²⁴ The RPI rate used is 3.3% as of September 2018

²⁵ Including construction spend related to service concession arrangements net of amounts subject to legal contractual process

Comparator reanalysed on a consistent basis with the 2017/18 year end reporting - H1 2017/18 reported capital investment of £245.1 million adjusted by £22.8 million to reflect the amounts subject to legal contractual process

²⁶ Including construction spend related to service concession arrangements net of amounts subject to legal contractual process.

Comparator reanalysed on a consistent basis with the 2017/18 year end reporting - H1 2017/18 reported capital investment of £147.1 million adjusted by £22.8 million to reflect the amounts subject to legal contractual process

²⁷ Net debt – total borrowings less cash and cash deposits

Non-underlying Items

There is one non-underlying item in H1 2018/19 which arises as a result of the movement in the fair value of long-dated derivatives associated with South West Water's 2040 bond. This results in a charge of £8.9 million (H1 2017/18 charge of £7.8 million). The tax impact of this non-underlying item is a credit of £1.7 million, resulting in an after tax position of £7.2 million.

In the prior period, the net charge before tax for H1 2017/18 was £1.3 million and included a £6.5 million credit as a result of the reset of the Greater Manchester contracts as well as the £7.8 million charge for the movement in the fair value of long-dated derivatives associated with South West Water's 2040 bond. Net non-underlying items after tax for the prior period resulted in a £3.0 million credit.

South West Water

Underlying	H1 2018/19	H1 2017/18	Change
Revenue ²⁸	£301.5m	£292.2m	+3.2%
Operating costs	(£106.8m)	(£105.1m)	(1.6%)
EBITDA	£194.7m	£187.1m	+4.1%
Depreciation and amortisation	(£58.8m)	(£56.4m)	(4.3%)
Operating profit	£135.9m	£130.7m	+4.0%
Net interest	(£35.6m)	(£34.5m)	(3.2%)
Profit before tax	£100.3m	£96.2m	+4.3%

Viridor

Underlying	H1 2018/19	H1 2017/18	Change
Revenue ²⁹	£422.3m	£407.0m	+3.8%
EBITDA	£78.4m	£66.6m	+17.7%
<i>ERFs</i>	£66.6m	£51.7m	+28.8%
<i>Landfill</i>	£3.8m	£3.3m	+15.2%
<i>Landfill gas</i>	£8.1m	£9.2m	(12.0%)
<i>Recycling</i>	£7.4m	£10.6m	(30.2%)
<i>Contracts, Collections & Other</i>	£20.3m	£20.0m	+1.5%
<i>Indirect costs</i>	(£27.8m)	(£28.2m)	+1.4%
Depreciation and amortisation	(£36.2m)	(£34.2m)	(5.8%)
Share of JV profit after tax	£4.8m	£5.3m	(9.4%)
Net interest	(£10.8m)	(£7.1m)	(52.1%)
Profit before tax	£36.2m	£30.6m	+18.3%
<i>Share of JV EBITDA</i>	£13.4m	£25.4m	(47.2%)
<i>IFRIC 12 interest receivable</i>	£7.3m	£6.9m	+5.8%
<i>Adjusted EBITDA</i> ³⁰	£99.1m	£98.9m	+0.2%

²⁸ Includes wholesale revenue for non-household customers

²⁹ Including landfill tax and construction spend on service concession arrangements

³⁰ EBITDA plus share of Joint Venture EBITDA and IFRIC 12 interest receivable

Pennon Water Services

	H1 2018/19	H1 2017/18	Change
Revenue	£84.1m	£83.5m	+0.7%
EBITDA	£0.9m	£0.5m	+80.0%
Depreciation and amortisation	(£0.4m)	(£0.3m)	(33.3%)
Operating profit	£0.5m	£0.2m	+150.0%
Net interest	(£1.0m)	(£0.7m)	(42.9%)
Profit before tax	(£0.5m)	(£0.5m)	-

Strong Group underlying financial performance

Group revenue in H1 2018/19 increased by 3.1% (£22.8 million) to £746.7 million.

Revenue from South West Water increased by 3.2% (£9.3 million) to £301.5 million due to customer demand increases of 2.7%, from the hot and dry weather over the summer, tariff increases of 1.0% and increased infrastructure connections. Viridor revenues increased by 3.8% (£15.3 million) to £422.3 million primarily due to the ERF build out (net of reduced construction IFRIC 12 revenue).

Group EBITDA and adjusted EBITDA were ahead of the same period last year by 8.1% and 3.1% respectively, with South West Water, Viridor and Pennon Water Services all ahead of H1 2017/18. The gap between EBITDA and adjusted EBITDA narrowed in the period as expected due to reduced share of JV EBITDA following the reset of the Greater Manchester waste contract in 2017/18.

South West Water's EBITDA and operating profit increased by 4.1% and 4.0% respectively. Strong cost management and efficiency delivery has resulted in lower than inflation cost increases, despite the increased costs required to meet higher customer demand of c.£3 million in H1 2018/19. In addition, South West Water's bad debt performance remains strong with a charge of 0.6% of revenues (H1 2017/18 0.9%) reduced from 1.7% at March 2015. This continues to be driven by efficient collections as we work with our customers to manage their debt and strive to support those customers in vulnerable circumstances with affordability challenges.

Viridor's EBITDA for the first half of 2018/19 increased by 17.7% (£11.8 million) compared with H1 2017/18.

The ERF business has performed strongly during the period, in line with expectations. The EBITDA generated from our portfolio was 28.8% higher at £66.6 million (H1 2017/18 £51.7million) reflecting financial contributions from Beddington and Dunbar. We are on track to deliver another year of availability for our current operational assets in excess of 90%³¹ across the portfolio (including Joint

³¹ Forecast average ERF availability is weighted by site capacity, includes 100% of joint venture availability, excludes Bolton

Ventures). As we continue to optimise our performance, more of our planned maintenance outages have been completed in the first half of this financial year, when electricity demand and pricing is lower. Planned maintenance has been performed at all major sites during the half year and as a result availability during H1 2018/19 was 89%.

Landfill EBITDA has increased by 15.2% to £3.8 million since H1 2017/18 (£3.3 million). Volumes and pricing have held up, with cost savings contributing to the higher EBITDA. We continue to see demand for a landfill solution into the medium term, and have sites well positioned to meet these demands, with 11 sites operational for H1 2018/19. As part of the planned closure profile, one site (Rigmuir) closed in September leaving 10 operational sites.

In our landfill gas business we are currently progressing our engine replacement strategy, including investing in maintenance and more efficient engines. This is improving reliability and securing generation for the longer term, whilst optimising the generating capacity potential at our sites. EBITDA for the period at £8.1 million, is down 12.0% from the prior year (H1 2017/18 £9.2 million). This has been driven by higher planned maintenance activities during the summer period to secure reliable generation during the winter and a natural decline in gas volumes produced from sites (although at 4% this is at a lower rate than previous years). The benefit of higher year on year hedged electricity prices has helped support the overall performance.

Recycling EBITDA at £7.4 million is £3.0 million higher than H2 2017/18, with EBITDA margin increasing by £5 per tonne to £12 per tonne reflecting some recovery in the global recycling markets following import restrictions by China in H2 2017/18. EBITDA is £3.2 million lower than the first half of last year (H1 2017/18 £10.6 million) which was before the Chinese restrictions were implemented, consequently EBITDA margin per tonne has decreased from £14 (H1 2017/18) to £12 (H1 2018/19). Market led quality demands have remained challenging, and we have continued to face challenges with poor input quality. We have continued to focus on producing high quality outputs which has contributed to an increase in revenue per tonne to £110 (H2 2017/18 £97; H1 2017/18 £97). We have seen an overall reduction in recycle volumes sold, higher waste output and an increase in costs of production. Our focus continues to be on the production of higher quality recyclates as well as adopting 'self-help' measures to create margin improvement. To help mitigate our exposure to recycle price volatility we continue to share commodity risks and rewards with our customers.

In the period Contracts, Collections and Other EBITDA was broadly comparable with the prior period at £20.3 million (H1 2017/18 £20.0 million). Following last year's reset, the Greater Manchester run off contract financial results are in line with our expectations. In November 2018 Viridor withdrew from the Greater Manchester waste operating contract tender process and we expect the run-off contract to cease in early 2019/20. The financial impact of not continuing with this operational contract is not material to the Group, and our position with the ERFs at Runcorn is unaffected.

Viridor's indirect costs have continued to fall, marginally down this period to £27.8 million from £28.2 million in H1 2017/18, and are 17% lower in real terms than 2015/16.

Joint venture EBITDA has reduced from £25.4 million in H1 2017/18 to £13.4 million. This is a result of the contract reset at Greater Manchester in September last year. This saw both the disposal of our Viridor Laing joint venture and the introduction of a lower contractual EBITDA for our TPSCo joint venture following the repayment of external debt as part of the reset. Interest savings mean that TPSCo profit after tax was not significantly impacted by the reset. TPSCo continues to deliver strong operational and financial performance.

Planned maintenance profiling in H1 2018/19 at our Lakeside joint venture has resulted in financial performance slightly below last year, however, underlying operational and financial performance has remained strong, again exceeding our original expectations, for both waste processing and power generation.

IFRIC 12 interest receivable at £7.3 million is broadly comparable with H1 2017/18 of £6.9 million.

Pennon Water Services has continued to successfully gain new customers during its second year of trading. Overall EBITDA for the first half is £0.9 million (H1 2017/18 £0.5 million), with a focus on improving operating cost efficiencies.

Group efficiencies achieved as a result of the Shared Services initiatives have delivered a further £2 million of cost savings and synergy benefits during the first half of the year bringing the cumulative position to c.£15 million p.a. to date, and we are on track for the cumulative c.£17 million p.a. targeted from 2019.

Net Finance Costs

Underlying net finance costs of £40.8 million are £4.2 million higher than last half year (H1 2017/18 £36.6 million). This is attributable to higher net debt from continuing capital investments and lower interest receivable on shareholder loans following the Greater Manchester contract reset.

We have secured funding at a cost that is efficient and effective with the effective interest rate reducing marginally to 3.6% (H1 2017/18 3.7%), remaining sector leading.

The effective interest rate is calculated after adjusting for capitalised interest of £8.3 million, notional interest items totalling £6.3 million, interest received from shareholder loans to joint ventures of £2.5 million and IFRIC 12 interest receivable of £7.3 million. The effective interest rate for South West Water in the period was 3.5% (H1 2017/18 3.5%).

During H1 2018/19 underlying net finance costs (excluding pensions net interest costs of £0.9 million, discount unwind of provisions of £5.4 million and IFRIC 12 notional interest receivable of £7.3 million) were £52.6 million, covered 4.3 times by Group operating profit (H1 2017/18 £51.1 million and 4.3 times).

Profit before tax

Group underlying profit before tax was £142.5 million, an increase of 8.7%, compared with the prior half year (H1 2017/18 £131.1 million). Included in profit before tax is our share of joint venture profit after tax of £4.8 million (H1 2017/18 £5.3 million). On a statutory basis, profit before tax was £133.6 million (H1 2017/18 £129.8 million) reflecting a non-underlying charge before tax of £8.9 million (H1 2017/18 £1.3 million).

Taxation

The Group's underlying mainstream UK corporation current tax charge for the half year (before prior year adjustments) was £15.6 million, reflective of an effective tax rate of 10.9% (H1 2017/18 £14.3 million, 10.9%). The lower effective rate versus the UK's mainstream corporation tax rate of 19% reflects the accelerated level of capital allowance claims available to the Group compared to the Group depreciation charge. There was a prior year credit of £3.2 million recognised for the period (H1 2017/18 credit of £4.3 million), the credits reflect the resolution of minor outstanding tax items with HMRC.

Underlying deferred tax for the period (before prior year adjustments) was a charge of £12.2 million (2017/18 H1 charge £10.2 million). The charge for H1 2017/18 primarily reflects capital allowances across the Group in excess of depreciation charged. There was a prior year deferred tax credit of £5.3 million recognised for the period (H1 2017/18 £1.6 million charge), reflecting finalisation of capital allowance claims.

In addition, in H1 2018/19 there is a non-underlying £1.7 million current year deferred tax credit (2017/18 H1 £1.3 million deferred tax credit) relating to the non-underlying movement in the fair value of long-dated derivatives associated with South West Water's 2040 bond. There was also a £3.0 million non-underlying current tax credit in H1 2017/18 (relating to the reset of the Greater Manchester Contract); there is no current tax effect of the non-underlying items in H1 2018/19.

Overall the total tax charge for the period was £17.6 million (H1 2017/18 £17.5 million).

Earnings per share

Earnings per share on both a statutory and underlying basis before deferred tax has been positively impacted by a reduction in hybrid costs³² period on period in addition to increased profits. As a consequence earnings per share on both a statutory and underlying basis has increased by 17.4% at 25.6p (H1 2017/18 21.8p) and 18.6% at 30.0p (H1 2017/18 25.3p) respectively.

³² Perpetual capital securities (hybrid). H1 2018/19 adjusted hybrid cost of £4.3 million (H1 2017/18 £15.7 million). H1 2018/19 statutory hybrid costs of £8.6 million (H1 2017/18 £21.5 million)

Robust cash inflow from operations, continuing investment in future growth

The Group's operational cash inflows in H1 2018/19 were £266.6 million³³ (H1 2017/18 £308.9 million). These funds have been put to use in efficiently financing the Group's capital structure and investing in future growth. This investment has resulted in higher Group net debt.

Contributions into the Group's pension schemes for the half year were £8.5 million, and corporation tax payments were £12.2 million. Included in other movements of £48.0 million is the 2017 unwind settlement of the PMB derivative. Total tax payments reflecting all taxes borne by the Group in H1 2018/19 were £63.4 million³⁴ (H1 2017/18 £59.0 million).

Sustainable funding position underpinning investment

The Group has a strong liquidity and funding position with £1,056 million cash and committed facilities at 30 September 2018. This consists of cash and deposits of £406 million (including £186 million of restricted funds representing deposits with lessors against lease obligations) and undrawn facilities of £650 million. At 30 September 2018 the Group's borrowings totalled £3,448 million.

Pennon has pioneered a sustainable financing framework to integrate commitments to environmental and social objectives into a variety of funding opportunities across the Group. The framework allows Pennon to access future funding opportunities aligned with the green loan principles, green bond principles and social bond principles. The framework has been certified by DNV GL a leading sustainability verifier. Pennon is committed to continuous annual improvements in sustainability ratings and KPIs which may lead to improved interest rate margins.

During the period, £480 million of new and renewed facilities have been signed, £340 million in Pennon Group plc and £140 million in South West Water. In total, £350 million of the new facilities signed in the half year are linked to the sustainable nature of the business. Included in these facilities is an inaugural Pennon Group loan from the EIB³⁵.

Pennon has cash and committed facilities for the remainder of South West Water's planned K6 capital programme and our ERF investments. Further funding will be sourced over K6 to:

- Maintain an appropriate headroom of cash and committed facilities, including replacing maturing finance
- Prepare for the next regulatory period.

³³ Before construction spend on service concession agreements of £11 million (H1 2017/18 £44 million), pension contributions of £9 million (H1 2017/18 £5 million), £44 million for the 2017 unwind settlement of the PMB derivative and other tax payments of £51 million (H1 2017/18 £49 million). Working capital movements include higher metered accrued income resulting from increased demand over the summer and timing of payments on local authority contracts

³⁴ Total tax includes corporation tax, business rates, employers' national insurance, fuel excise duty, carbon reduction commitment, environmental payments, climate change levy and external landfill tax

³⁵ EIB – European Investment Bank

Efficient long-term financing strategy

The Group has a diversified funding mix of fixed (£1,771 million, 58%), floating (£708 million, 23%) and index-linked borrowings (£563 million³⁶, 19%). The Group's debt has a maturity of up to 39 years with a weighted average maturity of c.20 years. Much of the Group's debt is floating rate and derivatives are used to fix the rate on that debt. The Group has fixed, or put swaps in place to fix, the interest rate on a substantial portion of the existing water business debt for the entire K6 period, in line with the Group's policy for this regulatory period to have at least 50% of funding fixed.

South West Water's cost of finance is amongst the lowest in the industry. Around two thirds of South West Water's net debt is from finance leases which provide a long maturity profile. Interest payable benefits from the fixed credit margins which are secured at the inception of each lease. £563 million (c.25%) of South West Water's debt is index-linked at an overall real rate under 2.0%. This represents a quarter of the net funding for South West Water, a level below Ofwat's notional level of 33%, which we believe gives an advantageous position given the RPI to CPIH transition.

Following the submission of the South West Water business plan the Group is looking to align the hedging for the next regulatory period with the changed regulatory methodology. A proportion of new debt will be hedged in K7 on a rolling ten year basis whilst still maintaining flexibility within the overall portfolio. Embedded debt hedging will be aligned with the regulatory delivery period.

Net debt position

In the first half of 2018/19 the Group's net debt increased by £240 million to £3,042 million. Cash inflow from operations was £267 million. Cash outflows relating to the capital programme totalled £192 million³⁷, slightly reduced as expected from the peak years of the Group's capital expenditure in 2016/17 and 2017/18. The gearing ratio at 30 September 2018, being the ratio of net debt to (equity plus net debt) was 65.5% (31 March 2018 63.1%, 30 September 2017 64.8%) and is expected to reduce by the year end.

The combined South West Water and Bournemouth Water debt to RCV ratio is 62.1%³⁸ (31 March 2018 60.3%, 30 September 2017 62.1%) which broadly aligns with Ofwat's K6 target for efficient gearing of 62.5%.

Group net debt includes £2,125 million for South West Water with the remaining £917 million supporting investment in Viridor growth and expansion including the amount invested in joint ventures, through shareholder loans of £41 million for TPSCo and Lakeside.

³⁶ Includes £137 million of index-linked finance leasing

³⁷ Including service concession construction spend of £11 million (2017/18 £44 million)

³⁸ Based on RCV at March 2018

Capital investment focused on regulatory expenditure and ERF build out

Group capital investment was £201 million³⁹ in H1 2018/19 compared with £222 million³⁹ in H1 2017/18.

Viridor

Viridor's capital spend³⁹ in the period was £131.9 million (H1 2017/18 £124.3 million), an increase of £7.6 million over H1 2017/18.

The majority of capital investment continues to relate to the delivery of the ERF fleet⁴⁰, with £103 million of total spend relating to the three ERFs in operational ramp up and Avonmouth under construction. Our ERFs at Glasgow, Beddington and Dunbar are all processing waste.

Other capital expenditure included lifecycle capital expenditure on our operational ERF fleet and development of our Clyde Valley ERF fuel supply facility. On-going restoration and remediation programmes continue for our landfill assets, ensuring we meet or exceed our environmental duties and responsibilities.

South West Water

South West Water's capital expenditure in the first half of the year was £68.6 million, compared with £97.6 million in H1 2017/18 with the profile aligned with the K6 capital plan reflecting the completion of specific large investment programmes at Mayflower Water Treatment Works and the bathing and shellfish water improvements.

Key areas of drinking water investment and activity during H1 2018/19 included:

- Completion of the new state-of-the-art Mayflower water treatment works which has entered commissioning, with c.£6 million of expenditure in H1 2018/19 (H1 2017/18 c.£19 million)
- Investment in our infrastructure to reduce the number of bursts and leakage impacted by the 'freeze and thaw' in March 2018 and costs associated with the hot dry summer (c.£6 million).

Key areas of wastewater investment and activity during H1 2018/19 included:

- Finalisation and completion of the Plymouth bathing water scheme
- Continued improvements at wastewater treatment works including flood resilience
- Investment for growth in order to meet increases in supply and demand.

³⁹ Including construction spend related to service concession arrangements, capitalised interest (£8 million in H1 2018/19 of which £7 million was within Viridor), ERF maintenance expenditure, net of amounts subject to legal contractual process. Comparator reanalysed on a consistent basis with the 2017/18 year end reporting - H1 2017/18 reported capital investment of £245.1 million adjusted by £22.8 million to reflect the amounts subject to legal contractual process

⁴⁰ Total ERF portfolio forecast expenditure to completion of £1,529 million excluding capitalised interest, net of amounts subject to legal contractual process

Pensions

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

At 30 September 2018 the Group's pension schemes showed an aggregate deficit (before deferred tax) of £44.8 million (March 2018 £49.5 million), a reduction of £4.7 million. Pension liabilities decreased by £3.8 million mainly due to higher corporate bond yields, while asset values increased marginally by £0.9 million.

The net aggregate liabilities of £37 million (after deferred tax) represented around 1% of the Group's market capitalisation at 30 September 2018.

Energy hedging

Pennon has adopted a group portfolio management approach to energy hedging, and has the ability to hedge its market position for periods up to five years ahead, further helping to protect revenues.

Forward hedges have been put in place in the liquid market with the Group c.80% hedged until March 2020 and c.55% hedged until 2021 for its energy (generation net of internal usage of electricity). In addition, the Group has a natural hedging opportunity which represents one third of Viridor's energy generation, as South West Water is a net user of electricity.

The energy portfolio management team continues to actively manage the Group net energy generation position in liquid markets.

SOUTH WEST WATER

OPERATIONAL PERFORMANCE

Delivering a resilient service for customers – excellent management of operational challenges

Despite the challenges of extreme weather, South West Water has continued to deliver a resilient service to its customers. During the exceptional cold weather⁴¹ in March, with the first red weather warning for snow in the South West, our proactive planning and management ensured we were able to manage the impacts of the ‘freeze and thaw’ effectively. We have also supported customers with leak repair activity and focused on fixing visible leaks within two days.

Alongside this increased activity we have maintained supplies to customers despite the unprecedented demand over the hot dry summer. This has been the hottest summer on record and water through our network has increased c.6.0% from last year. This increased demand has been further challenged with the significant increase in visitors to the region over the summer period (c.20% increase). Despite this, 2018 has been our 22nd year without water restrictions and supply interruptions have reduced this period. In addition, we have supported the Isles of Scilly over the summer months to maintain supplies in that area when water levels fell to extreme lows.

Customers at the heart of our delivery

Improving customer service is at the heart of our delivery plans. South West Water achieved its best ever quality service score in H1 2018/19, ranked 2nd out of all water and sewerage companies in England and Wales. Our customer service score (SIM) increased again and is now expected to be above average for the industry this year, with no penalty forecast for the K6 period. The SIM score is calculated against a qualitative element (based on a customer survey) and a quantitative element that takes into account, amongst other things, the number of complaints received in writing or by phone, which continue to fall.

The improvement in service is driven by a range of activities including enhanced ‘customer journeys’, which have been developed jointly with customers, increasing customer resolution as well as improving the channels with which customers can contact us, such as online and social media.

South West Water has been leading the way for the last 10 years in providing support to customers who find themselves in vulnerable circumstances or who struggle to pay their bills. We have continued to focus on this and are targeting to eliminate water poverty in our 2020-2025 Business Plan. Preparation for these additional activities is already underway and those currently receiving

⁴¹ Reflecting a 1 in 60 year event

support through reduced tariffs has increased to c.23,000 customers, the highest proportion in the industry⁴², and over 55,000 customers are supported through other programmes.

Since the opening of the non-household retail market in April 2017, South West Water has operated successfully with 19 different retailers and our wholesale service desk has been operating effectively.

Maintaining momentum – continued sector leading outperformance

South West Water has performed well in H1 2018/19, and has delivered in line with management expectations. Strong operational and financial performance underpins our sector leading RORE⁴³, which has been consistently above 11%⁴⁴ annually and remains 11.8% cumulatively since the start of the K6 business plan period. Of the 11.8%, 6.0% is the base return, 2.6%⁴⁵ reflects Totex savings and efficiencies, 0.3% reflects a net reward on Outcome Delivery Incentives (ODIs) and 2.9%⁴⁶ reflects the difference between actual and assumed financing costs using a cumulative forecast RPI over K6 of 2.8%, which is consistent with the approach adopted for calculating our innovative WaterShare mechanism. Cumulatively the WaterShare RORE outperformance over K6 is consistent with the approach adopted by Ofwat.

	H1 2018/19⁴⁷	K6 to date
Base return	6.0%	6.0%
Totex outperformance ⁴⁵	2.6%	2.6%
ODI outperformance ⁴⁷	0.2%	0.3%
Financing Outperformance ⁴⁶	2.8%	2.9%
WaterShare RORE	11.6%	11.8%
<i>Ofwat RORE⁴⁴</i>	<i>12.3%</i>	<i>11.8%</i>

Totex efficiency reducing customer bills

South West Water is striving for ever greater efficiency. Totex outperformance has already achieved cumulative savings of £209 million⁴⁸ to H1 2018/19 and we are on track to deliver c.£300 million of Totex savings by 2020, which are embedded into our 2020-2025 business plan.

⁴² English operational water companies, (excluding Welsh Water), normalised per 10,000 customers (based on 2017/18 data)

⁴³ RORE reflects base plus outperformance. It is calculated using actual results before non-underlying items (deflated into 2012/13 prices) and compared against the Final Determination allowances and based on notional gearing, annual average RCV and reflecting the value of tax impacts at the actual annual effective tax rate for the year

⁴⁴ H1 2018/19 full year equivalent RORE of 11.6% delivered reflecting 6.0% base return, 2.6% totex savings and efficiencies, 0.2% net reward on ODIs and 2.8% on financing outperformance. RORE based on Ofwat guidance results in 3.5% of financing outperformance (calculated using in-year average RPI rate of 1.1% for 2015/16, 2.1% for 2016/17, 3.7% for 2017/18 and 3.3% for H1 2018/19) resulting in a total RORE of 12.3% for H1 2018/19 (2017/18 4.1% and 12.4% respectively)

⁴⁵ Includes integration synergies already delivered. Phasing of actual expenditure compared to the planned programme has been reflected. Outperformance includes a reduction in the RCV run-off for the RCV element of Totex outperformance calculated based on the Final Determination pay-as-you-go (PAYG). Tax impacts reflect actual effective tax rates

⁴⁶ Interest outperformance is based on the outturn effective interest rate on net debt, translated into an effective real interest rate using cumulative K6 forecast RPI of 2.8%, notional debt gearing of 62.5%, and actual effective tax rates

⁴⁷ Annual equivalent percentage for the period to 30 September 2018

⁴⁸ Delivered around two thirds from capital expenditure and one third from operating cost savings

These savings are being driven by:

- Managing upward cost pressures, with actual net price rises being below annual average inflation rates
- Continuing advantages from our strategic alliances and driving efficiency from our procurement processes
- Reducing customer debt through enhanced collections activities and increasing our affordability schemes (such as social tariffs), with the cost of bad debt now below the level assumed within the 2014 Final Determination
- Efficiencies from the Bournemouth Water integration, including delivery of key capital schemes in the region, with c.£19 million of net synergies delivered to date
- Ensuring efficient capital investment through the use of data analytics, optimising capital and operating solutions and promoting efficient off-site build techniques.

This focus on cost efficiency is reducing bills for customers, and our 2020-2025 business plan continues to target cost efficiency, supporting an 11% real reduction in customer bills by 2025.

ODIs continue to deliver net reward

Operational performance for the half-year based on delivery by 30 September 2018 resulted in a net ODI reward of £1.2 million⁴⁹ (£9.3 million cumulatively for K6) reflecting RORE outperformance of 0.2%⁵⁰, a slight reduction from last year. Good asset reliability with stable serviceability across all water and wastewater areas has been maintained. Rewards were delivered across bathing water quality and water restrictions, as well as significant improvements in external and internal sewer flooding, which continue to deliver rewards. The cumulative net reward of £9.3 million to H1 2018/19 comprises £15.4 million of total rewards and £6.1 million of total penalties. ODI penalties which apply within the regulatory period will reduce customer bills as they are 'passed back'. ODI net penalties of £2.1 million have been adjusted in customer bills for 2018/19 and £0.3 million will be adjusted in the 2019/20 tariffs.

Whilst the overall net value of ODI reward has fallen in 2018/19, this is a result of the profile of ODI rewards over the current regulatory period. South West Water is forecasting to meet all its ODI commitments this year with a number of areas moving out of penalty.

⁴⁹ £1.2 million (£9.3 million cumulatively) net ODI reward; £1.2 million (£11.6 million cumulatively) net reward will be recognised at the end of the regulatory period and £nil (£2.3 million cumulatively) net penalty which may be reflected during the regulatory period

⁵⁰ Annual equivalent RORE benefit at H1 2018/19

- *Pollution incidents*

Pollution incidents in the year have continued to fall, with only one significant pollution incident in the calendar year so far. This would result in zero penalties for the year (compared to the cumulative penalty of £3.6 million).

- *Flooding*

Continuing the strong performance in 2017/18, the number of flooding incidents in H1 2018/19 has reduced and based on this performance is expected to result in further rewards this year.

- *22nd consecutive year without water restrictions*

Despite the unprecedented increase in customer demand over the hot dry summer, water resources in the South West Water region remained unrestricted for a twenty-second consecutive year and the Bournemouth water region maintained its position of having no water restrictions since privatisation. As the weather continues to remain drier than usual South West Water is actively managing our water resources and may implement storage schemes to protect future supplies.

- *Bathing water quality – c.99% achieving sufficient quality, over 78% excellent*

Our legacy of major investment to protect bathing waters continues to be reflected in extremely positive results for the 2018 bathing water season. Of the 151 bathing waters tested in the South West Water region, 149 (c.99%) were classified 'sufficient' or better, with more than 78% classified as 'excellent'. Neither of the two bathing waters rated as 'poor' were attributed to any failure of South West Water's assets.

- *Leakage*

The impact of the 'freeze and thaw' in March 2018 has seen leakage levels increase along with the number of bursts in the region. South West Water is targeting investment and operational resources to meet our leakage target of 84 megalitres per day in 2018.

- *Supply interruptions – meeting targets*

Demand over the summer months placed pressure on both our treatment works and network to meet customer demand. Despite this the average duration of supply interruptions per property for South West Water remains on track to meet the target for the year based on performance in H1 2018/19.

Financing investment efficiently

Alongside strong operational outperformance, South West Water is confident that the efficient and effective financing strategy in place will continue to deliver cumulative K6 financing outperformance, with £115 million delivered in the K6 period to date. Since the year end a £60 million lease has been agreed under the Pennon sustainable financing framework, specifically linked to the new innovative Mayflower water treatment works. Gearing levels remain aligned with Ofwat's current notional level and South West Water is the only UK water company to share the benefits of lower interest rates with customers.

Sharing outperformance between customers and shareholders

South West Water is sharing the benefits of business outperformance between customers and shareholders through our unique WaterShare mechanism. Since 2015 c.£100 million of cumulative benefits⁵¹ have been identified to share with customers through investment in services and lower future bills. This reflects £71 million of Totex savings, £9 million of net ODI benefits and £16 million of other benefits (including financing). These Totex savings and efficiencies (including the forecast to 2020) have been reflected in the 2020-2025 business plan, lowering bills for customers over the next regulatory period. The other savings identified in recent years and expected out to 2020 will provide the basis for delivering the New Deal for customers.

New Deal 2020-2025 – delivery preparations underway

Empowering customers through a New Deal

The key focus for our 2020-2025 business plan is empowering customers through a New Deal. It will ensure customers are sharing in our success and having a say through a Customer AGM, which will allow customers to hold us directly to account. In addition, the option for customers to have a shareholding gives them a tangible stake in our business through the outperformance delivered and will further ensure customers are at the heart of our business.

The business plan proposes new benchmarks for service and efficiency, with a key target being to eliminate water poverty by 2025.

Delivery preparations underway

The next regulatory period includes specific comparative service and environmental targets which will be measured consistently across the whole industry every year. Based on existing performance South West Water is already delivering above average performance in 10 ODIs⁵².

A successful part of our delivery has been our commitment to strong partnerships. For the next regulatory period we have already put in place a number of key partnerships, including our capital

⁵¹ Benefits delivered through future bill reductions (Totex savings), ODI service improvements and reinvestment

⁵² Common ODIs – 12 financial and 2 reputational measures for 2020-2025

investment partners who will transition to our capital alliance H5O. In addition we have secured a number of other partners including universities, housing associations, customer advocates and environmental charities.

South West Water has also focused on preparing for operational excellence and early planning of our investment programme. This includes pilot trials of new water treatment technology in Bournemouth and supporting the Isles of Scilly operations over the summer months with preparatory work for take-over already in progress.

VIRIDOR

Confident outlook for Viridor in the waste sector

Viridor is focused on UK recycling and residual waste processing and transformation.

Recycling

The Government's Resource & Waste Strategy is expected to confirm the fundamentals of the waste market and provide a stimulus to recycling. The 'Blue Planet' effect continues to drive Government action and there are potential opportunities arising from Brexit which also require consideration.

The UK Plastics Pact (a unique pact between governments, businesses, local authorities, NGOs and citizens) is seeking to transform the UK's plastics system. The pact has targets including:

- 100% of plastic packaging to be reusable or recyclable
- 70% of plastic packaging effectively recycled (from current 43%)
- Problematic or unnecessary single-use plastics eliminated
- 30% average recycled content across all plastic packaging.

EPR & PRN⁵³ reform is also recommended by the National Audit Office and is expected to improve the returns from investments in recycling, a key factor being standardised collections increasing household waste quality.

Viridor's 2018 Recycling Index Report shows that over 80% of the public is worried about plastics in the oceans, and over 60% of consumers were more likely to buy products with packaging made from recycled materials.

Residual waste activities (ERFs and Landfill)

The market fundamentals for ERFs remain strong, with the gap between combustible residual waste arisings and ERF capacity forecast to remain over 7 million tonnes (mT) per annum to 2030.

⁵³ EPR – Extended Producer Responsibility; PRN – Packaging Recovery Note

In addition the Autumn Budget noted that ‘the Government recognises the important role incineration currently plays in waste management in the UK...’.

The Viridor portfolio processes a fifth of the UK ERF combustible waste tonnage and continues to optimise its assets through capacity expansions, heat transfer and offtake opportunities.

Viridor recognises that the landfill portfolio complements its residual waste strategy. We continue to foresee a requirement for a landfill solution into the medium term. As landfill sites close over the coming years, parts of the country will experience a shortage of capacity. Viridor’s landfill sites are well positioned to support future market requirements. Available void on operating sites is c.30 million cubic metres, equivalent to c.15 years overall capacity at current run rates, with 5 sites having capacity to 2030 and beyond.

Strong operational focus

	H1 2018/19	H1 2017/18
Total Waste Inputs (mT)	3.5	3.9
ERFs	1.0	1.1
Landfill	0.9	0.9
Recycling and Other	1.6	1.9
Recycling Volumes Traded	0.6	0.7
ERF availability ⁵⁴	89%	90%

ERFs continuing to perform strongly

Our ERFs have delivered strong operational performance in the first half of 2018/19.

We are on track to deliver another year of availability in excess of 90% across our operational portfolio (including joint ventures). As we continue to optimise our performance, more of our planned maintenance outages have been completed in the first half of the financial year, when electricity demand and pricing is lower. Planned maintenance has been performed at all major sites during the half year. Cumulatively to date maintenance is running at c.2.1% of capital expenditure. This is expected to increase over the life of the assets with an underlying future average rate of c.3.5%.

Glasgow, Beddington and Dunbar are all processing waste. Optimisation is ongoing and operations will ramp up over the next 18 months, as has previously occurred at the other ERFs in our portfolio.

As previously reported, completion of construction of our Glasgow Recycling and Renewable Energy Centre has required a higher level of remediation and expenditure than predicted. This has been driven by the high level of non-conformances that have required rectification for work

⁵⁴ Rebasing planned maintenance on a consistent basis, H1 2018/19 availability would be >90%

performed by our previous Engineering, Procurement and Construction (EPC) contractor. Viridor is contractually entitled to recover incremental costs from the original principal contractor, Interserve, under certain circumstances. Discussions with Interserve are ongoing with regard to the contractual settlement. The gross receivable is £72 million, after taking into account an assessment of market indicators of credit risk for the EPC contractor, a provision of £8 million has been recognised resulting in a net receivable of £64 million at 30 September 2018.

Construction work progresses at Avonmouth and is on track for takeover in line with the planned costs and timetable. Processing equipment is now being erected within the structural steel frame.

With the new facilities burning waste, our operational design capacity has increased to 2.9 million tonnes of waste and 242 megawatts (MW) per annum, including joint ventures. This will extend to 3.2 million tonnes of waste and 276 MW by 2021.

Responding to recycling markets

Following the impact that import restrictions imposed by China had on global recycling markets in H2 2017/18, we have seen some recovery in H1 2018/19. Paper prices have improved from their low point, and pricing on other commodities are slightly ahead of last year.

We have continued to focus on producing higher quality recyclates to fulfil market demands and revenue per tonne has increased 13.4% to £110 (H1 2017/18 £97, H2 2017/18 £97). This increase in quality requirement has resulted in increased costs of production and a reduction in volumes being produced.

We remain confident that our recycling business is on track for full year results in line with our expectations.

We have made good progress with our FMCG⁵⁵ customers in the period in developing 'closed-loop' solutions, providing high quality recycled plastics and polymers. Utilising innovative technology and processes we are creating value from the requirement for recycled materials, to replace virgin material in premium consumer packaging.

Landfill portfolio complements residual waste strategy

Viridor continued to operate 11 landfill sites in H1 2018/19, with one site at Rigmuir (Glasgow) closed in September as part of the planned closure profile leaving 10 operational sites. Consented landfill capacity reduced from 40.5 million cubic metres (mcm) to 30 mcm in the 6 months to September 2018, reflecting usage during the period and the closure of Rigmuir. We have a track record of effectively restoring our sites and repurposing these for alternative uses with 3 closed landfill sites repurposed for development in recent years.

⁵⁵ FMCG – Fast Moving Consumer Goods

Landfill volumes and average gate fees are comparable with H1 last year at 0.9 million tonnes and £22 per tonne. Our landfill energy business continues to be managed to maximise the value of landfill gas power generation. We continue to explore alternative commercial development opportunities and other renewable energy solutions at our landfill sites, such as photovoltaic (PV) and energy storage.

At present, Viridor's landfill gas engines contribute 86MW of landfill gas generation capacity, a decrease from 88MW at March 2018. This reflects the replacement of larger older engines with smaller more efficient engines designed to optimise the gas volumes produced at the sites. Viridor also has a PV capacity of 3.2MW. We currently have surplus grid connection capacity at some sites, which presents an opportunity for growth subject to suitable capital investment. Investment opportunities to create energy parks, including private wire connections to local industry and developments are being assessed.

Average revenue per Megawatt hour (MWh) increased by 7.4% to £87 (H1 2017/18 £81). Average operating costs increased 23.1% to £48 per MWh (H1 2017/18 £39) reflecting increased investment in planned preventative maintenance to secure reliable generation, including for the upcoming winter period.

Revenue during the period has increased by 2.8% compared to H1 2017/18, with a 4% reduction in gas volumes in H1 2018/19 being offset by the higher energy prices.

Contracts and Collections

The run-off contract to operate the recycling assets of the Greater Manchester Combined Authority has delivered in line with expectations. In November 2018 Viridor withdrew from the Greater Manchester waste operating contract tender process and we expect the run-off contract to cease in early 2019/20. The financial impact of not continuing with an operational contract is not material to the Group, and our position with the ERFs at Runcorn is unaffected.

Our Contract and Collections business continues to provide a valuable service to all our customers and secures the volume of input materials needed to operate our ERF, landfill and recycling assets.

Joint Ventures continue to perform strongly

The joint venture at Lakeside ERF (a 50:50 joint venture with Grundon Waste Management) has had another strong half year. In its ninth year of operation it continues to outperform its original targets for both waste processing and power generation.

The TPSCo joint venture (between Viridor, John Laing Investments and Inovyn) has also performed strongly during the half year.

In November 2018, Viridor exercised its pre-emption rights and agreed a £54.5 million cash consideration to acquire John Laing Investments Limited's 37.5% economic interest and 20% voting rights in the Runcorn I ERF. The acquisition consolidates further Viridor's leading market position in UK Energy Recovery and results in an increase to Pennon's economic interest in INEOS Runcorn (TPS) Holdings Limited from 37.5% to 75.0%, with the associated voting rights moving from 20% to 40%.

PENNON WATER SERVICES

Focus on delivering operating cost efficiencies

Pennon Water Services (PWS), our 80:20 retail venture with South Staffordshire Plc, continues to deliver net customer⁵⁶ and revenue growth during its second year of operation, with continued success with the dual service position.

Serving over 160,000 customer accounts across 18 different wholesale regions, Pennon Water Services has c.10,000⁵⁶ new customer accounts generating around £31 million of new revenue, with 100% new contract renewal rate to date.

We continue to focus on delivering customer service that reflects the needs of our business customers with satisfaction scores increasing in the period. We are now implementing further strategies to improve operating cost efficiency within the competitive market including within billing and cash management.

⁵⁶ As at 19 November 2018. c.10,000 new accounts, net growth of c.2,000 accounts

Board Matters

As previously announced and in line with governance best practice, Martin Angle, Non-Executive Director and chairman of the Remuneration Committee, who has been a Director for nine years, will stand down from the Board on 31 December 2018. Iain Evans has been appointed as his successor and joined the Board in September 2018. We thank Martin for his considerable contribution to the Group's success and strong governance over the years.

Chris Loughlin
Group Chief Executive Officer
27 November 2018

Financial Timetable

24 January 2019	Ex-dividend date
25 January 2019	Record date
January 2019	Viridor Waste Capital Markets Day
8 March 2019	Final date for receipt of DRIP applications
25 March 2019	Trading Statement
4 April 2019	Interim dividend payment date
4 June 2019	Full Year Results 2018/19
Early June 2019	Annual Report & Accounts published
25 July 2019	Annual General Meeting
25 July 2019*	Ordinary shares quoted ex-dividend
26 July 2019*	Record date for final dividend
12 August 2019*	Final date for receipt of DRIP applications
3 September 2019*	Final dividend paid
September 2019	Trading Statement
26 November 2019	Half Year Results 2019/20

* These dates are provisional and, in the case of the final dividend subject to obtaining shareholder approval at the 2019 Annual General Meeting.

PRINCIPAL RISKS AND UNCERTAINTIES

In accordance with DTR4.2.3 and 4.2.7 of the Disclosure & Transparency Rules, the principal risks and the associated residual risk exposure for the remaining six months of the financial year have been reviewed by the Directors and are considered to be unchanged from those reported on pages 55 to 60 of the Annual Report and Accounts 2018. A summary of Pennon Group's principal risks is detailed below.

These principal risks have been reconsidered against a continued back drop of broader macro political and economic uncertainties; including the potential renationalisation of the water industry in the event of a change in Government and ongoing negotiations between the UK and the EU on any withdrawal agreement.

Specifically, the Board has considered the potential implications of a 'no deal' scenario between the UK and the EU on the Group's principal risks, which was informed by guidance documentation issued by the UK Government. Appropriate mitigation strategies have been developed in order to minimise any potential impact on the Group.

The Board considers the principal risks to be:

Law, Regulation and Finance

- Changes in Government Policy – renationalisation
- Changes in Government Policy – single use plastics
- Regulatory 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
- Increase in the defined benefit pension scheme deficit

Market and Economic Conditions

- Non-recovery of customer debt
- Macro-economic risks arising from global and UK economic downturn impacting commodity and power prices

Operating Performance

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

Business Systems and Capital Investment

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

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 on renationalisation and use of single use plastics; regulatory 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; increase in defined benefit pension scheme deficit; non-recovery of customer debt; poor operating performance due to extreme weather or climate change; macro-economic risks impacting commodity and power; poor service and/or increased competition leading to loss of customers; business interruption or significant operational failure/incidents; difficulty in recruitment, retention and development of skills; failure or increased cost of capital projects/exposure to contract failures; and failure of information technology systems, management and protection, including cyber risks. These risks were described in greater detail in the Pennon Group Annual Report published at the beginning of June 2018. Such forward looking statements should therefore be construed in light of such risks, uncertainties and other factors and undue reliance should not be placed on them. Nothing in this report should be construed as a profit forecast.

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

UNSOLICITED COMMUNICATIONS WITH SHAREHOLDERS

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

PENNON GROUP PLC
Consolidated income statement for the half year ended 30 September 2018

	Notes	Unaudited					
		Before non-underlying items half year ended 30 September 2018 £m	Non-underlying items (note 5) half year ended 30 September 2018 £m	Total half year ended 30 September 2018 £m	Before non-underlying items half year ended 30 September 2017 £m	Non-underlying items (note 5) half year ended 30 September 2017 £m	Total half year ended 30 September 2017 £m
Revenue	4	746.7	-	746.7	723.9	3.2	727.1
Operating costs							
Employment costs		(101.5)	-	(101.5)	(99.1)	-	(99.1)
Raw materials and consumables used		(70.2)	-	(70.2)	(60.0)	-	(60.0)
Other operating expenses		(301.0)	-	(301.0)	(311.3)	-	(311.3)
Earnings before interest, tax, depreciation and amortisation	4	274.0	-	274.0	253.5	3.2	256.7
Depreciation and amortisation		(95.5)	-	(95.5)	(91.1)	-	(91.1)
Operating profit	4	178.5	-	178.5	162.4	3.2	165.6
Finance income	6	11.5	-	11.5	13.5	-	13.5
Finance costs	6	(52.3)	(8.9)	(61.2)	(50.1)	(27.0)	(77.1)
Net finance costs	6	(40.8)	(8.9)	(49.7)	(36.6)	(27.0)	(63.6)
Share of post-tax profit from joint ventures		4.8	-	4.8	5.3	22.5	27.8
Profit before tax	4	142.5	(8.9)	133.6	131.1	(1.3)	129.8
Taxation	7	(19.3)	1.7	(17.6)	(21.8)	4.3	(17.5)
Profit for the period		123.2	(7.2)	116.0	109.3	3.0	112.3
Attributable to:							
Ordinary shareholders of the parent		114.7	(7.2)	107.5	87.9	3.0	90.9
Non-controlling interests		(0.1)	-	(0.1)	(0.1)	-	(0.1)
Perpetual capital security holders		8.6	-	8.6	21.5	-	21.5
Earnings per ordinary share (pence per share)	8						
- Basic				25.6			21.8
- Diluted				25.5			21.7

The notes on pages 39 to 58 form part of this condensed half year financial information.

PENNON GROUP PLC
Consolidated statement of comprehensive income for the half year ended 30 September 2018

	Unaudited					
	Before non- underlying items half year ended 30 September 2018 £m	Non-underlying items (note 5) half year ended 30 September 2018 £m	Total half year ended 30 September 2018 £m	Before non- underlying items half year ended 30 September 2017 £m	Non-underlying items (note 5) half year ended 30 September 2017 £m	Total half year ended 30 September 2017 £m
Profit for the period	123.2	(7.2)	116.0	109.3	3.0	112.3
Other comprehensive income						
<i>Items that will not be reclassified to profit or loss</i>						
Remeasurement of defined benefit obligations (note 16)	7.6	-	7.6	15.3	-	15.3
Income tax on items that will not be reclassified	(1.3)	-	(1.3)	(2.5)	-	(2.5)
Total items that will not be reclassified to profit or loss	6.3	-	6.3	12.8	-	12.8
<i>Items that may be reclassified subsequently to profit or loss</i>						
Share of other comprehensive income from joint ventures	0.7	-	0.7	(3.9)	-	(3.9)
Cash flow hedges	4.1	-	4.1	15.0	-	15.0
Income tax on items that may be reclassified	(1.1)	-	(1.1)	(2.6)	-	(2.6)
Total items that may be reclassified subsequently to profit or loss	3.7	-	3.7	8.5	-	8.5
Other comprehensive income for the period net of tax	10.0	-	10.0	21.3	-	21.3
Total comprehensive income for the period	133.2	(7.2)	126.0	130.6	3.0	133.6
Total comprehensive income attributable to:						
Ordinary shareholders of the parent	124.7	(7.2)	117.5	109.2	3.0	112.2
Non-controlling interests	(0.1)	-	(0.1)	(0.1)	-	(0.1)
Perpetual capital security holders	8.6	-	8.6	21.5	-	21.5

The notes on pages 39 to 58 form part of this condensed half year financial information.

PENNON GROUP PLC
Consolidated balance sheet at 30 September 2018

		<u>Unaudited</u>	
		30 September	31 March
		2018	2018
		£m	£m
	Notes		
ASSETS			
Non-current assets			
Goodwill		385.0	385.0
Other intangible assets		73.0	72.6
Property, plant and equipment		4,412.3	4,310.6
Other non-current assets		266.2	263.5
Derivative financial instruments		60.0	70.5
Investments in joint ventures		28.3	22.8
		5,224.8	5,125.0
Current assets			
Inventories		30.2	24.6
Trade and other receivables		483.2	416.0
Derivative financial instruments		10.1	12.9
Cash and cash deposits	14	405.7	585.3
		929.2	1,038.8
LIABILITIES			
Current liabilities			
Borrowings	14	(109.4)	(209.8)
Financial liabilities at fair value through profit		(2.6)	(2.6)
Derivative financial instruments		(9.5)	(9.4)
Trade and other payables	18	(311.1)	(342.0)
Current tax liabilities		(24.6)	(24.4)
Provisions		(41.3)	(38.0)
		(498.5)	(626.2)
Net current assets		430.7	412.6
Non-current liabilities			
Borrowings	14	(3,338.2)	(3,177.0)
Other non-current liabilities	18	(148.0)	(140.1)
Financial liabilities at fair value through profit		(45.6)	(46.6)
Derivative financial instruments		(4.6)	(8.2)
Retirement benefit obligations	16	(44.8)	(49.5)
Deferred tax liabilities		(303.1)	(295.6)
Provisions		(172.6)	(181.5)
		(4,056.9)	(3,898.5)
Net assets		1,598.6	1,639.1
Shareholders' Equity			
Share capital	10	171.0	170.8
Share premium account	11	222.3	218.8
Capital redemption reserve		144.2	144.2
Retained earnings and other reserves		763.0	807.1
Total shareholders' equity		1,300.5	1,340.9
Non-controlling interests		1.4	1.5
Perpetual capital securities	12	296.7	296.7
Total equity		1,598.6	1,639.1

The notes on pages 39 to 58 form part of this condensed half year financial information.

PENNON GROUP PLC
Consolidated statement of changes in equity for the half year ended 30 September 2018

	Unaudited						
	Share capital (note 10)	Share premium account (note 11)	Capital redemption reserve	Retained earnings and other reserves	Non- controlling interests	Perpetual capital securities (note 12)	Total Equity
	£m	£m	£m	£m	£m	£m	£m
At 1 April 2017	168.4	217.4	144.2	684.4	-	294.8	1,509.2
Profit for the period	-	-	-	90.9	(0.1)	21.5	112.3
Other comprehensive income for the period	-	-	-	21.3	-	-	21.3
Total comprehensive income for the period	-	-	-	112.2	(0.1)	21.5	133.6
<i>Transactions with equity shareholders:</i>							
Dividends paid	-	-	-	(149.5)	-	-	(149.5)
Adjustment for shares issued under the Scrip Dividend Alternative	2.1	(2.1)	-	41.7	-	-	41.7
Adjustment in respect of share-based payments (net of tax)	-	-	-	1.8	-	-	1.8
Issuance of perpetual capital securities	-	-	-	-	-	296.7	296.7
Redemption of perpetual capital securities	-	-	-	(5.2)	-	(294.8)	(300.0)
Distributions due to perpetual capital security holders	-	-	-	-	-	(25.3)	(25.3)
Current tax relief on distributions to perpetual capital security holders	-	-	-	-	-	3.8	3.8
Own shares acquired by the Pennon Employee Share Trust in respect of Share options granted	0.1	0.4	-	(1.8)	-	-	(1.3)
Proceeds from shares issued under the Sharesave Scheme	0.2	2.5	-	-	-	-	2.7
Non-controlling interests	-	-	-	-	0.7	-	0.7
	2.4	0.8	-	(113.0)	0.7	(19.6)	(128.7)
At 30 September 2017	170.8	218.2	144.2	683.6	0.6	296.7	1,514.1
	Unaudited						
	Share capital (note 10)	Share premium account (note 11)	Capital redemption reserve	Retained earnings and other reserves	Non- controlling interests	Perpetual capital securities (note 12)	Total Equity
	£m	£m	£m	£m	£m	£m	£m
At 1 April 2018	170.8	218.8	144.2	807.1	1.5	296.7	1,639.1
Profit for the period	-	-	-	107.5	(0.1)	8.6	116.0
Other comprehensive income for the period	-	-	-	10.0	-	-	10.0
Total comprehensive income for the period	-	-	-	117.5	(0.1)	8.6	126.0
<i>Transactions with equity shareholders:</i>							
Dividends paid	-	-	-	(162.0)	-	-	(162.0)
Adjustment in respect of share-based payments (net of tax)	-	-	-	1.9	-	-	1.9
Distributions due to perpetual capital security holders	-	-	-	-	-	(8.6)	(8.6)
Own shares acquired by the Pennon Employee Share Trust in respect of Share options granted	-	-	-	(1.5)	-	-	(1.5)
Proceeds from shares issued under the Sharesave Scheme	0.2	3.5	-	-	-	-	3.7
	0.2	3.5	-	(161.6)	-	(8.6)	(166.5)
At 30 September 2018	171.0	222.3	144.2	763.0	1.4	296.7	1,598.6

The notes on pages 39 to 58 form part of this condensed half year financial information.

PENNON GROUP PLC
Consolidated statement of cash flows for the half year ended 30 September 2018

		Unaudited	
		Half year ended 30 September 2018 £m	Half year ended 30 September 2017 £m
	Notes		
Cash flows from operating activities			
Cash generated from operations	13	151.7	211.2
Interest paid		(31.4)	(33.2)
Tax paid		(12.2)	(10.4)
Net cash generated from operating activities		108.1	167.6
Cash flows from investing activities			
Interest received		4.4	1.9
Dividends received		-	1.0
Loan repayments received from joint ventures		2.0	23.7
Purchase of property, plant and equipment		(181.9)	(198.1)
Proceeds from sale of property, plant and equipment		0.5	7.1
Purchase of intangible assets		-	(0.5)
Acquisition of subsidiary undertakings		-	(7.0)
Deposit of restricted cash		(3.7)	-
Net cash used in investing activities		(178.7)	(171.9)
Cash flows from financing activities			
Proceeds from issuance of ordinary shares		3.7	3.2
Proceeds from the issuance of perpetual capital securities		-	296.7
Redemption and periodic return of 2013 perpetual capital securities		-	(304.8)
Disposal of non-controlling interest		-	0.7
Deposit of restricted funds		-	(3.7)
Purchase of ordinary shares by the Pennon Employee Share Trust		(1.5)	(1.8)
Proceeds from new borrowing	14	50.0	56.3
Repayment of borrowings	14	(16.1)	(50.1)
Finance lease sale and leaseback	14	35.0	100.0
Finance lease principal repayments	14	(16.0)	(15.1)
Dividends paid	9	(162.0)	(107.8)
Perpetual capital securities periodic return		(5.8)	-
Net cash used in financing activities		(112.7)	(26.4)
Net decrease in cash and cash equivalents			
		(183.3)	(30.7)
Cash and cash equivalents at beginning of period	14	403.0	374.3
Cash and cash equivalents at end of period		219.7	343.6

The notes on pages 39 to 58 form part of this condensed half year financial information.

PENNON GROUP PLC**Notes to condensed half year financial information****1. General information**

Pennon Group plc is a company registered in the United Kingdom (UK) under the Companies Act 2006. The address of the registered office is given on page 58. Pennon Group's business is operated through two principal subsidiaries. South West Water Limited includes the merged 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. Viridor Limited's business is recycling, energy recovery and waste management. 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.

This condensed half year financial information was approved by the Board of Directors on 26 November 2018.

The financial information for the period ended 30 September 2018 does not constitute statutory accounts within the meaning of section 435 of the Companies Act 2006. The statutory accounts for 31 March 2018 were approved by the Board of Directors on 24 May 2018 and have been delivered to the Registrar of Companies. The independent auditor's report on these financial statements was unqualified, and did not contain a statement under section 498 of the Companies Act 2006.

2. Basis of preparation

This condensed half year financial information has been prepared in accordance with the Disclosure and Transparency Rules of the Financial Services Authority and with IAS 34 "Interim financial reporting" as adopted by the European Union (EU). This condensed half year financial information should be read in conjunction with the Pennon Group plc Annual Report and Accounts for the year ended 31 March 2018, which were prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the EU.

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

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

The preparation of the half year financial information requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets and liabilities, income and expense. Actual results may differ from these estimates. The significant judgements made by management in applying the Group's accounting policies and the key sources of estimation uncertainty are consistent with those that applied to the consolidated financial statements for the year ended 31 March 2018, with the exception of changes in estimates that are required in determining the half year provision of income taxes.

PENNON GROUP PLC**Notes to condensed half year financial information (continued)****3. Accounting policies**

Other than the revised policy on revenue as a result of the application of IFRS 15, as set out in note 21 below, the accounting policies adopted in this condensed half year financial information are consistent with those applied and set out in the Pennon Group plc Annual Report and Accounts for the year ended 31 March 2018 and are in accordance with all IFRSs and interpretations of the IFRS Interpretations Committee expected to be applicable for the year ending 31 March 2019 in issue which have been adopted by the EU.

The tax charge for September 2018 and September 2017 has been derived by applying the anticipated effective annual rate to the first half year profit before tax.

New standards or interpretations which were mandatory for the first time in the year beginning 1 April 2018 did not have a material impact on the net assets or results of the Group.

New standards or interpretations due to be adopted from 1 April 2019, including IFRS 16 'Leases' are not expected to have a material impact on the Group's net assets or results. Existing borrowing covenants are not impacted by changes in accounting standards.

As disclosed in the Pennon Group plc Annual Report and Accounts for the year ended 31 March 2018 the Directors anticipate the adoption of IFRS 16 on 1 April 2019 will affect primarily the accounting for the Group's operating leases. At 31 March 2018 the Group had non-cancellable operating lease commitments of £163 million. These predominantly relate to leases of properties occupied by the Group in the course of carrying out its businesses. If the standard had been adopted for the year ended 31 March 2018 it is estimated that this would have resulted in the Group recognising an asset in use and corresponding lease liability figure in the region of £115 million. This would have resulted in a minimal impact of profit before tax but an estimated increase of around £7 million to EBITDA which would be replaced by increased charges for depreciation and finance costs.

Initial adoption of IFRS 15 Revenue from Contracts with Customers

The Group adopted the standard with effect from 1 April 2018 using the full retrospective approach to transition. As the impact of the new standard has not had a material effect on the Group's reported revenues, net assets or any specific financial statement line, there has been no restatement of prior year figures.

The disaggregation of revenue information required by IFRS 15 is given below within note 4 (Segmental information) for the six month periods ended 30 September 2018 and 30 September 2017.

The revised accounting policy on revenue following implementation of IFRS 15 is set out below in note 21.

Initial adoption of IFRS 9 Financial Instruments

IFRS 9, which applies from 1 April 2018, requires the Group to evaluate and recognise expected credit losses on financial assets and to ensure changes in credit risk are assessed at regular intervals, and to make suitable adjustments for expected credit losses where applicable.

As disclosed within note 4 Critical accounting judgements and estimates in the Pennon Group Plc Annual Report and Accounts for the year ended 31 March 2018, at the balance sheet date each subsidiary evaluates the collectability of trade receivables and records provisions for doubtful debts based on experience including comparisons of the relative age of accounts and consideration of actual write-off history. On adoption of IFRS 9 the evaluation has been extended to include the forward-looking assessment of expected credit losses and changes in credit risk. Adoption of the new approach has not had a material impact on the impairment of trade receivables.

PENNON GROUP PLC
Notes to the condensed half year financial information (continued)
4. Segmental information

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

The water business comprises the regulated water and wastewater services undertaken by South West Water. The waste management business is the recycling, energy recovery and waste management services provided by Viridor. The non-household retail business reflects the services provided by Pennon Water Services following the opening of the non-household water and wastewater retail market to competition on 1 April 2017.

	Unaudited	
	Half year ended 30 September 2018 £m	Half year ended 30 September 2017 £m
Revenue		
Water	301.5	292.2
Waste management	422.3	410.2
Non-household retail	84.1	83.5
Other	10.6	7.2
Less intra-segment trading	(71.8)	(66.0)
	746.7	727.1
Segment result		
Operating profit before depreciation, amortisation and non-underlying items (EBITDA)		
Water	194.7	187.1
Waste management	78.4	66.6
Non-household retail	0.9	0.5
Other	-	(0.7)
	274.0	253.5
Operating profit before non-underlying items		
Water	135.9	130.7
Waste management	42.1	32.4
Non-household retail	0.5	0.2
Other	-	(0.9)
	178.5	162.4
Profit before tax and non-underlying items		
Water	100.3	96.2
Waste management	36.2	30.6
Non-household retail	(0.5)	(0.5)
Other	6.5	4.8
	142.5	131.1
Profit before tax		
Water	91.2	87.2
Waste management	36.2	37.1
Non-household retail	(0.5)	(0.5)
Other	6.7	6.0
	133.6	129.8

PENNON GROUP PLC
Notes to the condensed half year financial information (continued)
4. Segmental information (continued)

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

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

The grouping of revenue streams by how they are affected by economic factors, as required by IFRS 15, is as follows:

Six months ended 30 September 2018 Unaudited	Water	Waste Management (WM)					Non-Household Retail	Other	Total
	UK Total	UK	Rest of EU	China	Rest of World	WM Total	UK Total	UK Total	
	£m	£m	£m	£m	£m	£m	£m	£m	£m
Segment revenue	301.5	400.1	6.6	10.6	5.0	422.3	84.1	10.6	818.5
Inter-segment revenue	(59.9)	-	-	-	-	-	(1.3)	(10.6)	(71.8)
Revenue from external customers	241.6	400.1	6.6	10.6	5.0	422.3	82.8	-	746.7
Significant service lines									
Water	241.6	-	-	-	-	-	-	-	241.6
Non-household retail	-	-	-	-	-	-	82.8	-	82.8
Waste management services	-	342.8	-	-	-	342.8	-	-	342.8
Energy	-	26.0	-	-	-	26.0	-	-	26.0
Recyclate	-	31.3	6.6	10.6	5.0	53.5	-	-	53.5
	241.6	400.1	6.6	10.6	5.0	422.3	82.8	-	746.7

Six months ended 30 September 2017 Unaudited	Water	Waste Management (WM)					Non-Household Retail	Other	Total
	UK Total	UK	Rest of EU	China	Rest of World	WM Total	UK Total	UK Total	
	£m	£m	£m	£m	£m	£m	£m	£m	£m
Segment revenue	292.2	378.8	6.4	20.4	4.6	410.2	83.5	7.2	793.1
Inter-segment revenue	(57.8)	-	-	-	-	-	(1.0)	(7.2)	(66.0)
Revenue from external customers	234.4	378.8	6.4	20.4	4.6	410.2	82.5	-	727.1
Significant service lines									
Water	234.4	-	-	-	-	-	-	-	234.4
Non-household retail	-	-	-	-	-	-	82.5	-	82.5
Waste management services	-	324.5	-	-	-	324.5	-	-	324.5
Energy	-	23.3	-	-	-	23.3	-	-	23.3
Recyclate	-	31.0	6.4	20.4	4.6	62.4	-	-	62.4
	234.4	378.8	6.4	20.4	4.6	410.2	82.5	-	727.1

PENNON GROUP PLC
Notes to the condensed half year financial information (continued)
5. Non-underlying items

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

	Unaudited	
	Half year ended 30 September 2018 £m	Half year ended 30 September 2017 £m
Revenue		
Construction contract settlements (1a)	-	3.2
Earnings before interest, tax, depreciation and amortisation	-	3.2
Remeasurement of fair value movement in derivatives (2)	(8.9)	(7.8)
Write-down of joint venture shareholder loans (1b)	-	(19.2)
Refinancing of joint venture arrangement (1c)	-	22.5
Tax credit arising on non-underlying items	1.7	4.3
Net non-underlying (charge) / credit	(7.2)	3.0

1 Last year, on reset of the contracts associated with the Greater Manchester Waste Disposal Authority (GMWDA) an overall net credit before tax of £6.5m was recognised as follows:

- (a) A net amount of £3.2m was recognised in revenue following the settlement of all outstanding claims relating to the construction of assets.
- (b) On reset of the contracts associated with GMWDA, ownership of Viridor Laing Holdings Limited passed to the GMWDA. On transfer £23.5m of Viridor's shareholder loans were repaid, resulting in the write down of the remaining financial asset of £19.2m.
- (c) On reset of the contracts associated with GMWDA repayment of external bank debt in our joint venture, INEOS Runcorn TPSCo Limited, was financed by GMWDA. This change in cash flows resulted in the recognition of income in this joint venture, with an amount deferred relating to a lower ongoing gate fee. The overall share of profit after tax in the half year related to the reset was £22.5m, which contributed to an increase in investments in joint ventures recognised on the balance sheet to £23.0m (31 March 2017 £0.1m).

2 In the period a charge of £8.9m was recognised relating to non-cash derivative fair value movements associated with derivatives that are not designated as being party to an accounting hedge relationship (H1 2017/18 £7.8m). These movements are non-underlying due to the nature of the item being market dependant and potentially can be significant in value (size).

PENNON GROUP PLC
Notes to the condensed half year financial information (continued)
6. Net finance costs

	Unaudited					
	Half year ended 30 September 2018			Half year ended 30 September 2017		
	Finance cost £m	Finance income £m	Total £m	Finance cost £m	Finance income £m	Total £m
Cost of servicing debt						
Bank borrowings and overdrafts	(25.0)	-	(25.0)	(25.8)	-	(25.8)
Interest element of finance lease rentals	(19.6)	-	(19.6)	(17.1)	-	(17.1)
Other finance costs	(1.4)	-	(1.4)	(1.5)	-	(1.5)
Interest receivable	-	1.7	1.7	-	1.1	1.1
Interest receivable on shareholder loans to joint ventures	-	2.5	2.5	-	5.5	5.5
	(46.0)	4.2	(41.8)	(44.4)	6.6	(37.8)
Notional interest						
Interest receivable on service concession arrangements	-	7.3	7.3	-	6.9	6.9
Retirement benefit obligations	(0.9)	-	(0.9)	(0.9)	-	(0.9)
Unwinding of discounts on provisions	(5.4)	-	(5.4)	(4.8)	-	(4.8)
	(6.3)	7.3	1.0	(5.7)	6.9	1.2
Net finance costs before non-underlying items	(52.3)	11.5	(40.8)	(50.1)	13.5	(36.6)
Non-underlying items (note 5)						
Write-down of joint venture shareholder loans	-	-	-	(19.2)	-	(19.2)
Fair value remeasurement of non-designated derivative financial instruments, providing commercial hedges	(8.9)	-	(8.9)	(7.8)	-	(7.8)
	(8.9)	-	(8.9)	(27.0)	-	(27.0)
Net finance costs after non-underlying items	(61.2)	11.5	(49.7)	(77.1)	13.5	(63.6)

PENNON GROUP PLC
Notes to the condensed half year financial information (continued)
7. Taxation

	Before non-underlying items half year ended 30 September 2018 £m	Non-underlying items (note 5) half year ended 30 September 2018 £m	Total half year ended 30 September 2018 £m	Before non-underlying items half year ended 30 September 2017 £m	Non-underlying items (note 5) half year ended 30 September 2017 £m	Total half year ended 30 September 2017 £m
Analysis of charge						
Current tax charge	12.4	-	12.4	10.0	(3.0)	7.0
Deferred tax	6.9	(1.7)	5.2	11.8	(1.3)	10.5
Tax charge for the period	19.3	(1.7)	17.6	21.8	(4.3)	17.5

UK corporation tax is calculated at 19% (H1 2017/18 19%) of the estimated assessable profit for the year. The tax charge for September 2018 and September 2017 has been derived by applying the anticipated effective annual tax rate to the first half year profit before tax.

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

The effective tax rate for the period before the impact of non-underlying items was 14% (H1 2017/18 17%).

The effective tax rate for the period including the impact of non-underlying items was 13% (H1 2017/18 13%).

PENNON GROUP PLC
Notes to the condensed half year financial information (continued)
8. Earnings per share

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

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

	Unaudited	
	Half year ended 30 September 2018	Half year ended 30 September 2017
Number of shares (millions)		
For basic earnings per share	419.3	416.6
Effect of dilutive potential ordinary shares from share options	1.1	1.5
For diluted earnings per share	420.4	418.1

Adjusted basic and diluted earnings per ordinary share

Adjusted earnings per share are presented to provide a more useful comparison on business trends and performance. Non-underlying items are adjusted for by virtue of their size, nature or incidence to enable a full understanding of the Group's financial performance (as described in note 5). Perpetual capital returns are proportionately adjusted to allow a more useful comparison in the period. Earnings per share have been calculated as follows:

	Unaudited					
	Half year ended 30 September 2018			Half year ended 30 September 2017		
	Profit after tax £m	Earnings per share		Profit after tax £m	Earnings per share	
		Basic p	Diluted p		Basic p	Diluted p
Statutory earnings	107.5	25.6	25.5	90.9	21.8	21.7
Deferred tax before non-underlying items	6.9	1.7	1.7	11.8	2.8	2.8
Non-underlying items (net of tax)	7.2	1.7	1.7	(3.0)	(0.7)	(0.7)
Proportionate impact of perpetual capital returns (note 12)	4.3	1.0	1.0	5.8	1.4	1.4
Earnings before non-underlying items and deferred tax	125.9	30.0	29.9	105.5	25.3	25.2

PENNON GROUP PLC
Notes to the condensed half year financial information (continued)
9. Dividends
Amounts recognised as distributions to ordinary equity holders in the period:

	Unaudited	
	Half year ended 30 September 2018 £m	Half year ended 30 September 2017 £m
Interim dividend paid for the year ended 31 March 2018 : 11.97p (2017 11.09p) per share	50.2	45.9
Final dividend paid for the year ended 31 March 2018 : 26.62p (2017 24.87p) per share	111.8	103.6
	162.0	149.5

In the six months to 30 September 2018 the 2017/18 interim and final dividends were paid resulting in a cash outflow of £162.0m.

	Unaudited	
	Half year ended 30 September 2018 £m	Half year ended 30 September 2017 £m
Proposed interim dividend		
Proposed interim dividend for the year ended 31 March 2019 : 12.84p (2018 11.97p) per share	54.0	50.2

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

The proposed interim dividend for 2019 will be paid on 4 April 2019 to shareholders on the register on 25 January 2019.

PENNON GROUP PLC
Notes to the condensed half year financial information (continued)
10. Share capital
Allotted, called up and fully paid

	Unaudited		£m
	Number of shares		
1 April 2017 to 30 September 2017	Treasury shares	Ordinary shares	
At 1 April 2017 Ordinary shares of 40.7p each	8,443	413,893,293	168.4
Shares issued under the Scrip Dividend Alternative	-	5,223,089	2.1
For consideration of £0.5m, shares issued to the Pennon Employee Share Trust	-	46,205	0.1
For consideration of £2.7m, shares issued in respect of the Company's Sharesave Scheme	-	449,717	0.2
At 30 September 2017 ordinary shares of 40.7p each	8,443	419,612,304	170.8

	Unaudited		£m
	Number of shares		
1 April 2018 to 30 September 2018	Treasury shares	Ordinary shares	
At 1 April 2018 Ordinary shares of 40.7p each	8,443	419,743,183	170.8
For consideration of £3.7m, shares issued in respect of the Company's Sharesave Scheme	-	563,592	0.2
At 30 September 2018 ordinary shares of 40.7p each	8,443	420,306,775	171.0

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

The weighted average market price of the Company's shares at the date of exercise of Sharesave Scheme options during the year was 753p (H1 2017/18 806p).

PENNON GROUP PLC
Notes to the condensed half year financial information (continued)

11.	Share premium account	<u>Unaudited</u> £m
	1 April 2017 to 30 September 2017	
	At 1 April 2017	217.4
	Adjustment for shares issued under the Scrip Dividend Alternative	(2.1)
	Shares issued under the Sharesave Scheme	2.5
	Shares issued to the Pennon Employee Share Trust	0.4
	At 30 September 2017	<u>218.2</u>
	1 April 2018 to 30 September 2018	
	At 1 April 2018	218.8
	Shares issued under the Sharesave Scheme	3.5
	At 30 September 2018	<u>222.3</u>
12.	Perpetual capital securities	
		Unaudited
		Half year ended
		30 September
		2018
		£m
		Year ended
		31 March
		2018
		£m
	GBP 300m 2.875% perpetual subordinated capital securities	<u>296.7</u>
		<u>296.7</u>

On 22 September 2017 the Company issued £300m perpetual capital securities. Costs directly associated with the issue of £3.3m were set off against the value of the issuance. They have no fixed redemption date but the Company can at its sole discretion redeem all, but not part, of these securities at their principal amount on 22 May 2020 or any subsequent periodic return payment date after this.

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

As the Company paid a dividend on 4 April 2018 the periodic return of £8.6m, scheduled 22 May 2019, is payable and consequently has been recognised as a liability at 30 September 2018.

PENNON GROUP PLC
Notes to the condensed half year financial information (continued)
14. Net borrowings

	Unaudited	
	Half year	Year ended
	ended 30	31 March
	September	2018
	2018	2018
	£m	£m
Cash and cash deposits	405.7	585.3
<i>Borrowings – current</i>		
Bank and other loans	(52.7)	(149.6)
Other current borrowings	(29.5)	(32.0)
Finance lease obligations	(27.2)	(28.2)
Total current borrowings	(109.4)	(209.8)
<i>Borrowings – non-current</i>		
Bank and other loans	(1,556.3)	(1,408.8)
Other non-current borrowings	(277.9)	(291.4)
Finance lease obligations	(1,504.0)	(1,476.8)
Total non-current borrowings	(3,338.2)	(3,177.0)
Total net borrowings	(3,041.9)	(2,801.5)

PENNON GROUP PLC
Notes to the condensed half year financial information (continued)
14. Net borrowings (continued)

The movements in net borrowings during the periods presented were as follows:

	Unaudited					Net borrowings at 30 September 2017
	Net borrowings at 1 April 2017	Cash flows - other	Foreign exchange adjustments	Other non-cash movements		£m
	£m	£m	£m	£m		£m
Cash and cash deposits	598.1	(27.0)	-	-		571.1
Bank and other loans due within one year	(74.9)	25.0	-	49.9		-
Other current borrowings	(41.1)	25.1	-	(15.9)		(31.9)
Finance leases due within one year	(30.5)	7.6	-	(5.1)		(28.0)
Bank and other loans due after one year	(1,439.3)	(56.3)	(2.6)	(50.2)		(1,548.4)
Other non-current borrowings	(323.4)	-	-	16.0		(307.4)
Finance leases due after one year	(1,353.8)	(92.5)	-	-		(1,446.3)
Total	(2,664.9)	(118.1)	(2.6)	(5.3)		(2,790.9)

	Unaudited					Net borrowings at 30 September 2018
	Net borrowings at 1 April 2018	Cash flows - other	Foreign exchange adjustments	Other non-cash movements		£m
	£m	£m	£m	£m		£m
Cash and cash deposits	585.3	(179.6)	-	-		405.7
Bank and other loans due within one year	(149.6)	-	-	96.9		(52.7)
Other current borrowings	(32.0)	16.1	-	(13.6)		(29.5)
Finance leases due within one year	(28.2)	28.9	-	(27.9)		(27.2)
Bank and other loans due after one year	(1,408.8)	(50.0)	(0.9)	(96.6)		(1,556.3)
Other non-current borrowings	(291.4)	-	-	13.5		(277.9)
Finance leases due after one year	(1,476.8)	(35.0)	-	7.8		(1,504.0)
Total	(2,801.5)	(219.6)	(0.9)	(19.9)		(3,041.9)

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

	Unaudited	Year ended 31 March 2018
	Half year ended 30 September 2018	£m
	£m	£m
Cash and cash deposits as above	405.7	585.3
Less : deposits with a maturity of three months or more (restricted funds)	(186.0)	(182.3)
	219.7	403.0

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

PENNON GROUP PLC
Notes to the condensed half year financial information (continued)
15. Fair value disclosure for financial instruments
Fair value of financial instruments carried at amortised cost

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

	Unaudited		Year ended	
	Half year ended 30 September 2018		31 March 2018	
	Book value	Fair value	Book value	Fair value
	£m	£m	£m	£m
Non-current borrowings :				
Bank and other loans	1,556.3	1,701.3	1,408.8	1,578.1
Other non-current borrowings	277.9	239.7	291.4	251.5
Finance lease obligations	1,504.0	1,364.4	1,476.8	1,350.0
Total non-current borrowings	3,338.2	3,305.4	3,177.0	3,179.6
Other non-current assets	266.2	286.8	263.5	294.7

Valuation hierarchy of financial instruments carried at fair value

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

- quoted prices (unadjusted) in active markets for identical assets or liabilities (level 1)
- inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices) (level 2).

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

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

	Unaudited	
	Half year ended 30 September 2018 £m	Year ended 31 March 2018 £m
Level 2 inputs		
Assets		
Derivatives used for hedging	12.4	11.1
Derivatives deemed held for trading	57.7	72.3
Total assets	70.1	83.4
Liabilities		
Derivatives used for hedging	14.1	16.7
Derivatives deemed held for trading	-	0.9
Total liabilities	14.1	17.6

PENNON GROUP PLC
Notes to the condensed half year financial information (continued)
16. Retirement benefit obligations
Defined benefit schemes

The principal actuarial assumptions were: the rate used to discount schemes' liabilities and expected return on scheme assets of 2.85% (March 2018 2.70%) and the inflation assumption of 3.25% (March 2018 3.15%).

	<u>Unaudited</u>			<u>Year ended</u>		
	Half year ended 30 September 2018			31 March 2018		
	Present value of obligation	Fair value of plan assets	Total	Present value of obligation	Fair value of plan assets	Total
	£m	£m	£m	£m	£m	£m
At 1 April	(948.0)	898.5	(49.5)	(971.4)	903.4	(68.0)
Amounts recognised in the income statement	(18.2)	10.9	(7.3)	(38.7)	22.5	(16.2)
Remeasurements through other comprehensive income	4.7	2.9	7.6	30.2	(5.7)	24.5
Contributions	17.3	(12.9)	4.4	31.9	(21.7)	10.2
	(944.2)	899.4	(44.8)	(948.0)	898.5	(49.5)

17. Capital expenditure

	<u>Unaudited</u>	<u>Year ended</u>
	Half year ended 30 September 2018 £m	31 March 2018 £m
Property, plant and equipment		
Additions	192.6	389.0
Net book value of disposals	0.4	1.5
Capital commitments		
Contracted but not provided	244.0	287.7

18. Trade and other payables & other non-current liabilities

	<u>Unaudited</u>	<u>Year ended</u>
	Half year ended 30 September 2018 £m	31 March 2018 £m
Trade and other payables - current		
Trade payables	114.9	98.2
Amounts owed to joint ventures	3.7	3.7
Other tax and social security	38.2	48.4
Accruals and other payables	154.3	191.7
	311.1	342.0
Other non-current liabilities		
Deferred income	123.5	118.5
Other payables	24.5	21.6
	148.0	140.1

PENNON GROUP PLC
Notes to the condensed half year financial information (continued)
19. Contingencies
Contingent liabilities

	Unaudited	
	Half year ended 30 September 2018 £m	Year ended 31 March 2018 £m
Performance bonds	215.7	185.1

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

Other contractual and litigation uncertainties

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.

Contingent assets

In addition to contractual recoveries related to our construction contracts in respect of Glasgow Recycling and Renewable Energy Centre that are reflected in the financial statements, there are further possible recoveries that are contingent on events in the future that are not wholly within the Group's control. These contingent assets have not been recognised as at 30 September 2018.

20. Related party transactions

The Group's significant related parties during the period were its joint venture in Lakeside Energy from Waste Holdings Limited and its associate INEOS Runcorn (TPS) Holdings Limited, for which disclosures were made in the Pennon Group plc Annual Report and Accounts for the year ended 31 March 2018.

There were no material changes during the half year to September 2018 in the nature of transactions with these related parties.

21. Accounting policy on revenue recognition

IFRS 15 provides a single, principles based five-step model to be applied to all sales contracts. It is based on the transfer of control of goods and services to customers and replaces the separate models for goods, services and construction contracts previously included in IAS 11 Construction Contracts and IAS 18 Revenue. Under IFRS 15, revenue is recognised at an amount that reflects the consideration to which an entity expects to be entitled in exchange of fulfilling its performance obligations to a customer.

The implementation of the new standard has not had a material effect on the Group's reported revenues, net assets or any specific financial statement line, but the Group has reviewed and amended its accounting policy in line with the concepts and terminology used in the standard. The revised policy is as follows:

Revenue recognition

Group revenue is recognised following delivery of performance obligations and an assessment of when control over the product or service is transferred to the customer. Revenue is only recognised when collection of consideration is highly probable.

Revenue is recognised either when the performance obligation in the contract has been performed ('point in time' recognition) or 'over time' as the performance obligations to the customer are satisfied. For each obligation satisfied over time, the Group applies a revenue recognition method that accurately reflects performance in transferring control of the services to the customer.

Notes to the condensed half year financial information (continued)**21. Accounting Policy on revenue recognition (continued)**

Where a contract with a customer includes more than one performance obligation revenue is allocated to each obligation in proportion to a fair value assessment of the total contract sales value split across the services provided.

At the inception of a contract the total transaction price is estimated, being the fair value to which the Group expects to be entitled under the contract, including any variable consideration. Variable consideration is based on the most likely outcome of the performance obligations.

Revenue excludes value added tax, trade discounts and revenue arising from transactions between Group companies. Revenue includes landfill tax.

Water (domestic and non-household retail)

For most of the services provided to domestic customers, contract terms are implied through statute and regulation in the absence of formal, written contracts. South West Water has a duty under legislation to provide domestic customers with services regardless of payment and is not permitted to disconnect domestic customers for non-payment of bills. Charges are set via the periodic review price-setting process, regulated by Ofwat.

In respect of ongoing, continuous services to customers, such as the provision of drinking water and waste water services, revenue is recognised over time in line with customer usage of those services.

Customers with an unmeasured supply are billed at the start of the year for the full amount of the annual charge but typically take advantage of a choice of payment arrangements to pay by regular instalments.

Customers with a metered supply are sent up to four bills per year, based either on actual meter readings or estimated usage. For these customers, revenue includes an estimation of the amount of unbilled usage at the period end. Payment options for domestic customers include an annual Meter Payment Plan where customers agree to pay a fixed amount per month which is adjusted to reflect actual consumption at the end of the year.

A range of regulated services is offered to property developers and owners who require connection to the water and sewerage networks or need the networks to be extended or altered. Typically, these customers pay an estimate of the charges in advance as a deposit, which is treated as a contract liability and are billed or refunded the difference between the estimate and actual costs on completion of the work.

Where the performance obligation relates solely to a connection to the network, revenue is recognised at the point of connection when the customer is deemed to obtain control.

Where assets are constructed or provided by the Group or assets transferred to the Group, it is considered that there is an explicit or implied performance obligation to provide an ongoing water and / or waste water service, with the result that revenue is recognised over a time no longer than the economic life of assets provided by or transferred to the Group.

Pennon Water Services provides specialist retail water and waste water services to business customers. It raises bills and recognises revenue in accordance with its contracts with customers and in line with the limits established for the non-household periodic price-setting process where applicable.

PENNON GROUP PLC**Notes to the condensed half year financial information (continued)****21. Accounting Policy on revenue recognition (continued)***Energy sales*

The Group receives revenue from the sale of electricity from generating assets. These assets include solar, anaerobic digestion, gas from landfill and Energy Recovery facilities. Revenue from the sale of electricity from the Group's generating assets is measured based upon metered output delivered at rates specified under contract terms or prevailing market rates. Revenue is recognised at a 'point in time', being the point of distribution to the grid. Typically, invoices are raised monthly with standard payment terms.

Waste Management Services

In respect of single services with fixed fees, such as the receipt of gate and collection fees, revenue is recognised at the time the service is provided.

The Group also delivers other waste management services for which revenue is recognised 'over time' in accordance with contracts with customers. The nature of contracts and/or performance obligations includes management fees to operate local authority recycling centres and energy recovery facilities, multi service contracts including collections and gate fees.

Revenue from other services can be fixed (i.e. management fees) or variable (i.e. gate fees).

Gate fee revenue, derived from the Group's operational assets, is recognised as customer waste is deposited and is based on tonnage received.

In respect of waste collection services, revenue is recognised at the point of collection from customer premises.

A majority of waste management customers are invoiced monthly for services provided within the monthly billing period. Payments are made on an end of month following invoice basis. Alternative billing and/or payment terms are agreed in exceptional circumstances.

The Group transfers control of such waste management services prior to invoicing. Receipt of payment following invoice is based solely on the passage of time. A trade receivable is recognised until payment is made and/or refund issued.

Where the Group has entered into service concession arrangements it accounts for these contracts in accordance with IFRIC12. Consideration is treated as contract assets or other intangible assets, depending upon the right to receive cash from the asset. Consideration is split between construction of assets, operation of the service and provision of finance recognised as interest receivable.

Revenue in respect of construction services is recognised over time and is based on the fair value of work performed, with reference to the total sales value and the stage of completion of those services, as this best reflects the manner in which control passes to the customer. In accordance with IFRIC 12 an amount equal to the revenue recognised is split between costs recoverable from construction activities disclosed within other intangible assets when the concession grantor has not provided a contractual guarantee in respect of the recoverable amount regardless of the service use by customers, and/or within other non-current assets when the concession grantor contractually guarantees the payment of amounts determined in the contract or the shortfall, if any, between amounts received from users of the public service and amounts specified or determined in the contract. No payments are received during construction.

In respect of operating services, revenue is recognised over time in line with delivery of operational services in accordance with the contract with the local authority.

PENNON GROUP PLC**Notes to the condensed half year financial information (continued)****21. Accounting Policy on revenue recognition (continued)**

Once the operational phase commences the Group has a right to receive consideration for the construction and operational services delivered. Invoicing occurs monthly and payments are due by the end of the month following date of invoice.

Recyclate

The Group transforms waste into recyclate ready for resale. Revenue is measured at the agreed transaction price per tonne of recyclate under the contract with the customer. Revenue recognition occurs when control over the recyclate assets has been transferred to the customer.

In respect of UK sales, the Group's performance obligation is satisfied at the point of collection by the customer. This is the point in time when an invoice is issued and revenue is recognised. Payment terms are typically end of month following invoice date. Overseas sales are predominantly agreed under a letter of credit. Goods are despatched at the point the letter of credit is accepted by the customer's bank. Payment is released when the customer confirms satisfactory receipt of the recyclate. This is the point legal title (i.e. control) passes to the customer and revenue is recognised.

22. Post balance sheet events

On 26 October 2018, the High Court of Justice of England and Wales issued a judgement in a claim between Lloyds Banking Group Pension Trustees Limited (claimant) and Lloyds Bank plc and others (defendants) regarding the rights of female members of certain pension schemes to equality of treatment in relation to pension benefits (GMP equalisation). The judgement concluded that the claimant is under a duty to amend the schemes in order to equalise benefits for men and women in relation to guaranteed minimum pension benefits.

The judgement also provided comments on the method to be adopted in order to equalise benefits, on the period during which a member can claim in respect of previously underpaid benefits, and on what should be done in relation to benefits that have been transferred into, and out of, the relevant schemes. The issues determined by the judgement arise in relation to many other occupational pension schemes. The extent to which the judgement will increase the liabilities of the Group's defined benefit pension schemes is under consideration. The Group expect to recognise a past service cost amount in the income statement in the range of £2-4m in the second half of 2018/19, following a detailed assessment of the GMP equalisation impact.

On 16 November 2018, Viridor Waste Management Limited exercised its pre-emption rights to acquire John Laing Investments Limited's 37.5% economic interest and 20% voting rights in INEOS Runcorn (TPS) Holdings Limited for a cash consideration of £54.52m, following a decision by John Laing to sell its holding in the joint venture.

The acquisition will increase Viridor's economic interest in INEOS Runcorn (TPS) Holdings from 37.5% to 75%, with the associated voting rights moving from 20% to 40%.

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Registered in England No 2366640

PENNON GROUP PLC**DIRECTORS' RESPONSIBILITIES STATEMENT**

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

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

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

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

For and on behalf of the Board of Directors who approved this half year report on 26 November 2018.

C Loughlin
Group Chief Executive Officer

S J Davy
Chief Financial Officer

INDEPENDENT REVIEW REPORT TO PENNON GROUP PLC

Introduction

We have been engaged by the Company to review the condensed consolidated set of financial statements in the half-yearly financial report for the six months ended 30 September 2018 which comprises the Consolidated income statement, the Consolidated statement of comprehensive income, the Consolidated balance sheet, the Consolidated statement of changes in equity, the Consolidated statement of cash flows and related notes. We have read the other information contained in the half yearly financial report and considered whether it contains any apparent misstatements or material inconsistencies with the information in the condensed set of financial statements.

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

Directors' Responsibilities

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

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

Our Responsibility

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

Scope of Review

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

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the condensed consolidated set of financial statements in the half-yearly financial report for the six months ended 30 September 2018 is not prepared, in all material respects, in accordance with International Accounting Standard 34 as adopted by the European Union and the Disclosure and Transparency Rules of the United Kingdom's Financial Conduct Authority.

Ernst & Young LLP
Reading
26 November 2018