



**Pennon Group Plc**

**Preliminary Results  
2003/04**

27 May 2004

**Pennon Group Plc**  
*2003/04 Financial Highlights*

- Operating profit up 7.3% to £136.3m<sup>(1)</sup>
  - South West Water up 6.6% to £118.9m
  - Viridor up 18.8% to £22.7m (before goodwill)
- Profit before tax up 6.2% to £78.8m<sup>(1)</sup>
- Earnings per share (before deferred tax) up 4.9% to 57.7p<sup>(1)</sup>
- Recommended final dividend per share up 4.9% to 27.8p (full year dividend up 4.9% to 41.0p)

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<sup>(1)</sup> Before exceptional item in 2003/04 of £6.5m re abortive acquisition costs

## **Pennon Group Plc**

### *Operational Highlights*

- South West Water
  - On track to outperform the current regulatory contract
  - Final 2005 - 2010 Business Plan submitted to Ofwat
- Viridor Waste
  - Strong growth in profits from landfill and power generation
  - Acquisitions performing in line with expectations

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## **Pennon Group Plc**

### **Shanks**

- Acquisition would have tied in very well with Viridor strategy
- Our offer price of £202.5m satisfied our investment criteria
  - IRR/NPV
  - earnings enhancement
  - reinforcement of progressive dividend policy
- Terra Firma prepared to pay a substantially higher price (£227.5m)
  - price would not have satisfied Pennon's investment criteria
- Our track record proves there are acquisitions available which do meet our investment criteria

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## **Pennon Group Plc Terra Firma**

- Pennon recently received an unsolicited, indicative, non-binding approach from a consortium of financial investors led by Terra Firma, at an effective value of 822 pence per share for each issued ordinary share of the Company (the “Approach”)
  - Pennon shareholders would have received a cash payment of 850p per share but would have foregone the final dividend of 27.8 pence for the year ended 31 March 2004
- Preliminary and contingent approach from a consortium of two financial investors
  - subject to further extensive due diligence
  - execution risk given complex transaction structure
  - competition risk
- The Board unanimously rejected the Approach as it failed to recognise the strategic value of Pennon, its track record and its future prospects
- Shareholders approached endorsed board decision



## Pennon Group Plc

### Summary Financial Results

	2003/04 £m	2002/03 £m	Change
Group turnover	471.3	417.2	13.0%
Group operating profit after goodwill <sup>(1)</sup>	136.3	127.0	7.3%
Group profit before tax <sup>(1)</sup>	78.8	74.2	6.2%

- c£2.0m interest received from Viridor Instrumentation sale proceeds in 2002/03

<sup>(1)</sup> Before exceptional item in 2003/04 of £6.5m re abortive acquisition costs – note further £2.5m to be charged in 2004/05

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## Pennon Group Plc

### Cash Flow

	2003/04 £m	2002/03 £m
Cash inflow from operations	215.1	198.9
Net interest paid	(41.3)	(42.9)
Dividends and tax paid	(47.1)	(147.3)
Capital expenditure	(179.2)	(198.2)
Acquisitions	(20.0)	(37.2)
Net cash outflow	(72.5)	(226.7)
Shares issued for cash	2.1	1.1
Non-cash movements	(15.1)	(11.7)
Increase in net debt	(85.5)	(237.3)

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## Pennon Group Plc

### *Net Debt*

As at 31 March

	2004 £m	2003 £m
Loans and finance leases		
- over one year	1,234.8	1,083.2
- under one year	107.0	96.4
	1,341.8	1,179.6
Less: investments and cash	(267.7)	(191.0)
Net debt	1,074.1	988.6
Net gearing	119%	111%

- Significant drawdowns from EIB and other loans of £140m and finance leases of £36m

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### *Net Interest Payable*

	2003/04 £m	2002/03 £m
Interest payable	(66.6)	(62.1)
Interest receivable	9.4	10.0
Net interest payable	(57.2)	(52.1)
Average rate of interest	5.5%	6.0%
Net interest cover <sup>(1)</sup>	2.4x	2.4x

- 2002/03 included c.£2m interest receivable on sale proceeds from Viridor Instrumentation

<sup>(1)</sup> Before exceptional item in 2003/04 of £6.5m re abortive acquisition costs

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## Pennon Group Plc

### *Financing Initiatives*

- Funding requirements for the K3 period fully sourced
- Funding strategy uses mix of fixed and floating rate borrowings
- Interest rate swaps on majority of debt up to 2005
- Locks-in benefit of current low interest rates compared to Ofwat assumptions

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### *Depreciation*

	2003/04 £m	2002/03 £m
South West Water		
- infrastructure assets	14.2	13.9
- other assets	48.6	45.2
	<u>62.8</u>	<u>59.1</u>
Viridor	20.5	18.8
Other	(0.1)	(0.1)
	<u>83.2</u>	<u>77.8</u>

## Pennon Group Plc

### *Taxation*

	2003/04 £m	2002/03 £m
UK corporation tax	7.5	3.4
Deferred tax	3.3	13.7
	<u>10.8</u>	<u>17.1</u>

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

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### *Pensions*

- Indicative net deficit of c£55m at 31 March 2004, similar to 31 March 2003
- Represents c.6% market capitalisation
- Employer contributions increased from 4.8% to 11.5% from 1 April 2003
- Defined contribution pension scheme for new entrants to Viridor introduced July 2003
- Triennial actuarial valuation process commenced April 2004, expected to add up to £6m costs p.a.

## Pennon Group Plc

### *Key Financial Ratios*

	2003/04	2002/03
Dividend cover <sup>(1)</sup>	1.4 times	1.5 times
Net interest cover <sup>(1)</sup>	2.4 times	2.4 times
Net gearing	119%	111%

<sup>(1)</sup> Before exceptional item, special dividend and deferred tax

## Pennon Group Plc

### *Dividends*

- Progressive dividend policy
- Interim dividend per share increased by 4.8% to 13.2p
- Recommended final dividend up 4.9% to 27.8p
- Full year dividend up 4.9% to 41.0p
- Scrip dividend alternative





## **South West Water**

### *Financial Performance Summary*

	2003/04 £m	2002/03 £m	Change
Turnover	291.8	270.2	8.0%
Operating profit	118.9	111.5	6.6%

## South West Water *Turnover*

- Increase of £21.6m (8.0%) in year
- Reflects impact of

	£m
- tariff increase	19.5
- meter option switchers	(6.0)
- new connections	2.1
- measured demand (Summer 2003)	3.0
- other – commercial and service sales	3.0
	21.6

- Number of meter switchers 30,900
- Number of new customers 6,900

## South West Water *Operating Costs*

	2003/04 £m	2002/03 £m	Change
Total operating costs	172.9	158.7	8.9%
Less depreciation charges	(62.8)	(59.1)	6.3%
Operating costs before depreciation	110.1	99.6	10.5%

Increase in total operating costs due to:

	£m
- inflation	3.4
- new works (including depreciation)	8.6
- other (pensions, cost of sales, bad debts)	6.3
- efficiency savings	(4.1)
	14.2

## South West Water

### *Analysis of Efficiency Savings*

	£m
• Manpower/overheads	1.2
• Supply chain/contracted services	1.9
• Power costs	0.5
• Other	0.5
	<hr/>
	4.1
	<hr/>

- Cumulative K3 savings of £18.4m (£46.0m since 1995)

## South West Water

### *Operational Performance Summary*

- Highest ever drinking water quality
- Original “Clean Sweep” programme now complete
  - bathing water compliance at all time high in South West
    - Devon 100% compliant
  - 115 of 141 of region’s bathing waters to guideline standards
- Highest percentage length of high quality river in England
- An industry leader in managing leakage and security of supply
- Continued progress on service standards requiring capital investment
- Significant improvement in OPA score expected
- Continued good performance on customer “Levels of Service Indicators”

## South West Water

### *Capital Programme*

- Regulatory Contract K3:
  - Ofwat provision £725m (May 1999 prices)
  - targeting outperformance of 10%
  - on track to achieve
- Reduced capex 2003/04 - £139m (2002/03 - £182m)
- Over 400km water mains laid, replaced or refurbished
- Investment to improve waste water compliance – OPA
- Completion of original “Clean Sweep” programme - Torbay

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## South West Water

### *Regulatory Asset Value*

	Year end	2003	2004	2005
		£m	£m	£m
At 2002/03 prices <sup>(1)</sup>		1620	1706	1784
Actual/Predicted Outturn prices including COPI indexation <sup>(2)</sup>		1642	1770	1896

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

<sup>(1)</sup> Source: Ofwat

<sup>(2)</sup> Source: South West Water

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## South West Water

### *PR04 Final Business Plan*

- Overall 17% higher capex than AMP3
- A reduced waste water environmental improvement programme
- A bigger water mains rehabilitation programme to meet DWI requirements by 2010
- Increased levels of capital maintenance expenditure
- Asset investment to meet demand growth including 2 new towns
- Meeting customer concerns through targeted programmes to deal with odours at sewage treatment works and sewage flooding
- Higher running costs, including EA charges, business rates, insurance, pensions, climate change levy and corporate tax changes

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## South West Water

### *Debt to RAV*

Year	South West Water Final Business Plan
2003/04	54.3%
2009/10	59.4%

- On this basis no additional equity required to fund South West Water capital programme

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## South West Water *Looking Towards PR04*

- *October 2002*      *Ofwat framework document*
- *January 2003*      *Initial ministerial guidance*
- *August 2003*      *Draft Business Plan*
- *October 2003*      *Ofwat response to Draft Business Plans*
- *March 2004*      *Final ministerial guidance*
- *April 2004*      *Final Business Plan*
- *5 August 2004*      *Draft Determination*
- *Sept/Oct 2004*      *Stakeholder response to Draft Determination*
- *2 December 2004*      *Final Determination*
- *April 2005*      *New price limits apply*

**Viridor**  
WASTE

## Viridor

### *Delivering Strong Financial Performance*

Year Ended 31 March

	2001 £m	2002 £m	2003 £m	2004 <sup>(1)</sup> £m
Turnover <sup>2</sup>	106.1	125.3	152.3	183.1
EBITDA	28.8	32.1	38.2	43.2
Operating profit				
- before goodwill	13.1	15.2	19.1	22.7
- after goodwill	13.1	14.9	17.6	20.2
Operating margin (before goodwill and excluding landfill tax)	17.7%	17.3%	17.4%	16.9%

- Strong growth in Turnover, EBITDA and Operating Profit
- Consistent strong margin

<sup>(1)</sup> As per unaudited preliminary results  
<sup>(2)</sup> Including landfill tax

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## Viridor

### *2003/04 Financial Highlights*

- At beginning of year projected moderate growth in operating profit before goodwill
  - after strong growth in each of the previous 2 years
- Turnover up £30.8m (£25.0m excluding landfill tax)
- EBITDA up 13.1% to £43.2m
- Operating profit before goodwill up 18.8%
  - landfill contribution up 23% (2002/03 – 25%) <sup>(1)</sup>
  - power generation contribution up 46% (2002/03 – 88%)<sup>(2)</sup>
- Operating margin 16.9% (2002/03 – 17.4%)
- Capex £30.5m (2002/03 £23.0m)

<sup>(1)</sup> Includes acquisitions

<sup>(2)</sup> Includes effect of 2002/03 introduction of ROCs

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## **Viridor**

### ***Operational and Business Highlights - Landfill***

- Landfill volumes increased by 6.3% (primarily full year effect of Parkwood) to 3.7m tonnes
- Gate fees increased by 3.5%
  - ahead of cost increases
- Increased landfill asset base (83m cubic metres consented capacity, up 3m from last year end) <sup>(1)</sup>
  - acquisitions 4m
  - planning gains 3m
  - usage (4m)

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<sup>(1)</sup> Includes landfill void gained with Thames Waste acquisition

## **Viridor**

### ***Operational & Business Highlights – Power Generation***

- 272,400 MWH generated 2003/04
  - average price: £50.25 per MWH
- Power generation capacity increased by 22% to 45 MW <sup>(1)</sup>
  - on top of 32% increase in 2002/03
  - benefiting from Renewables Obligations Certificates (ROCs)
  - Government target of 10% of electricity from renewables by 2010 and 15% by 2015 and aspiration of 20% by 2020 vs. under 4% at present

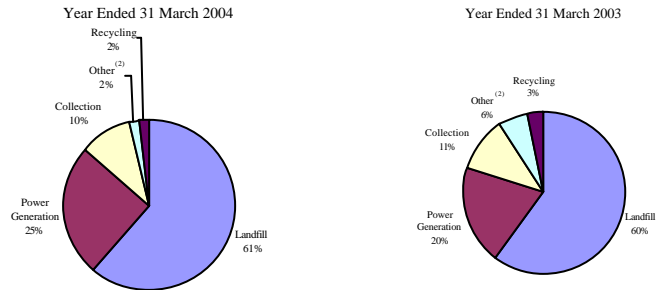
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<sup>(1)</sup> Includes power generation gained with Thames Waste acquisition



# Viridor

## Profit Contribution by Segment <sup>(1)</sup>



<sup>(1)</sup> Contribution before goodwill and central overheads

<sup>(2)</sup> Other includes clinical, minerals and civic amenity contracts

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# Viridor

## Operational and Business Highlights - Acquisitions

- 2002/03 acquisitions earnings enhancing pre-goodwill in line with expectations
- Churrgold Holdings Limited acquired June 2003 for £19.8m
  - already earnings enhancing pre-goodwill
- Thames Waste Management Limited acquired April 2004 for £30.5m
  - EBITDA £7.8m
- 25 year PFI contract with West Sussex County Council commenced April 2004
- New regional management structure

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## **Viridor**

### ***Delivering Value in the Waste Sector***

- A leading waste management company in the UK
- Strategy
  - capitalise on leading position in landfill disposal
  - exploit opportunities in renewable energy generation
  - pursue profitable opportunities arising from Government's developing waste strategy
- Proven track record of delivering growth
  - 20% p.a. growth in operating profit before goodwill (2001-04)
  - organic profit growth of around 10% p.a. driven by increasing landfill volumes, rising gate fees and significantly increased contribution from renewable energy
- Active participant in consolidation of UK waste sector
  - 7 acquisitions for c.£104m since 2001 (including Thames Waste Management, acquired in April 2004)
  - substantially integrated (apart from TWM) and delivering expected returns

# **Pennon Group Plc**

## *Summary*

- Strategy clearly focused on water, sewerage and waste management
- South West Water remains confident of outperforming the Regulatory Contract to 2005
  - strong growth in RAV up to 2005, outstripping anticipated growth in net debt
  - planning for the K4 period
- Viridor delivering strong growth by
  - capitalising on landfill asset base
  - exploiting landfill gas power generation opportunities
  - continuing to pursue profitable opportunities in line with the Government's developing waste strategy
  - pursuing selective acquisitions

