

# Preliminary Results 2004/05

26 MAY 2005

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# Pennon Group Plc

## 2004/05 Financial Highlights

- Operating profit before goodwill up 9.1% to £151.5m <sup>(1)</sup>
  - South West Water up 2.4% to £121.7m
  - Viridor Waste up 31.3% to £29.8m
- Profit before tax up 10.9% to £87.4m <sup>(1)</sup>
- Earnings per share (before deferred tax) up 9.4% to 63.1p <sup>(1)</sup>
- Recommended final dividend per share up 5.0% to 29.2p (full year dividend up 4.9% to 43.0p)

<sup>(1)</sup> Before net exceptional items in 2004/05 of £0.1m (income of £5.0m less costs of £4.9m; 2003/04 – cost £6.5m)

# Pennon Group Plc

## *2004/05 Operational Highlights*

- South West Water
  - Successful delivery of K3 regulatory contract
  - Strong growth in K3 RAV outstripped growth in net debt
  - Delivery under way of K4 regulatory contract
- Viridor Waste
  - Continued strong growth in profits from landfill and power generation
  - Recent acquisitions successfully integrated and performing ahead of expectations
  - West Sussex PFI successful first year



**Pennon Group Plc**

# Pennon Group Plc

## Summary Financial Results

	2004/05 £m	2003/04 £m	Change
Group turnover	554.2	471.3	17.6%
Group operating profit before goodwill <sup>(1)</sup>	151.5	138.8	9.1%
Group profit before tax <sup>(1)</sup>	87.4	78.8	10.9%

<sup>(1)</sup> Before net exceptional items in 2004/05 of £0.1m, comprising:

- £5.0m proceeds from a disposal in 1998 (2003/04 – nil); less
- £1.5m abortive acquisition costs (2003/04 – £6.5m)
- £3.4m restructuring costs in SWW (2003/04 – nil)

# Pennon Group Plc

## Cash Flow

	2004/05 £m	2003/04 £m
Cash inflow from operations	255.3	215.1
Net interest paid	(59.1)	(41.3)
Dividends and tax paid	(28.7)	(47.1)
Capital expenditure	(174.7)	(178.6)
Acquisitions	(28.6)	(20.0)
Net cash outflow	<u>(35.8)</u>	<u>(71.9)</u>
Shares issued for cash	0.8	2.1
Own shares purchased	-	(0.6)
Non-cash movements	(9.7)	(15.1)
Increase in net debt	<u><u>(44.7)</u></u>	<u><u>(85.5)</u></u>

- **Modest increase in net debt - £44.7m**
- **Scrip dividend take up**

# Pennon Group Plc

## Net Debt

As at 31 March

	2005 £m	2004 £m
Loans and finance leases		
- over one year	1,366.8	1,234.8
- under one year	54.8	107.0
	<hr/>	<hr/>
	1,421.6	1,341.8
<u>Less:</u> investments and cash	(302.8)	(267.7)
Net debt	<hr/>	<hr/>
	1,118.8	1,074.1

Net gearing

119%

119%

- **Significant drawdowns of bilateral loans of net £20m and finance leases of net £52m**
- **£105m existing bilaterals refinanced**
- **Gearing stable**

## Pennon Group Plc

### Net Interest Payable

	2004/05 £m	2003/04 £m
Interest payable	(74.0)	(66.6)
Interest receivable	13.3	9.4
Net interest payable	<u>(60.7)</u>	<u>(57.2)</u>
Average rate of interest	5.5%	5.5%
Net interest cover <sup>(1)</sup>	2.4x	2.4x

- **Average interest rate unchanged – benefit of swaps strategy**

<sup>(1)</sup> Before exceptional items



# Pennon Group Plc

## *Financing Initiatives*

- Funding strategy uses mix of fixed and floating rate borrowings
- Locks-in benefit of low interest rates compared to Ofwat assumptions
- 75% of SWW debt fixed to March 2006
- 50% of SWW debt fixed to March 2010
- Recently signed £70m facility with EIB on a sub-libor basis
- Committed funding in place for SWW up to March 2007

# Pennon Group Plc

## Depreciation

	2004/05 £m	2003/04 £m
South West Water		
- infrastructure assets	14.9	14.2
- other assets	51.2	48.6
	<u>66.1</u>	<u>62.8</u>
Viridor	26.2	20.5
Other	0.1	(0.1)
	<u>92.4</u>	<u>83.2</u>

## Pennon Group Plc

### Taxation

	2004/05 £m	2003/04 £m
UK corporation tax	7.9	7.5
Deferred tax	10.8	3.3
	<u>18.7</u>	<u>10.8</u>

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

# Pennon Group Plc

## Taxation

	2004/05 £m	2003/04 £m
Corporation tax		
Current year	13.1	12.8
Prior year	(5.2)	(5.3)
	<u>7.9</u>	<u>7.5</u>
Deferred tax (undiscounted)	<u>18.4</u>	<u>16.2</u>
PBT (post exceptionals)	<u>87.5</u>	<u>72.3</u>
Effective rate (pre-exceptionals)		
Corporation tax	9.8%	9.5%
Corporation tax & deferred tax	31.7%	30.1%

- **Items impacting 2005/06 tax charge**
  - **Change to tax relief on capitalised revenue expenditure**
  - **Change in focus of capital spend**

# Pennon Group Plc

## *Pensions*

- Indicative net deficit of c £56m at 31 March 2005, similar to 31 March 2004
- Represents c 4.5% market capitalisation
- Triennial actuarial valuation April 2004
  - added c £5.5m costs pa (SSAP 24)

# Pennon Group Plc

## IFRS

- Ongoing preparation for adoption of IFRS in 2005/06
- Significant changes in:
  - deferred tax
  - pensions
  - fixed asset accounting (“renewals”)
  - goodwill
- Overall reduction to net assets and potential increase in reported earnings volatility
- Presentation 28 June at 6pm, London Paddington Hilton
  
- ***Does not affect underlying cashflow***

# Pennon Group Plc

## *Dividends*

- Progressive dividend policy
  - real growth projected up to 2010
- Interim dividend per share increased by 4.5% to 13.8p
- Recommended final dividend up 5.0% to 29.2p
- Full year dividend up 4.9% to 43.0p
- Scrip dividend alternative
- Dividend cover maintained at 1.4x (before exceptional items/deferred tax)



**SOUTH WEST WATER**





## South West Water

### Financial Performance Summary

	2004/05 £m	2003/04 £m	Change
Turnover	309.8	291.8	6.2%
Operating profit <sup>(1)</sup>	121.7	118.9	2.4%

<sup>(1)</sup> Before exceptional restructuring charge of £3.4m in 2004/05

## South West Water

### Turnover

- Increase of £18.0m (6.2%) in year
- Reflects impact of

	£m
- tariff increase	21.2
- meter option switchers	(6.3)
- new connections	2.0
- measured demand (high summer 2003)	(2.4)
- other – commercial and service sales	3.5
	<hr/>
	18.0
	<hr/>

- **Number of meter switchers** **25,500**
- **Number of new customers** **7,300**

# South West Water

## Operating Costs

	2004/05 £m	2003/04 £m	Change
Total operating costs <sup>(1)</sup>	188.1	172.9	8.8%

Increase in total operating costs due to:

	£m
- inflation	4.4
- new works (including depreciation)	5.7
- other (pensions, cost of sales, bad debts)	9.2
- efficiency savings	(4.1)
	<u>15.2</u>

<sup>(1)</sup> Before exceptional restructuring charge of £3.4m in 2004/05

# South West Water

## Analysis of Efficiency Savings

£m

- Manpower/overheads 1.0
- Supply chain/contracted services 2.0
- Energy and rates management 1.0
- Other 0.1

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4.1

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- ***Improved efficiency banding***
- ***Annual savings of £22.5m by end of K3 period***

# South West Water

## *Operational Performance Summary*

- Highest ever drinking water and river water quality
- Remaining UWWTD schemes underway following completion of original “Clean Sweep”
- Leakage management continues on target
- Continued progress on service standards dependent on capital investment
- 45 point OPA improvement in 2003/04 – one of the largest gains in the sector. Further improvement has been achieved 2004/05
- Continued high performance on customer “Levels of Service Indicators”

# South West Water

## Capital Programme

- Capital programme since privatisation totals just over £2bn (over 1,000 schemes): delivered to target and beating budget
- Capital expenditure 2004/05 – £141.9m (2003/04 – £139.3m)
  - £95m Torbay scheme commissioned
  - almost 570km water mains replaced/refurbished (55% higher than 2003/04)
- Regulatory contract K3:
  - Ofwat provision £725m (May 1999 prices)
  - outperformance of 10% targeted and achieved
- Regulatory contract K4:
  - achieving new progressive operating efficiencies
  - building on track record of capital programme delivery inside Ofwat targets

## South West Water

### *Efficiency Challenge – Operating Costs*

- Company wide initiatives
  - Customer Focused Asset Management (CFAM)
  - Integrated Customer and Operational Management (Service +)
- Target efficiency savings: £13m pa off base operating costs by 2010
- Savings breakdown:
  - Manpower
  - Asset planning/management
  - Customer service improvements
  - Engineering services
  - Contract strategy/strategic suppliers
  - Mobile working

All supported by development of IT systems implemented during K3 period.

# South West Water

## *Efficiency Challenge - Capital*

Capital Programme: £762m at 2002/03 prices

- Organisational focus on asset management
- Manpower
- Process re-engineering
- Further rationalisation/development
- Product innovation
- Benchmarking
- Value engineering
- Overhead cost minimisation
- Standards



## South West Water Regulatory Asset Value

Year end	2005 £m	2006 £m	2007 £m	2008 £m	2009 £m	2010 £m
At 2002/03 prices <sup>(1)</sup>	1847	1929	1994	2042	2095	2136
Actual/Predicted outturn prices <sup>(2)</sup>	1956	2104	2234	2349	2476	2594

- **Strong growth in RAV 2006-10 reaching £2.6bn by March 2010 – highest percentage increase of any quoted water company**

*(1) Source: Ofwat*

*(2) Source: South West Water*



**Viridor**  
WASTE

# Viridor Waste

## Continuing to Deliver Strong Financial Performance

	Year Ended 31 March					CAGR % 2001-05
	2001 £m	2002 £m	2003 £m	2004 £m	2005 £m	
Turnover <sup>(1)</sup>	106.1	125.3	152.3	183.1	248.3	23.7
EBITDA	28.8	32.1	38.2	43.2	56.0	18.1
Operating profit						
- before goodwill	13.1	15.2	19.1	22.7	29.8	22.8
- after goodwill	13.1	14.9	17.6	20.2	26.3	19.0

- **Strong growth in turnover, EBITDA and operating profit**

<sup>(1)</sup> Including landfill tax

# Viridor

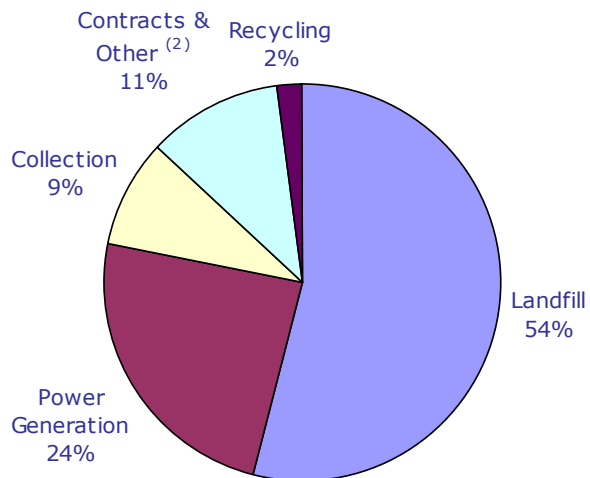
## 2004/05 Financial Highlights

- Turnover up 36% or £65.2m compared to 2003/04
- EBITDA up 30% to £56m
- Operating profit before goodwill up 31% to £29.8m
  - up 11% excluding this year's and full effect of last year's acquisitions and additional pensions charge
  - within underlying businesses landfill, power generation, collection and contracts performed particularly well
- Capex £45.8m (2003/04 £30.5m)

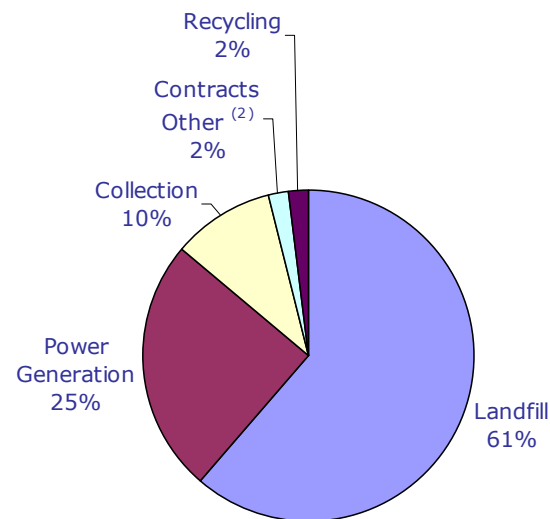
# Viridor Waste

## Profit Contribution by Segment (1)

Year Ended 31 March 2005



Year Ended 31 March 2004



(1) Contribution before goodwill and central overheads

(2) "Contracts" include West Sussex PFI and "Other" includes clinical, minerals and civic amenity contracts

# Viridor

## *Operational and Business Highlights - Landfill*

- Landfill volumes increased by 10% to 4.0m tonnes compared to 2003/04
  - 2% increase excluding acquisitions
  - aided by particularly high inputs preceding the ending of hazardous waste disposal to non-hazardous landfills in July 2004
- Gate fees increased by 10%
  - continuing to outstrip cost increases
- Current landfill capacity 80m m<sup>3</sup> (reflecting planning gains of 3m m<sup>3</sup> and 2004/05 usage of 5m m<sup>3</sup>)
- Not currently pursuing opportunity for dedicated hazardous waste landfill
  - long-term market demand unclear
  - aftercare in perpetuity
  - but six Viridor Waste sites now permitted for stabilised non-reactive hazardous waste or asbestos

# Viridor Waste

## *Operational and Business Highlights – Power Generation*

- Capacity increased by a further 7MW to 52MW
  - compared to 28 MW March 2002
  - additional 3MW under development
- 56% of output under ROCs and 44% under NFFO 3 and 4
  - average price £54/MWH
- Government target of 10% of electricity from renewables by 2010 and 15% by 2015 and aspiration of 20% by 2020 vs under 4% at present

# Viridor Waste

## *Operational and Business Highlights - Developments*

- 25 year £450m PFI contract with West Sussex County Council commenced April 2004
  - profit contribution of £0.9m (slightly ahead of expectations)
- Thames Waste Management Limited acquired April 2004 for £30.8m
  - already earnings enhancing after goodwill and restructuring costs
- Churngold Holdings Limited acquired June 2003 for £19.8m
  - already earnings enhancing after goodwill



# Viridor Waste

## *Municipal Landfill Diversion Targets - I*

- EU Landfill Directive set targets for reduction of biodegradable municipal waste to landfill
  - by 2020 UK must achieve 65% reduction from 1995 levels
- Substantial ongoing landfill market in UK
  - municipal only around one third of landfill total
  - landfill in short supply

# Viridor Waste

## *Municipal Landfill Diversion Targets - II*

- UK Government has allocated landfill allowances to each disposal authority for every year up to 2020
  - penalty if exceed allowance
  - allowances can be traded
- UK as whole will require substantial investment in municipal waste management infrastructure
  - up to £30bn by 2020 according to ICE<sup>(1)</sup>
- To meet these targets councils are starting to let long term (c 25 year) integrated waste contracts, often with PFI funding
  - significant opportunity for established waste companies, subject to careful assessment of the risks

<sup>(1)</sup> *Institution of Civil Engineers*

# Viridor Waste

## *New Technologies*

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

# Viridor Waste

## *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
  - 23% pa growth in operating profit before goodwill (2001-05)
  - organic profit growth of around 12% pa driven by increasing landfill volumes, rising gate fees and significantly increased contribution from renewable energy
- Active participant in consolidation of UK waste sector
- Pursuing integrated waste management contracts



**Pennon Group Plc**

# Pennon Group Plc

## Summary

- Strategy clearly focused on water, sewerage and waste management
- South West Water
  - successful delivery of K3 regulatory contract
  - strong growth in K3 RAV outstripped growth in net debt
  - delivery under way of K4 regulatory contract
  - strong growth in K4 RAV reaching £2.6bn by March 2010
- 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/PFI contracts
- Progressive dividend policy
  - real growth projected up to 2010



**Pennon Group Plc**