PENNON GROUP PLC **1 June 2006**

PRELIMINARY RESULTS FOR THE YEAR ENDED 31 MARCH 2006

Pennon Group announces its unaudited results for the year ended 31 March 2006.

A presentation for City audiences will be held today, 1 June 2006, at 10:30 at The Brewery, Chiswell Street, London, EC1.

FINANCIAL HIGHLIGHTS

- Operating profit up 16.0% to £175.1m. (1)
  - South West Water up 15.8% to £141.5m.
  - Viridor Waste up 19.7% to £35.9m before amortisation of intangibles.
- Profit before tax up 24.6% to £110.9m. (1)
- Earnings per share up 17.4% to 75.5p. (2)
- Return of capital announced December 2005.
  - £200m capital return.
  - £14.5m South West Water customer payment.
- Dividend
  - Recommended final dividend per share up 20.2% to 35.1p.
  - Full year dividend up 20.0% to 51.6p.
  - Dividend policy of 3% per annum real increases until 2009/10
- Proposed 3 for 1 stock split.

(1) Before exceptional items (as detailed in note 4 to the financial statements).

(2) Before exceptional items (as detailed in note 4 to the financial statements) and deferred tax.

OPERATIONAL HIGHLIGHTS

- South West Water :
    - On target to deliver 2005 – 2010 Regulatory Contract.
    - Profit increase reflecting strong growth in Regulatory Capital Value (RCV) in 2005/06.
    - Successful re-focusing of capital programme to mains rehabilitation and asset maintenance.
    - Reservoir water storage of 85%, 3% above last year.
    - No restrictions envisaged.

- Viridor Waste :
    - Continued strong growth in profits from landfill, power generation and contracts.
    - Brett Waste Management Limited acquired June 2005 – successfully integrated and earnings enhancing in its first year.
    - Lakeside energy from waste plant joint venture signed September 2005 – now fully financed and under construction.
    - Since the year end, Wyvern Waste Services Limited acquired for £25m and long-term waste management PPP contract signed with Somerset County Council.

The Chairman, Ken Harvey, said, " Once again I am pleased to report excellent results for Pennon which clearly affirm our strategy of focusing on our two key businesses, South West Water and Viridor Waste. The Board announced last December its decision to increase the level of gearing in South West Water to increase the efficiency of the Group's capital structure. As a consequence, £145m has been returned to shareholders via a B Share scheme and £55m is to be returned via a share buyback. In addition, £14.5m has been paid to South West Water customers as a payment of £20 per customer. Viridor Waste continues to deliver a very strong performance based on both organic growth and acquisitions as a result of its successful focused strategy.

"Pennon's Board proposes, subject to shareholder approval at the forthcoming AGM, to effect a 3 for 1 share split to increase the liquidity and marketability of the Company’s shares.”

For further information today, 1 June 2006, please contact :

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ADOPTION OF INTERNATIONAL FINANCIAL REPORTING STANDARDS

All numbers contained herein are published in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union with prior year figures restated.

Full information relating to the restatement from UK GAAP to IFRS was published on 8 December 2005, principally comprising the consolidated balance sheet at 1 April 2004, half year results to 30 September 2004 and the full year results to 31 March 2005. Details of these results, together with reconciliations between previously published UK GAAP reported results and those reported under IFRS, are available on the Group's website www.pennon-group.co.uk.

GROUP OVERVIEW

- Revenue rose by 17.1% to £645.7m.

- Operating profit before exceptional items rose by 16.0% to £175.1m.

- Profit before tax was up 24.6% to £110.9m *

- Earnings per share from continuing operations before exceptional items and deferred tax increased by 17.4% from 64.3p to 75.5p. Earnings per share from continuing operations after exceptional items and deferred tax fell from 48.1p to 29.7p.

- Capital expenditure was £249.7m (2004/05 – £181.0m).

  * Before net exceptional costs totalling £56.8m in 2005/06 and £4.9m in 2004/05 as detailed in note 4 to the financial statements.

- Net borrowings at 31 March 2006 were £1,427m, an increase of £309m since 31 March 2005. Gearing, being net borrowings to shareholders' funds plus net borrowings, was 71% (2004/05 – 61%). Interest cover was 2.7 times (2004/05 - 2.4 times). South West Water net debt to RCV was 62.5% (2005 – 52.4%).

- The Board has recommended a final dividend of 35.1p, up 20.2%, subject to shareholder approval. Together with the interim dividend of 16.5p, this will result in a total dividend for the year of 51.6p, an increase of 20.0% on the total dividend for 2004/05. As confirmed at the time of the Group's interim results last December, the Board's policy is to grow the Group dividend by 3% above inflation per annum thereafter up to 2009/10. Shareholders will also be given the opportunity to participate in a Dividend Re-Investment Plan, details of which will be circulated in August.

- The Board proposes, subject to shareholder approval at the forthcoming AGM, to effect a stock split of 3:1 in Pennon's share capital in order to increase the liquidity of its shares. Further details will be circulated with the Annual Report.

STRATEGY

The Board's priority continues to be the creation of shareholder value through its strategic focus on water, sewerage and waste management. The preliminary results announced above are testament to the Board's strategy of focusing on these key business areas. The move to a more highly geared structure has allowed the Group to return value to shareholders and customers and provide an enhanced dividend.

SOUTH WEST WATER

South West Water revenue rose by £41.5m to £348.5m. Approved tariff increases, including the 12.5% K factor, amounted to £49.5m. 7,400 new customer connections contributed £2.8m. Customers switching from unmeasured to metered charging caused a reduction of £7.9m in turnover. Over 50% of South West Water's domestic customers are now metered. Other factors, including a small decrease in measured demand, reduced turnover by £2.9m.

South West Water's operating profit rose 15.8% to £141.5m, before exceptional costs of £14.5m from the customer payment (2004/05 exceptional restructuring costs of £3.4m). Operating costs, including depreciation, increased by £22.2m to £207.0m. Additional costs from new capital schemes of £7.7m, inflation of £8.4m (including energy and chemicals), and other cost increases of £10.1m (including depreciation increases and direct charging of a proportion of leakage expenditure to operating cost), were offset by £4.0m of efficiency savings. Detailed plans are in place and the company is on track to achieve the operating cost efficiency targets set by the Director General of Water Services for the period up to 2010.

In 2005/06 two of our key reservoirs were replenished by pumping water from downstream river flows to supplement the natural rain water inflow. The pump infrastructure was installed several years ago to provide enhanced drought protection. This contributed to current reservoir water levels in the region of 85%, 3% above last year. Ofwat's latest report on leakage confirms that South West Water remains one of the leading companies in managing water leakage and continues to deliver results in line with Ofwat's leakage target.

During the year, the company completed the majority of the 'Early Start' schemes agreed with Ofwat during the last Price Review, numbering around 45 in total and at a cost of some £20m. The programme is on track with the remaining schemes due to be completed in 2006/07.

Capital expenditure increased by 42.0% to £191.0m. £109.4m was invested in water supply improvements including water mains renovation, water treatment works enhancement and leakage control. A record length of 695km of water mains were laid, replaced or refurbished during the year, in line with the Drinking Water Inspectorate's (DWI) agreed programme for completion by 2010. Drinking water quality and river water quality are at an all time high and the region features the highest proportion of high quality rivers in England. Ofwat's Levels of Service Report showed that in 2004/05 South West Water achieved the largest Overall Performance Assessment score improvement, resulting in 6th position out of 10 water and sewerage companies, as it has become possible to redirect capital expenditure from the coastal clean-up programme to other areas of the business. This included an increase in the

Operational Performance Index (OPI) score used by the DWI to assess drinking water quality which has benefited from the water mains rehabilitation investment in recent years.

All of the major projects in the Company's 15 year original "Clean Sweep" coastal sewage treatment programme have been completed and the region is now attaining record levels of bathing water quality compliance. In the South West Water region last summer, 142 of the 143 designated bathing waters met the mandatory EU quality standards, with 88.8% meeting the substantially more stringent guideline level. Cornwall's bathing waters achieved an exceptionally high standard, with a 100% pass rate at mandatory level and a 96.4% pass rate at the guideline level.

Regulatory Capital Value (RCV) is expected to grow by 31% over the K4 period to £2.6bn by March 2010 – the highest forecast percentage increase of any quoted UK water company. After adjusting for the growth in gearing, the company again expects its growth in RCV to outstrip significantly the anticipated growth in net borrowings.

VIRIDOR WASTE

Financial performance in 2005/06 was again strong. Revenue rose by 20.4% (£50.6m) to £298.9m in 2005/06. Acquisitions accounted for £21.3m of the increase and underlying business £29.3m. Landfill tax within revenue increased by £19.8m.

Viridor Waste's operating profit before intangibles amortisation rose by 19.7% to £35.9m (£34.3m after intangibles amortisation), compared to £30.0m (£28.6m after intangibles amortisation) in 2004/05. The increase was driven by good performance in landfill, power generation, contracts and the Brett Waste Management acquisition. Of the 19.7% total growth in 2005/6 Brett Waste accounted for 11.7%, and the underlying business for 8.0%. Since 2000/01 operating profit before intangibles amortisation has grown at a compound rate of 22.3% pa of which around 11% has been organic, with the rest being achieved through acquisitions.

Earnings before interest, tax, depreciation and amortisation (EBITDA) grew 18.3% from £56.4m to £66.7m. Profit before tax at £21.9m was 9.0% up on the previous year. Capital expenditure for the year was £58.9m (2004/05 - £45.8m).

Total landfill disposal volumes increased by 7% to 4.3 million tonnes, due mainly to the Brett Waste Management acquisition. Total landfill disposal volumes excluding acquisitions remained unchanged compared to the previous year after adjusting for non-recurring volumes:

i) in the first quarter of 2004/05 in advance of the banning of the disposal of hazardous waste to non-hazardous landfill and
ii) in the first half of 2005/06, a significant one-off sludge contract at Masons.

Excluding the above, underlying volume was unchanged, with growth in industrial/commercial volumes (particularly from Viridor's own fleet) offsetting a decline in municipal waste volumes.

Average gate fees rose by 9%, reflecting inputs of stabilised non-reactive hazardous waste and the underlying tightness of UK landfill capacity. At 31 March 2006, Viridor had 87 million cubic metres of landfill capacity.

Viridor Waste's total power generation capacity increased by a further 17% in the year, principally through the Brett Waste acquisition. Viridor's power generation prices (excluding acquisitions) rose 10% to £59 per Megawatt hour, reflecting the increasing underlying brown energy price and the ongoing shortage of renewable energy in the UK which is driving the premium price achieved by renewables. Including the Brett Waste acquisition, total output increased by 12% in the year to 367 Gigawatt hours. Viridor's capacity as at 31 March 2006 (including the contribution from Brett Waste) was 61 Megawatts, around 52% of which was eligible for ROCs.

In June 2005, Viridor acquired Brett Waste, a landfill and power generation business, for a cash consideration of £44.4m. The company owns strategically located landfill sites in Kent and Essex with approximately 11m cubic metres of consented void capacity, landfill gas power generation schemes totalling 6 Megawatts capacity and associated waste transfer station, recycling, composting and transport activities. The acquisition fits well with Viridor's stated strategy and complements the Company's existing facilities in the adjacent counties of East Sussex, Surrey and Suffolk. Brett Waste has now been successfully integrated and was earnings enhancing (after integration costs and intangibles amortisation) in its first 9 months, a year ahead of expectations.

In August 2005, Viridor opened the first new landfill disposal site to be developed in Cornwall for about 20 years. With a capacity of 3m cubic metres, the Lean Quarry integrated waste management facility near Liskeard in Cornwall also provides a materials recycling facility, a waste transfer station and a collection services depot.

In September 2005, Viridor set up Lakeside Energy from Waste Limited, a joint venture with Grundon Waste Management Limited, to build and operate an energy from waste (EfW) plant. The 50 : 50 joint venture is in line with Viridor's strategy of capitalising on opportunities arising from the Government's developing waste strategy and will assist local authority customers in meeting their landfill diversion targets and avoiding penalties under the Landfill Allowance Trading Scheme (LATS). A number of these councils are existing waste disposal customers of Viridor or Grundon. The plant will have a capacity of 400,000 tonnes per annum and it will also provide power generation capacity of 32 Megawatts of electricity which will be fed into the national grid. The plant is being built at a strategically located site at Colnbrook near Slough, which has the relevant permissions and permits. Total investment is projected to be circa £160m, 86% of which is non-recourse debt financing with the balance split equally between Viridor and Grundon. The total project IRR is within normal project finance parameters. The plant is under construction and scheduled to be commissioned in mid-2008.

On 15 May 2006, Viridor Waste announced the acquisition of Wyvern Waste Services Limited from Somerset County Council for £25m (including £3m cash on the balance sheet) as part of a 25 year Public Private Partnership (PPP) contract with the County. The acquisition comprises 5m cubic metres of consented landfill void, 7 Megawatts of power generation capacity and associated recycling and treatment operations. It is expected to be earnings enhancing before amortisation of intangibles in its first full year. This acquisition and associated contract fit well with Viridor Waste's strategy.

Viridor Waste continues to explore other suitable PFI or PPP opportunities as part of its overall strategy : in May 2006 Greater Manchester Waste Disposal Authority announced that the Viridor Waste Management Limited/John Laing Plc partnership was one of two parties shortlisted to submit Best And Final Offers for its waste management services contract.

PENSIONS

The Group pension schemes had a deficit (net of deferred tax) under IAS 19 at 31 March 2006 of circa £29m, compared to circa £56m at 31 March 2005. In August 2005 the Company made a prepayment of employer pension contributions for the period to 2010 of £44m (£31m net of tax). A strong investment performance has been offset by an increase in liabilities.

FINANCING INITIATIVES

The total net interest charge increased from £62.0m to £64.3m (excluding exceptional items). The average interest rate on net debt has reduced to 5.1% (2004/05 5.6%) for the Group and 4.7% for South West Water.

The Group funding strategy utilises a mix of fixed, floating and index linked rate borrowings. To reduce the risk of adverse interest rate movements, South West Water has extended its swap arrangements to fix the interest rate on over 65% of its current net debt for the period up to March 2007 and on 60% up to March 2010.

In addition, South West Water has index linked 10% of its current net debt up to 2041. The £114m finance facility lease reported within the interim results announcement has been increased to £142m. In February 2006 South West Water exercised an option to convert this lease to an RPI index linked basis (1.365% real), taking advantage of historically low index linked rates and also to reduce earnings volatility.

During the year South West Water agreed a new £70m facility with the European Investment Bank. The 10.625% £150m bond due 2012 was retired in January 2006.

TAXATION

The mainstream corporation tax charge for the year was £14.8m (£3.9m credit after exceptional items) compared to a £7.9m charge in 2004/05.

The deferred tax charge for the year was £20.2m (£15.6m in 2004/05).

RETURN OF CAPITAL

On 15 February 2006 Pennon's shareholders approved the proposal to return £200m of cash to shareholders, with circa £145m of this return by way of a B Share scheme and circa £55m through an on-market share buy back programme. The B Shares have now been issued with circa £138m of capital returned in March 2006, and the balance in April.

In order to maintain comparability of the share price after the B Share scheme, Pennon undertook a share consolidation whereby shareholders received ten new ordinary shares for every eleven existing ordinary shares. As a result, the number of ordinary shares in issue was reduced from approximately 130.5 million to 118.6 million at year end. The weighted average number of shares during 2005/06 was 127.3m.

The £55m on-market share buy back scheme is to be progressed.

In association with the return of capital, a payment of £20 has been made to each South West Water customer at a cost of £14.5m.

BOARD MATTERS

Bob Baty, Chief Executive of South West Water, is due to retire at the end of July following 45 years service in the industry. The Board would like to take this opportunity to express its gratitude to Bob for his significant contribution to South West Water since privatisation in 1989 and to wish him well in his retirement.

The Board looks forward to welcoming Chris Loughlin as an Executive Director of Pennon and Chief Executive of South West Water. He will take up his post on 1 August.

PROSPECTS

The Board has confidence that South West Water will successfully deliver the new K4 regulatory contract and significantly grow its Regulatory Capital Value up to 2010. Viridor Waste's successful strategy of creating long-term sustainable profit growth is expected to continue through capitalising on its landfill asset base, exploiting its landfill gas power generation potential and pursuing profitable opportunities in line with the Government's developing waste strategy.

Ken Harvey
Chairman
1 June 2006

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Consolidated income statement for the year ended 31 March 2006

	Note	**Before exceptional items 2006 £m**	**Exceptional items (note 4) 2006 £m**	**Total 2006 £m**	Before exceptional items 2005 £m	Exceptional items (note 4) 2005 £m	Total 2005 £m
					Unaudited		
Continuing operations							
Revenue	3	**645.7**		**645.7**	551.4		551.4
Operating costs							
Manpower costs		**(79.9)**		**(79.9)**	(68.3)	(3.0)	(71.3)
Raw materials and consumables used		**(40.7)**		**(40.7)**	(32.8)		(32.8)
Other operating expenses		**(245.9)**	**(14.5)**	**(260.4)**	(207.3)	(1.9)	(209.2)
Depreciation		**(102.5)**		**(102.5)**	(90.7)		(90.7)
Amortisation of intangibles		**(1.6)**		**(1.6)**	(1.4)		(1.4)
Operating profit	3	**175.1**	**(14.5)**	**160.6**	150.9	(4.9)	146.0
Interest payable and similar charges		**(96.8)**	**(50.2)**	**(147.0)**	(89.3)		(89.3)
Interest receivable		**32.5**	**7.9**	**40.4**	27.3		27.3
Share of post-tax profit from joint venture		**0.1**		**0.1**	0.1		0.1
Profit before tax		**110.9**	**(56.8)**	**54.1**	89.0	(4.9)	84.1
Tax on ordinary activities	5	**(35.0)**	**18.7**	**(16.3)**	(23.5)		(23.5)
Profit/(loss) for the year from continuing operations		**75.9**	**(38.1)**	**37.8**	65.5	(4.9)	60.6
Discontinued operations							
Post-tax disposal profit				**-**		5.0	5.0
Profit/(loss) for the year		**75.9**	**(38.1)**	**37.8**	65.5	0.1	65.6
Profit/(loss) attributable to equity shareholders		**75.9**	**(38.1)**	**37.8**	65.5	0.1	65.6
Earnings per share (pence per share)	6						
- Basic				**29.7**			52.1
- Diluted				**29.4**			51.7
Earnings per share from continuing operations							
- Basic				**29.7**			48.1
- Diluted				**29.4**			47.8
Dividend per share (pence per share)	7			**51.6**			43.0
Dividend proposed for the period (£m)	7			**61.0**			55.1

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Consolidated statement of recognised income and expense for the year ended 31 March 2006

	Unaudited	
	2006	2005
	£m	£m
Profit for the year	**37.8**	65.6
Actuarial (losses)/gains on defined benefit schemes	**(2.8)**	1.9
Cash flow hedges		
Net fair value gains	**1.0**	-
Tax on items taken directly to or transferred from equity	**0.8**	(0.6)
Net (losses)/gains not recognised directly in income statement	**(1.0)**	1.3
Total recognised income for the year	**36.8**	66.9
Adjustments on adoption of IAS 32/39 1 April 2005 (net of tax)	**8.6**	-
	45.4	66.9
Attributable to equity shareholders	**45.4**	66.9

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Consolidated balance sheet at 31 March 2006

	Unaudited 2006 £m	2005 £m
Assets		
Non-current assets		
Goodwill	**98.6**	64.4
Intangible assets	**5.7**	6.0
Property, plant and equipment	**2,415.9**	2,218.5
Trade and other receivables	**6.0**	3.3
Investments accounted for using equity method	**1.3**	-
	2,527.5	2,292.2
Current assets		
Inventories	**5.0**	4.7
Trade and other receivables	**94.5**	99.6
Financial assets		
Derivative financial instruments	**3.1**	-
Cash and cash equivalents	**99.4**	303.4
	202.0	407.7
Liabilities		
Current liabilities		
Financial liabilities		
Borrowings	**(54.7)**	(54.8)
Derivative financial instruments	**(3.0)**	-
Trade and other payables	**(170.1)**	(127.8)
Current tax liabilities	**(24.0)**	(23.6)
Provisions for liabilities and charges	**(11.4)**	(8.4)
	(263.2)	(214.6)
Net current (liabilities)/assets	**(61.2)**	193.1
Non-current liabilities		
Financial liabilities		
Borrowings	**(1,471.8)**	(1,366.8)
Other non-current liabilities	**(2.2)**	(19.1)
Retirement benefit obligations	**(41.7)**	(79.8)
Deferred tax liabilities	**(302.8)**	(282.8)
Provisions for liabilities and charges	**(66.6)**	(27.9)
	(1,885.1)	(1,776.4)
Net assets	**581.2**	708.9
Shareholders' equity		
Share capital	**184.2**	142.0
Share premium account	**10.2**	153.7
Capital redemption reserve	**98.4**	-
Retained earnings and other reserves	**288.4**	413.2
Total shareholders' equity	**581.2**	708.9

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Consolidated cash flow statement for the year ended 31 March 2006

	Note	Unaudited 2006 £m	2005 £m
Cash flows from operating activities			
Cash generated from operations	8	**232.1**	242.4
Interest paid		**(128.9)**	(68.5)
Forward interest rate swap settlement		**-**	(3.4)
Tax paid		**(2.2)**	(0.4)
Net cash generated from operating activities		**101.0**	170.1
Cash flows from investing activities			
Interest received		**22.5**	12.8
Acquisition of subsidiaries (net of cash acquired)		**(44.7)**	(28.6)
Investment in joint venture		**(1.1)**	-
Proceeds of business disposal		**5.0**	-
Proceeds from sale of available for sale investments		**-**	4.2
Purchase of intangible assets		**-**	(0.2)
Purchase of property, plant and equipment		**(218.6)**	(167.1)
Proceeds from sale of property, plant and equipment		**4.8**	2.3
Net cash used in investing activities		**(232.1)**	(176.6)
Cash flows from financing activities			
Net proceeds from issue of ordinary share capital		**1.6**	0.8
Release of restricted cash balances		**177.1**	-
Net proceeds from new borrowing		**182.5**	150.0
Repayment of borrowings		**(224.3)**	(130.2)
Finance lease drawdowns		**141.6**	57.3
Finance lease principal repayments		**(15.8)**	(5.4)
Dividends paid		**(34.1)**	(28.3)
B share payments		**(137.8)**	-
Net cash received from financing activities		**90.8**	44.2
Net (decrease)/increase in cash and cash equivalents		**(40.3)**	37.7
Cash and cash equivalents at beginning of year		**120.6**	82.9
Cash and cash equivalents at end of year		**80.3**	120.6

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NOTES

1. **Basis of preparation**

These unaudited results are the first financial results following adoption of International Financial Reporting Standards (IFRS) as adopted by the European Union. The accounting policies adopted and the reconciliations from net assets and equity under UK Generally Accepted Accounting Principles (UK GAAP) at transition to IFRS on 1 April 2004 and for the year ended 31 March 2005 were set out in a separate document "Adoption of International Financial Reporting Standards (IFRS)" published on 8 December 2005.

All accounting policies have been consistently applied except where the Group has taken advantage of the exemption in IFRS 1 "First-time Adoption of IFRS" from the requirement to restate comparative information for IAS 32 "Financial Instruments : disclosure and presentation" and IAS 39 "Financial Instruments : recognition and measurement". These standards have been applied with effect from 1 April 2005.

The financial information has been prepared in accordance with all IFRS and interpretations of the Internal Financial Reporting Interpretations Committee (IFRIC) applicable for the year ended 31 March 2006 and with those parts of the Companies act 1985 applicable to companies reporting under IFRS.

2. **Financial information**

The financial information for the year ended 31 March 2005 does not constitute full financial statements within the meaning of section 240 of the Companies Act 1985. The full financial statements for that year, which were prepared under UK GAAP, have been delivered to the Registrar of Companies. The independent auditors' report on those financial statements was unqualified and did not contain a statement under section 237 (2) or (3) of the Companies Act 1985.

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NOTES (Continued)

3. **Segmental reporting**

	Unaudited	
	2006	2005
	£m	£m
Continuing operations		
Revenue		
Water and sewerage	**348.5**	307.0
Waste management	**298.9**	248.3
Other	**7.3**	6.9
Less intra-segment trading	**(9.0)**	(10.8)
	645.7	551.4
Segment result		
Earnings before depreciation, amortisation and exceptional items *		
Water and sewerage	**213.4**	186.4
Waste management	**66.7**	56.4
Other	**(0.9)**	0.2
	279.2	243.0
Earnings before amortisation and exceptional items *		
Water and sewerage	**141.5**	122.2
Waste management	**35.9**	30.0
Other	**(0.7)**	0.1
	176.7	152.3
Operating profit before exceptional items *		
Water and sewerage	**141.5**	122.2
Waste management	**34.3**	28.6
Other	**(0.7)**	0.1
	175.1	150.9
Operating profit		
Water and sewerage	**127.0**	118.8
Waste management	**34.3**	28.6
Other	**(0.7)**	(1.4)
	160.6	146.0
Discontinued operations		
Other	**-**	5.0

* The exceptional items are detailed in note 4.

4. **Exceptional items**

The exceptional items are :	**Unaudited 2006 £m**	2005 £m
Continuing operations		
Customer payment	**14.5**	**-**
Abortive acquisition costs	**-**	1.5
Business restructuring costs		
Manpower costs	-	3.0
Other external charges	-	0.4
Operating profit	**14.5**	4.9
Bond retirement	**50.2**	**-**
Receipt on transfer of lease	**(7.9)**	-
Profit before tax	**56.8**	4.9
Tax arising on exceptional items	**(18.7)**	-
	38.1	4.9
Discontinued operations		
Post-tax disposal profit	**-**	(5.0)
	38.1	(0.1)

The customer payment and bond retirement relate to financial restructuring in the Company and South West Water Limited.

The receipt on transfer of lease relates to a consent fee paid to South West Water Limited arising from the sale of finance leases between financial institutions.

The abortive acquisition costs arose from negotiations to acquire the UK landfill and landfill gas operations of Shanks Group Plc where discussions were terminated on 25 May 2004.

The business restructuring costs arose in the water and sewerage segment.

The business disposal profit relates to the balance of proceeds due from the 1998 arrangement to dispose of the Group’s interest in Societa Italo Britannica dell’Acqua Srl.

No tax charge arose from the business disposal profit.

NOTES (Continued)

5. **Tax on profit on ordinary activities**

	Unaudited			
	Before exceptional items 2006 £m	**Exceptional items (note 4) 2006 £m**	**Total 2006 £m**	2005 £m
Tax on profit on ordinary activities comprises:				
United Kingdom corporation tax	**14.8**	**(18.7)**	**(3.9)**	**7.9**
Deferred tax	**20.2**	**-**	**20.2**	**15.6**
	35.0	**(18.7)**	**16.3**	**23.5**

6. **Basic and diluted earnings per share**

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

	Unaudited	
Number of shares (millions)	**2006**	2005
For basic earnings per share	**127.3**	126.0
Effect of dilutive potential ordinary shares :		
Share options	**1.1**	0.9
For diluted earnings per share	**128.4**	126.9

At 31 March 2006 there were 118,608,847 Ordinary shares of £1.221 each in issue (2005 127,944,340 Ordinary shares of £1.11 each).

Earnings per share from discontinued operations
(in pence per share)

- Basic	-	4.0
- Diluted	-	3.9

Adjusted basic and diluted earnings per share

Adjusted earnings per share have been calculated to exclude the impact of the exceptional items and deferred tax on the results, as these items can have a distorting effect on earnings from year to year and therefore warrant separate consideration. Adjusted earnings have been calculated as follows :

PENNON GROUP PLC

NOTES (Continued)

6. **Basic and diluted earnings per share (continued)**

	Unaudited					
			2006			2005
		Earnings per share			Earnings per share	
	Earnings	**Basic**	**Diluted**	Earnings	Basic	Diluted
	£m	**p**	**p**	£m	p	p
Adjusted earnings :						
Earnings per share from continuing operations	**37.8**	**29.7**	**29.4**	60.6	48.1	47.8
Exceptional items (net of tax)	**38.1**	**29.9**	**29.7**	4.9	3.9	3.8
Deferred tax	**20.2**	**15.9**	**15.7**	15.6	12.3	12.3
Adjusted earnings per share from continuing operations	**96.1**	**75.5**	**74.8**	81.1	64.3	63.9

7. **Dividends**

	Unaudited	
	2006	2005
	£m	£m
Amounts recognised as distributions to equity holders in the year :		
Interim dividend paid for the year ended 31 March 2005 : 13.8p (2004 13.2p) per share	**17.7**	16.4
Final dividend paid for the year ended 31 March 2005 : 29.2p (2004 27.8p) per share	**37.4**	34.7
	55.1	51.1

	Unaudited	
	2006	2005
	£m	£m
Proposed dividends		
Proposed interim dividend for the year ended 31 March 2006 : 16.5p (2005 13.8p) per share	**19.4**	17.7
Proposed final dividend for the year ended 31 March 2006 : 35.1p (2005 29.2p) per share	**41.6**	37.4
	61.0	55.1

The proposed interim and final dividends have not been included as a liability in these financial statements. The proposed interim dividend was paid on 13 April 2006 and the proposed final dividend is subject to approval by shareholders at the Annual General Meeting.

If approved at the Annual General Meeting on 27 July 2006 the final dividend of 35.1p per share will be paid on 3 October 2006 to shareholders on the register at 4 August 2006. The Company is intending to offer a Dividend Re-Investment Plan (DRIP) in respect of this dividend and full details will be sent to shareholders on 21 August 2006. The final date for receipt of DRIP application forms will be 12 September 2006.

PENNON GROUP PLC

NOTES (Continued)

8. **Cash flow from operating activities**

The reconciliation of operating profit to net cash inflow from operating activities is :

Cash generated from operations	**Unaudited 2006 £m**	2005 £m
Profit for the year	**37.8**	60.6
Adjustments for:		
Employee share schemes	**1.7**	1.5
Deferred income released to profits	**(0.3)**	(0.2)
Profit on disposal of property, plant and equipment	**(1.1)**	(1.4)
Depreciation charge	**102.5**	90.7
Amortisation of intangible assets	**1.6**	1.4
Share of post-tax profit from joint venture	**(0.1)**	(0.1)
Interest payable and similar charges	**147.0**	89.3
Interest receivable	**(40.4)**	(27.3)
Taxation	**16.3**	23.5
Changes in working capital *(excluding the effect of acquisition of subsidiaries)*		
Increase in inventories	**(0.3)**	(0.2)
Decrease/(increase) in trade and other receivables	**2.0**	(0.9)
Decrease in long-term deposits	**-**	(3.5)
Increase in trade and other payables	**8.4**	8.5
(Decrease)/increase in retirement benefit obligations	**(39.7)**	2.9
Decrease in provisions for liabilities and charges	**(3.3)**	(2.4)
Net cash generated from operations	**232.1**	242.4

9. **Net borrowings**

	Unaudited 2006 £m	2005 £m
Cash and cash equivalents	**99.4**	303.4
Borrowings – current		
Bank overdrafts	**(18.5)**	(5.1)
Other current borrowings	**(8.2)**	(20.4)
Finance lease obligations	**(28.0)**	(29.3)
Total current borrowings	**(54.7)**	(54.8)
Borrowings – non-current		
Bank loans	**(312.7)**	(255.3)
Other non-current borrowings	**(232.2)**	(316.4)
Finance lease obligations	**(926.9)**	(795.1)
Total non-current borrowings	**(1,471.8)**	(1,366.8)
Total net borrowings	**(1,427.1)**	(1,118.2)

NOTES (continued)

10. **Acquisitions**

On 21 June 2005 the entire issued share capital of Brett Waste Management Limited, (now renamed Viridor Waste Kent Limited), was purchased by Viridor Waste Management Limited for a cash consideration of £44.7 million including costs. The acquisition has been accounted for using the acquisition method and goodwill of £34.2 million and intangible fixed assets of £1.3 million have been capitalised. The intangible fixed assets are being amortised evenly over the Directors' estimate of useful economic life.

On 30 September 2005 Viridor Waste Management Limited acquired 50% of the entire issued share capital of Lakeside Energy From Waste Limited for an investment of £1.1 million including costs. The joint venture has been accounted for using the equity method.

11. The Annual Report for 2005/06 will be posted to shareholders on 26 June 2006.

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