news from Pennon Group Plc

PENNON GROUP PLC **31 May 2007**

PRELIMINARY RESULTS FOR THE YEAR ENDED 31 MARCH 2007

Pennon Group announces its unaudited results for the year ended 31 March 2007.

FINANCIAL HIGHLIGHTS

- Operating profit [(1)] up 14.2% to £201.8m.
  - South West Water up 10.8% to £156.8m.
  - Viridor up 30.4% to £46.8m.
- Profit before tax [(2)] up 18.2% to £131.1m.
- Earnings per share up 20.2% to 30.3p. [(3)]
- Dividend
  - Recommended final dividend per share up 8.5% to 12.7p.
  - Full year dividend up 7.8% to 18.55p.
  - Dividend policy of 3% per annum real increases until 2009/10.
- 3 for 1 stock split took place July 2006.

(1) Before amortisation of intangibles, and exceptional items in 2005/06

(2) Before exceptional items in 2005/06

(3) Before deferred tax, and exceptional items in 2005/06. Basic earnings per share are 26.5p (2005/06 – 9.9p)

OPERATIONAL HIGHLIGHTS

- South West Water :
  - On target to deliver 2005 – 2010 Regulatory Contract.
  - Profit increase reflecting strong growth in Regulatory Capital Value 2005 – 2010.
  - South West bathing waters 100% compliant with EU mandatory standards (all 144 beaches for the first time).
  - Tenth consecutive year without hosepipe bans and drought orders.
  - Drinking water quality sustained at all time high as direct result of mains rehabilitation.
  - Capital investment of £184.0m, 117% of operating profit.
  - All major projects delivered in line with Regulators' expectations.
  - Preparing for PR09.

- Viridor :
  - Particularly strong growth in operating profits.
  - Preferred bidder (consortium with John Laing) status achieved for the Greater Manchester Waste Disposal Authority PFI contract.
  - Wyvern Waste Services Limited acquisition fully integrated and earnings enhancing in its first ten months.
    - Long-term waste management PPP contract secured with Somerset County Council.
  - Skipaway Holdings Limited acquired in February for £14.7m.
  - Lakeside (joint venture with Grundon) energy from waste plant under construction and on schedule to open in 2008.

The Chairman, Ken Harvey, said, “I am delighted to report an excellent year for Pennon. These results demonstrate further profitable growth in the Group and affirm our strategy of focusing on our two key businesses, South West Water and Viridor. South West Water remains on target to meet the current regulatory contract and Viridor has had an outstanding year delivering a particularly strong performance based on both organic growth and successful acquisitions as a result of its focused strategy.

“The Board has noted the recent rise in the Group’s share price, but is not aware of any particular reason for the movement. The Group will continue to pursue its declared strategy.”

For further information today, 31 May 2007, please contact :

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GROUP OVERVIEW

- Revenue rose by 15.9% to £748.3m.

- Operating profit before amortisation of intangibles rose by 14.2% to £201.8m. [(1)]

- Profit before tax was up 18.2% to £131.1m [(1)]

- Earnings per share from continuing operations and before deferred tax increased by 20.2% from 25.2p [(1)] [(2)] to 30.3p. Basic earnings per share (after exceptional items in 2005/06) increased from 9.9p [(2)] to 26.5p.

- Capital expenditure was £245.1m (2005/06 – £249.7m).

- Net borrowings at 31 March 2007 were £1,557m, an increase of £130m since 31 March 2006. Gearing, being net borrowings to shareholders' funds plus net borrowings, was 71% (2005/06 – 71%). Interest cover was 2.9 times (2005/06 - 2.7 times). South West Water net debt to RCV was 62% (2006 – 62%).

- The Board has recommended a final dividend of 12.7p, up 8.5%, subject to shareholder approval. Together with the interim dividend of 5.85p, this will result in a total dividend for the year of 18.55p, an increase of 7.8% on the total dividend for 2005/06. The Board's stated policy is to grow the Group dividend by 3% above inflation per annum 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.

[(1)] Before exceptional items in 2005/06 as detailed in note 5 to the financial statements.

[(2)] Restated for 3 for 1 stock split in July 2006.

SOUTH WEST WATER

South West Water revenue rose by £33.0m to £381.5m. Approved tariff increases, including the 9.8% K factor, amounted to £43.0m. 7,100 new customer connections contributed £3.1m. Customers switching from unmeasured to metered charging caused a reduction of £8.0m in revenue. Over 57% of South West Water's domestic customers are now metered. A 2.9% decrease in measured demand reduced turnover by £5.1m.

South West Water's operating profit rose 10.8% (before exceptional costs in 2005/06) to £156.8m. Operating costs, excluding depreciation, increased by £11.9m to £147.0m. Additional costs from new capital schemes of £2.7m, inflation of £10.2m (including power costs of £5.5m) and other cost increases of £2.0m (including infrastructure expenditure charged to operating costs), were partially offset by £3.0m of efficiency savings. Depreciation increased by £5.8m to £77.7m, primarily as a result of new capital schemes. The cost of bad debts (part of which is charged against revenue) is rising more slowly than the tariff increase. The company is implementing detailed plans to ensure it is well on track to achieve the operating cost efficiency targets set by the Director General of Water Services for the period up to 2010.

South West Water has put in place a comprehensive strategy to help ensure a continued secure supply of water for the region. In 2006/07 three of the company's key reservoirs were again 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. 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 of 84 ML/day. South West Water has achieved Ofwat's leakage targets since their inception and this year has achieved its lowest ever level of leakage. These activities contributed to the tenth consecutive year of no water restrictions in our region.

In addition, the purchase of Park Lake in November 2006, a former china clay pit on Bodmin Moor, is a significant addition to water resources in Cornwall, further enhancing their robustness. The new lake will be the region's fourth largest reservoir. Work will now be carried out to build the appropriate infrastructure and it is anticipated that the water from this new source will become available during 2007/08 (subject to obtaining the necessary Environment Agency (EA) permissions).

Drinking water quality and river water quality have been sustained at an all time high and the region features the highest proportion of high quality rivers in England. In 2006, for the first time, 100% of the designated bathing waters in the South West Water region achieved the EU mandatory standard, and 91.7% achieved the even more stringent guideline standard.

Ofwat's 2005/06 'Levels of Service Report' confirms that South West Water has maintained last year's step change improvement in its Overall Performance Assessment (OPA) ranking, maintaining its 6th position out of the 10 water and sewerage companies. We expect this position to be consolidated when the 2006/07 scores are published later this year.

Capital expenditure was £184.0m (2005/06 - £191.0m). £93.6m was invested in water supply improvements including water mains renovation and water treatment works enhancement. Continued high levels of investment in the £240m water mains renovation programme to replace or reline 3,200kms of water mains will be a key element during the remainder of the K4 period. A further 638kms 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.

Waste water investment expenditure totalled £90.4m for the year. All of the major projects in the company's 15 year original 'Clean Sweep' coastal sewage treatment programme have been completed and as noted above the region is now attaining record levels of bathing water quality compliance.

South West Water continues to deliver capital projects in line with Ofwat, DWI and EA expectations. The company is targeting 5% efficiency outperformance of Ofwat's allowed K4 capital programme of £762m (2002/03 prices) and is on track to achieve this.

'Service +', a major project to improve the service to customers in relation to the company's day to day operational activities and to reduce costs, was launched in October 2006. The new

Service Centre in Exeter utilises the latest mobile computing technology to give quicker, more accurate information to customers on service issues as well as better prioritising the work of field operations staff. The benefits of the new system are already being seen with a significant reduction in the number of repeat contacts from customers.

‘WaterCare’, a ground-breaking new customer care programme, was launched early in 2007 targeted at helping those most in need pay their bills by advising them on how to manage better both their water use and household budget. Trained advisors are meeting with around 2,500 qualifying customers a year in their homes and offering a range of free services including home water audits, advice on potential savings from fitting a meter and advice on receiving financial benefits to which they are entitled. The identification of customers who would benefit from moving on to special payment plans enables them to make regular affordable payments, thereby reducing the company’s outstanding debt.

In preparing for the forthcoming periodic review of prices in 2009 (PR09), a number of projects are under way to ensure that South West Water is prepared for the new challenges that lie ahead. The customer contact/billing contract will be re-tendered during 2007 and the company will build on the success of ‘Service +’. The role of tariff structures in addressing the agenda of affordability and sustainability is also being reviewed.

To meet the twin objectives of service excellence and operational efficiency, South West Water has launched a long-term project, ‘Puros’, to move the organisation towards a more centralised operational structure employing increased levels of automation and remote working. In the shorter term, a new ‘rightsourcing’ review is under way to determine the optimal combination of internal and external resource provision. It is expected that the cost of £3m - £4m of ongoing organisational restructuring will be provided for in 2007/08.

Regulatory Capital Value (RCV) is expected to grow by 34% 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 step change in gearing following the capital restructuring in 2005/06, the company again expects its growth in RCV to outstrip significantly the anticipated growth in net borrowings over the K4 period.

VIRIDOR

Viridor traded particularly strongly in 2006/07, building further on the growth achieved over the past six years. Revenue was up £68.8m (23.0%) to £367.7m, of which acquisitions accounted for £39.6m and underlying business £29.2m. This increase included landfill tax of £21.7m.

Viridor's earnings before interest, tax, depreciation and amortisation (EBITDA) rose 24.1% from £66.7m to £82.8m. Operating profit before intangibles amortisation (PBITA) for the year increased by 30.4% (£10.9m) to £46.8m, compared to £35.9m in 2005/06. The increase reflected a full year's contribution from last year's Brett Waste Management acquisition, the positive effect of this year's acquisitions (Wyvern Waste and Skipaway), a one-off profit of £0.6m on the disposal of Viridor's interest in Devon Waste Management Limited and 12.6% growth in the underlying business.

Profit before tax at £27.6m was up 26.0% on the previous year. Capital expenditure for the year was £60.9m (2005/06 - £58.9m).

Total landfill disposal volumes increased by 9% to 4.7 million tonnes. Total landfill disposal volumes excluding acquisitions were held constant at 4.3 million tonnes. Average gate fees rose by 7% to £19 per tonne and margins increased by 50p to over £6 per tonne.
At 31 March 2007, Viridor had 90 million cubic metres of landfill capacity, an increase of 3 million over the previous year. This increase reflected the 5 million cubic metres that came with the Wyvern acquisition and 4 million cubic metres of net planning gains at 4 sites, offset by usage of 6 million cubic metres in the year.

Viridor's total power generation output increased by a further 15% in the year to 423 GWH. Average prices increased 4.3% to £62 per MWH reflecting the strong brown energy prices and the ongoing shortage of renewable energy in the UK which is driving the price premium achieved by renewables. The timing of open market sales contracts in 2006/07 was particularly favourable – current brown energy prices in 2007/08 are lower. Total capacity (excluding a small amount of sub contract capacity) grew 14 MW from 61 MW at 31 March 2006 to 75 MW at 31 March 2007 (of which Wyvern contributed 7 MW). At 31 March 2007

50% of Viridor's power generating capacity was eligible for Renewable Obligation Certificates (ROCs) and 50% for Non Fossil Fuel Obligation (NFFO).

In May 2006, Viridor acquired Wyvern Waste 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 company is already integrated and was earnings enhancing in its first ten months.

Viridor continues to explore other suitable Private Finance Initiative (PFI) and PPP opportunities as part of its overall strategy. In January 2007 Greater Manchester Waste Disposal Authority announced that the Viridor Waste Management Limited / John Laing Infrastructure Limited consortium had been selected as preferred bidder for its waste management services contract. With an investment value of around £300m, this will be the largest such scheme in the UK and will involve the handling of around 1.4 million tonnes of waste per annum. Final negotiations are underway with the contract due to commence in the current financial year. In addition, Viridor is one of Manchester's nominated landfill contractors for 5 years from April 2008.

In September 2005, Viridor entered into a joint venture with Grundon Waste Management Limited to set up Lakeside Energy from Waste Limited to build and operate an energy from waste 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 up to 37 MW of electricity which will be fed into the national grid. The plant is being built at a strategically located site at Colnbrook near Heathrow, 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 plant is under construction and on schedule to open in the second half of calendar 2008.

Other significant new developments in the year include :

- a 70,000 tonne pa recycling and disposal contract extension to 2027 for the Borough of Poole.
- a 7 year 120,000 tonne pa landfill contract for the City of Plymouth, starting in April 2008.
- 5 year landfill and 7 year recycling contracts for South Lanarkshire totalling £20m.
- preferred bidder status achieved for medium term disposal contracts with West Sussex and Suffolk County Councils.
- the acquisition of Skipaway for £14.7m in February 2007. This acquisition comprises three transfer stations plus associated collection and recycling activities in Kent and handles approximately 240,000 tonnes of material per annum.
- planning application submitted for a 60,000 tonne energy from waste facility in Exeter.

PENSIONS

The Group pension schemes had net liabilities at 31 March 2007 of £41 million (31 March 2006 - £42 million) from pension fund assets of £348m and liabilities of £389m. Sound investment performance, an increase in the market interest rate used to discount liabilities, plus a further £9m prepayment of employer contributions in September 2006, have been offset by an increase in liabilities of which £16m arises from the use of an updated longevity assumption for pensioners. A full actuarial valuation is being undertaken as at April 2007. The net liabilities (after deferred tax) represented circa 1% of the Group's total market capitalisation as at 31 March 2007.

FINANCING INITIATIVES

The total net interest charge increased from £64.3m (before exceptional net charges) in 2005/06 to £69.2m in 2006/07. The average interest rate on net debt for the Group overall has been reduced to 4.6% (2005/06 - 5.1%) for the Group and 4.3% for South West Water. This is believed to be amongst the lowest in the sector.

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 swap arrangements in place to fix the interest rate on circa 60% of its projected net debt for the period up to March 2010. In addition, circa 10% of South West Water current net debt is index-linked to 2041.

During the year the following financing initiatives were implemented :

- £180m finance lease extended by 20 years.
- £100m 4.13% private placement issued.
- £85m finance lease drawdown for water mains rehabilitation.

TAXATION

The mainstream corporation tax charge for the year was £23.9m (2005/06 - £14.8m) giving a mainstream effective tax rate of 18%.

The deferred tax charge for the year was £13.3m (2005/06 - £20.2m).

RETURN OF CAPITAL

The Company completed the redemption of the outstanding B shares for a total of £5.7m in April 2006. Circa £145m has now been returned through the B share issue.

STRATEGY & PROSPECTS

The Board's priority continues to be the creation of shareholder value through its strategic focus on water, sewerage and waste management. The excellent performance highlighted above is testament to the Board's strategy of focusing on these key business areas.

The Board has confidence that South West Water will successfully deliver the K4 regulatory contract and significantly grow its Regulatory Capital Value up to 2010 (£2.6bn). South West Water is now looking beyond K4 and preparing for PR09. Viridor'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. In addition, the Group has put in place a long-term funding structure to enable it to continue to finance its activities efficiently.

Ken Harvey
Chairman
31 May 2007

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Consolidated income statement for the year ended 31 March 2007

	Note	**2007 (Unaudited) £m**	Before exceptional items 2006 £m	Exceptional items (note 5) 2006 £m	Total 2006 £m
Revenue	3	**748.3**	645.7	-	645.7
Operating costs					
Manpower costs		**(91.0)**	(79.9)	-	(79.9)
Raw materials and consumables used		**(47.2)**	(40.7)	-	(40.7)
Other operating expenses		**(294.6)**	(245.9)	(14.5)	(260.4)
Depreciation		**(113.7)**	(102.5)	-	(102.5)
Amortisation of intangibles		**(1.8)**	(1.6)	-	(1.6)
Operating profit	3	**200.0**	175.1	(14.5)	160.6
Interest payable and similar charges		**(98.3)**	(96.8)	(50.2)	(147.0)
Interest receivable		**29.1**	32.5	7.9	40.4
Share of post-tax profit from joint ventures		**0.3**	0.1	-	0.1
Profit before tax	3	**131.1**	110.9	(56.8)	54.1
Tax on ordinary activities	4	**(37.2)**	(35.0)	18.7	(16.3)
Profit for the year		**93.9**	75.9	(38.1)	37.8
Profit attributable to equity shareholders		**93.9**	75.9	(38.1)	37.8
Earnings per share (pence per share) *	6				
- Basic		**26.5**			9.9
- Diluted		**26.3**			9.8
Proposed dividend per share (pence per share) *****	7	**18.55**			17.2
Proposed dividend for the year (£m)	7	**66.0**			61.0

All operating activities are continuing operations.

* The earnings per share and dividend per share for 2006 have been restated to reflect the sub-division of the Company's ordinary shares by way of a three for one split on 31 July 2006.

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Consolidated statement of recognised income and expense for the year ended 31 March 2007

	2007 (Unaudited) £m	2006 £m
Profit for the year	**93.9**	37.8
Actuarial losses on defined benefit schemes	**(1.2)**	(2.8)
Cash flow hedges		
Net fair value gains	**15.7**	1.0
Tax on items taken directly to or transferred from equity	**0.4**	0.8
Net gains/(losses) not recognised directly in income statement	**14.9**	(1.0)
Total recognised income for the year	**108.8**	36.8
Adjustments on adoption of IAS 32/39 1 April 2005 (net of tax)	**-**	8.6
	108.8	45.4
Attributable to equity shareholders	**108.8**	45.4

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Consolidated balance sheet at 31 March 2007

	Note	2007 (Unaudited) £m	2006 £m
Assets			
Non-current assets			
Goodwill		**134.3**	98.6
Other intangible assets		**7.8**	5.7
Property, plant and equipment		**2,559.4**	2,415.9
Trade and other receivables		**6.9**	6.0
Investments accounted for using equity method		**1.4**	1.3
		2,709.8	2,527.5
Current assets			
Inventories		**5.1**	5.0
Trade and other receivables		**122.5**	94.5
Derivative financial instruments		**16.0**	3.1
Cash and cash equivalents		**127.9**	99.4
		271.5	202.0
Liabilities			
Current liabilities			
Borrowings		**(85.8)**	(54.7)
Derivative financial instruments		**-**	(3.0)
Trade and other payables		**(175.9)**	(170.1)
Current tax liabilities		**(36.5)**	(24.0)
Provisions for liabilities and charges		**(13.2)**	(11.4)
		(311.4)	(263.2)
Net current liabilities		**(39.9)**	(61.2)
Non-current liabilities			
Borrowings		**(1,599.4)**	(1,471.8)
Other non-current liabilities		**(2.1)**	(2.2)
Retirement benefit obligations		**(41.2)**	(41.7)
Deferred tax liabilities		**(313.7)**	(302.8)
Provisions for liabilities and charges	8	**(86.3)**	(66.6)
		(2,042.7)	(1,885.1)
Net assets		**627.2**	581.2
Shareholders’ equity			
Share capital		**144.9**	184.2
Share premium account		**11.7**	10.2
Capital redemption reserve		**143.8**	98.4
Retained earnings and other reserves		**326.8**	288.4
Total shareholders’ equity	9	**627.2**	581.2

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Consolidated cash flow statement for the year ended 31 March 2007

	Note	**2007 (Unaudited) £m**	2006 £m
Cash flows from operating activities			
Cash generated from operations	10	**305.1**	232.1
Interest paid *		**(58.1)**	(128.9)
Tax paid		**(12.0)**	(2.2)
Net cash generated from operating activities		**235.0**	101.0
Cash flows from investing activities			
Interest received *		**6.7**	22.5
Acquisition of subsidiary undertakings (net of Cash acquired)		**(37.0)**	(44.7)
Investment in joint venture		**-**	(1.1)
Return of loan from joint venture		**0.1**	-
Proceeds of business disposal		**-**	5.0
Proceeds from investment disposal		**0.6**	-
Purchase of property, plant and equipment		**(251.4)**	(218.6)
Proceeds from sale of property, plant and equipment		**5.0**	4.8
Net cash used in investing activities		**(276.0)**	(232.1)
Cash flows from financing activities			
Net proceeds from issue of ordinary share capital		**1.9**	1.6
Purchase of ordinary shares		**(3.5)**	-
Purchase of ordinary shares by the Pennon Employee Share Trust		**(2.3)**	-
(Deposit)/release of restricted funds		**(4.1)**	177.1
Net proceeds from new borrowing		**110.0**	182.5
Repayment of borrowings		**(71.1)**	(224.3)
Finance lease drawdowns		**130.2**	141.6
Finance lease principal repayments		**(21.4)**	(15.8)
Dividends paid		**(61.0)**	(34.1)
B Share payments		**(5.7)**	(137.8)
Net cash received from financing activities		**73.0**	90.8
Net increase/(decrease) in cash and cash equivalents		**32.0**	(40.3)
Cash and cash equivalents at beginning of year		**80.3**	120.6
Cash and cash equivalents at end of year		**112.3**	80.3

* Interest paid and received in 2006 included exceptional items, note 5.

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NOTES

1. **Basis of preparation**

These unaudited financial statements have been prepared under the historical cost convention, except for derivative financial instruments, and in accordance with International Financial Reporting Standards and International Financial Reporting Interpretation (IFRIC) interpretations adopted by the European Union, with those parts of the Companies Act 1985 applicable to companies reporting under IFRS and the requirements of the Financial Services Authority.

2. **Financial information**

The financial information for the years ended 31 March 2007 and 31 March 2006 does not constitute full financial statements within the meaning of section 240 of the Companies Act 1985. The full financial statements for the year ended 31 March 2006 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.

3. **Segmental reporting**

	2007 (Unaudited) £m	2006 £m
Revenue		
Water and sewerage	**381.5**	348.5
Waste management	**367.7**	298.9
Other	**7.6**	7.3
Less intra-segment trading *	**(8.5)**	(9.0)
	748.3	645.7
Segment result		
Operating profit before depreciation, amortisation and exceptional items (EBITDA)		
Water and sewerage	**234.5**	213.4
Waste management	**82.8**	66.7
Other	**(1.8)**	(0.9)
	315.5	279.2
Operating profit before amortisation and exceptional items		
Water and sewerage	**156.8**	141.5
Waste management	**46.8**	35.9
Other	**(1.8)**	(0.7)
	201.8	176.7
Operating profit before exceptional items		
Water and sewerage	**156.8**	141.5
Waste management	**45.0**	34.3
Other	**(1.8)**	(0.7)
	200.0	175.1
Operating profit		
Water and sewerage	**156.8**	127.0
Waste management	**45.0**	34.3
Other	**(1.8)**	(0.7)
	200.0	160.6

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NOTES (Continued)

3. **Segmental reporting (Continued)**

	2007 (Unaudited) £m	2006 £m
Profit before tax and exceptional items		
Water and sewerage	**98.9**	87.4
Waste management	**27.6**	21.9
Other	**4.6**	1.6
	131.1	110.9

The exceptional items are detailed in note 5.

* Intra-segment trading between and to other segments by the water and sewerage and waste management segments is under normal commercial terms and conditions that would also be available to unrelated third parties. Intra-segment revenue of the Other segment is at cost.

4. **Tax on profit on ordinary activities**

	2007 (Unaudited) £m	Before exceptional items 2006 £m	Exceptional items (note 5) 2006 £m	Total 2006 £m
Tax on profit on ordinary activities comprises:				
United Kingdom corporation tax	**23.9**	14.8	(18.7)	(3.9)
Deferred tax	**13.3**	20.2	-	20.2
	37.2	35.0	(18.7)	16.3

5. **Exceptional items**

The exceptional items are :	**2007 (Unaudited) £m**	2006 £m
Customer payment	-	(14.5)
Operating profit	**-**	(14.5)
Bond retirement	-	(50.2)
Receipt on transfer of lease	-	7.9
Profit before tax	**-**	(56.8)
Tax arising on exceptional items	-	18.7
	-	(38.1)

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.

NOTES (Continued)

6. **Basic and diluted 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 is adjusted to include all dilutive potential ordinary shares.

A reconciliation of the weighted average number of shares and earnings used in the calculations is set out below :

Number of shares (millions)	**2007 (Unaudited)**	2006 (Restated)
For basic earnings per share	**353.9**	381.9
Effect of dilutive potential ordinary shares :		
Share options	**3.2**	3.3
For diluted earnings per share	**357.1**	385.2

The weighted average number of ordinary shares for 2006 has been restated to reflect the sub-division of the Company's ordinary shares by way of a three for one split on 31 July 2006.

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 :

		2007 Earnings per share (Unaudited)			2006 Earnings per share (Restated)	
	Earnings £m	**Basic p**	**Diluted p**	Earnings £m	Basic p	Diluted p
Earnings per share	**93.9**	**26.5**	**26.3**	37.8	9.9	9.8
Exceptional items (net of tax)	-	-	-	38.1	10.0	9.9
Deferred tax	**13.3**	**3.8**	**3.7**	20.2	5.3	5.2
Adjusted earnings per share	**107.2**	**30.3**	**30.0**	96.1	25.2	24.9

All operating activities are continuing operations.

PENNON GROUP PLC

NOTES (Continued)

7. **Dividends**

	2007 (Unaudited) £m	2006 £m
Amounts recognised as distributions to equity holders in the year :		
Interim dividend paid for the year ended 31 March 2006 : 5.5p (2005 4.6p) per share	**19.4**	17.7
Final dividend paid for the year ended 31 March 2006 : 11.7p (2005 9.7p) per share	**41.6**	37.4
	61.0	55.1

Proposed dividends

	2007 (Unaudited) £m	2006 £m
Proposed interim dividend for the year ended 31 March 2007 : 5.85p (2006 5.5p) per share	**20.8**	19.4
Proposed final dividend for the year ended 31 March 2007 : 12.7p (2006 11.7p) per share	**45.2**	41.6
	66.0	61.0

Dividend per share for 2006 has been restated to reflect the sub-division of the Company's ordinary shares by way of a three for one split on 31 July 2006.

The proposed interim and final dividends have not been included as liabilities in these financial statements. The proposed interim dividend was paid on 11 April 2007 and the proposed final dividend is subject to approval by shareholders at the Annual General Meeting on 26 July 2007.

If approved at the Annual General Meeting the final dividend of 12.7p per share will be paid on 2 October 2007 to shareholders on the register at 10 August 2007. 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 24 August 2007. The final date for receipt of DRIP application forms will be 18 September 2007.

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NOTES (Continued)

8. **Landfill restoration**

At 31 March 2007 landfill restoration provisions recognised with a matching addition to the cost of tangible fixed assets were £43.6m (2006 £32.3m) following a change in accounting methodology in 2006.

9. **Statement of changes in shareholders' equity**

	Share capital £m	Share premium account £m	Capital redemption reserve £m	Retained earnings and other reserves £m	**(Unaudited)** Total £m
Profit for the year	-	-	-	93.9	93.9
Other recognised income and expense for the year	-	-	-	14.9	14.9
Dividends paid	-	-	-	(61.0)	(61.0)
Shares issued for cash consideration	0.4	1.5	-	-	1.9
Shares cancelled and cost of buy back	(0.3)	-	0.3	(3.5)	(3.5)
Deferred shares redeemed	(39.4)	-	39.4	-	-
B Shares redeemed	-	-	5.7	(5.7)	-
Own shares acquired by the Pennon Employee Share Trust	-	-	-	(2.3)	(2.3)
Adjustment in respect of share-based payment	-	-	-	2.1	2.1
	(39.3)	1.5	45.4	38.4	46.0
At 1 April 2006	184.2	10.2	98.4	288.4	581.2
At 31 March 2007	**144.9**	**11.7**	**143.8**	**326.8**	**627.2**

PENNON GROUP PLC

NOTES (Continued)

10. **Cash flow from operating activities**

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

Cash generated from operations	**2007 (Unaudited) £m**	2006 £m
Profit for the year	**93.9**	37.8
Adjustments for:		
Employee share schemes	**2.1**	1.7
Deferred income released to profits	**-**	(0.3)
Profit on disposal of property, plant and equipment	**(2.6)**	(1.1)
Profit on disposal of investment	**(0.6)**	-
Depreciation charge	**113.7**	102.5
Amortisation of intangible assets	**1.8**	1.6
Share of post-tax profit from joint ventures	**(0.3)**	(0.1)
Interest payable and similar charges	**98.3**	147.0
Interest receivable	**(29.1)**	(40.4)
Taxation	**37.2**	16.3
Changes in working capital *(excluding the effect of acquisition of subsidiaries)*		
Increase in inventories	**(0.1)**	(0.3)
(Increase)/decrease in trade and other receivables	**(20.7)**	2.0
Increase in trade and other payables	**16.9**	8.4
Increase/(decrease) in retirement benefit obligations	**2.0**	(39.7)
Decrease in provisions for liabilities and charges	**(7.4)**	(3.3)
Cash generated from operations	**305.1**	232.1

11. **Net borrowings**

	2007 (Unaudited) £m	2006 £m
Cash and cash equivalents	**127.9**	99.4
Borrowings – current		
Bank overdrafts	**(10.9)**	(18.5)
Other current borrowings	**(26.0)**	(8.2)
Finance lease obligations	**(48.9)**	(28.0)
Total current borrowings	**(85.8)**	(54.7)
Borrowings – non-current		
Bank loans	**(350.1)**	(312.7)
Other non-current borrowings	**(215.9)**	(232.2)
Finance lease obligations	**(1,033.4)**	(926.9)
Total non-current borrowings	**(1,599.4)**	(1,471.8)
Total net borrowings	**(1,557.3)**	(1,427.1)

NOTES (continued)

12. **Acquisitions and disposals**

On 13 May 2006 the entire issued share capital of Wyvern Waste Services Limited, (now renamed Viridor Waste (Somerset) Limited), was purchased by Viridor Waste Management Limited for a cash consideration of £25.4m including costs of £0.4m. The acquisition has been accounted for using the acquisition method. Goodwill of £21.8m and intangible fixed assets of £3.6m have been capitalised. The intangible fixed assets are being amortised evenly over the Directors' estimate of useful economic life. Cash balances on acquisition amounted to £3.0m.

On 5 September 2006 Viridor Waste Management Limited disposed of its 15% interest in the issued share capital of Devon Waste Management Limited for a cash consideration of £0.6m.

On 13 February 2007, the entire issued share capital of Skipaway Holdings Limited, (now renamed Viridor Waste (Medway) Holdings Limited), was purchased by Viridor Waste Management Limited for a cash consideration of £15.1m including costs of £0.4m. The acquisition has been accounted for using the acquisition method. Provisional goodwill of £13.9m and intangible fixed assets of £0.3m have been capitalised. The intangible fixed assets are being amortised evenly over the Directors' estimate of their useful economic life.

13. The Annual Report for 2006/07 will be posted to shareholders on 26 June 2007 and will be available for viewing on the Company's website at www.pennon-group.co.uk on 27 June 2007.

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