

Regulatory Story

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Company Pennon Group PLC
TIDM PNN
Headline Final Results
Released 07:00 03-Jun-2014
Number 6526107



RNS Number : 6526I
 Pennon Group PLC
 03 June 2014

PENNON GROUP PLC**3 June 2014****PRELIMINARY RESULTS FOR THE YEAR ENDED 31 MARCH 2014**

Pennon Group announces its unaudited results for the year ended 31 March 2014.

A presentation for City audiences will be held today, Tuesday, 3 June 2014, at 9am at Haberdashers' Hall, 18 West Smithfield, London, EC1. A live webcast of the results presentation will be available at pennon-group.co.uk/investor/presentations and a recording of the presentation will be available thereafter.

For further information today, 3 June 2014, please contact :

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FINANCIAL HIGHLIGHTS

- Profit before tax^{(1) (2)} up 9.1% to £207.3m
 - South West Water up 10.8% to £162.5m
 - Viridor down 19.5% to £27.6m
 - Viridor PBIT + JVs down 4.6% to £43.6m
 - Viridor EBITDA down 1.8% to £76.3m
- Net exceptional charges £48.6m (post tax £39.7m)
- Earnings per share^{(1) (3)} up 5.7% to 42.6p
- Dividend
 - Full year dividend up 6.5% to 30.31p
 - Recommended final dividend per share up 6.2% to 20.92p
- Strong liquidity and funding position
 - £640m new/refinanced facilities since 31 March 2013
 - £1,303m cash/committed facilities at 31 March 2014
 - Average cost of debt reduced to 3.8%

- Substantial progress in delivery of major capital programmes
 - South West Water capex up 22% - target efficiencies delivered
 - Viridor - 70% of spend now complete on EfW projects under construction
- Group businesses well positioned for the future

(1) Comparatives restated for IAS 19 (Revised)

(2) Before net exceptional charges of £48.6m (post tax £39.7m). Statutory profit before tax £158.7m

(3) Before net exceptional charges and deferred tax. Basic earnings per share (statutory basis) 38.8p

OPERATIONAL HIGHLIGHTS

- **South West Water:**
 - Strong performance against 2010 - 2015 (K5) regulatory contract
 - Well placed to deliver outcomes and outperform
 - Robust operational performance, despite extreme weather, and improving standards of customer service
 - Strong performance against bathing water compliance
 - Further improvement in SIM⁽¹⁾ performance
 - PBT up due to
 - Higher revenue and good cost control
 - Average funding cost 3.8%
 - Business Plan for 2015-2020 (K6) achieved 'enhanced' status
 - Only water and sewerage company to achieve Ofwat's top assessment
 - Financial benefits from enhanced status
 - Draft Determination already received
 - Enabling early K6 implementation

(1) Service Incentive Mechanism

- **Viridor:**
 - Excellent continuing progress in strategic re-orientation of Viridor business model
 - Financial performance⁽¹⁾ delivered in line with management expectations
 - PBIT plus joint ventures broadly similar to 2012/13
 - Substantial recovery in recycling margins, supported by focus on costs, but remain cautious about future prospects.
 - Landfill energy - focus on reducing landfill operations and optimising energy production
 - Focus on strategic sites for residual landfill
 - Maximising value of landfill gas generation
 - Development of alternative uses for closed sites including new energy opportunities
 - Significant developments in long term Energy from Waste (EfW) business
 - Circa 80% of the waste inputs required at opening secured, of which circa 60% is from long term contracts
 - Runcorn I and Exeter - burning waste
 - Ardley in commissioning
 - Runcorn II and Cardiff - shortly to enter commissioning
 - South East Wales residual waste project (Prosiect Gwyrdd) - signed December 2013
 - Glasgow and Peterborough under construction

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- South London Waste Partnership PPP (Beddington) - planning secured but "Notice to Proceed" delayed due to expected judicial review

(1) Before net exceptional charges

Ken Harvey, Chairman said:

"This has been a year of significant achievements for the Group.

"South West Water is continuing its strong performance against the 2010-2015 regulatory contract and is well placed to outperform its assumptions. The company continues to deliver robust operational performance and improving standards of customer service, notwithstanding the dry summer of 2013 and then the extreme weather and resultant flooding of last winter. I am delighted that the quality of South West Water's Business Plan was such that it was awarded 'enhanced' status in the 2014 price review - the only water and sewerage company to achieve this. As a result we received our fast tracked Draft Determination for 2015-2020 on 30 April which will enable early implementation of key elements of the Business Plan.

"Financial performance at Viridor before exceptional items has been in line with management expectations. Notwithstanding the difficult trading conditions, Viridor's operating contribution is slightly ahead of last year and PBIT plus joint ventures is broadly similar to last year. The company has made excellent progress in establishing its Energy from Waste (EfW) business which will transform Viridor into a leading player in the UK renewable energy sector. The EfW contracts and projects already contribute to Viridor's bottom line and reflect the realisation of a strategy which is expected to contribute circa £100m to Viridor's EBITDA within the next three years."

GROUP OVERVIEW⁽¹⁾

- Revenue up by 10.0% to £1,321m
- Operating profit⁽²⁾ up by 4.8% to £257.5m
- Net interest payable⁽²⁾ down by 12.2% to £53.9m
- Profit before tax⁽²⁾ up 9.1% to £207.3m. Profit before tax (statutory basis) £158.7m
- Net exceptional charges post tax of £39.7m reflecting a further impairment of landfill assets and additional environmental provisions
- Earnings per share up by 5.7% to 42.6p.⁽³⁾ Basic earnings per share (statutory basis) increased from 5.7p to 38.8p

- Capital investment⁽⁴⁾ down 1% to £434m
- Net borrowings £2,194m, an increase of £185m since 31 March 2013. Gearing, being net borrowings to (shareholders' funds plus net borrowings), was 65% (2012/13 - 65%). Net debt includes £663m for EfW plants under construction (Runcorn II, Oxford, Exeter, Cardiff and Glasgow)
- Substantial cash resources and committed facilities of £1,303m⁽⁵⁾ to fund future investment
- South West Water net debt to RCV was 55.6% (31 March 2013 - 54.9%)
- Net interest cover (excluding pensions net interest, IFRIC 12 contract interest receivable, discount unwind on provisions and exceptional items) was 5.2 times (2012/13 - 4.1 times)

(1) Comparatives restated for IAS 19 (Revised)

(2) Before net exceptional charges

(3) Before net exceptional charges and deferred tax

(4) Including construction spend on service concession arrangements

(5) Including £173m deposits with Letter of Credit providers and lessors

DIVIDENDS

The Board has recommended a final dividend of 20.92p, up 6.2%, subject to shareholder approval at the Annual General Meeting. Together with the interim dividend of 9.39p, this will result in a total dividend for the year of 30.31p, an increase of 6.5%⁽¹⁾. This is in line with the previously announced sector leading policy to grow the Group dividend by 4% above inflation per annum up to the end of 2014/15.

The final dividend will be paid on 3 October 2014 to shareholders on the register on 8 August 2014. The Company is also intending to offer a scrip dividend alternative, subject to obtaining shareholder approval at this year's Annual General Meeting. If approved, the final date for the receipt of Forms of Election/Mandate in respect of the scrip dividend alternative for the final dividend will be 15 September 2014.

The Board will review the dividend policy for the K6 period following the Final Determination for South West Water and will make an announcement at the 2014/15 Preliminary Results.

(1) RPI for the twelve months to 31 March 2014 was 2.5%

SOUTH WEST WATER

Despite the extreme weather during the year - a hot dry summer followed by storms over the

winter - South West Water continued to deliver good operational performance against the K5 (2010-2015) regulatory contract alongside further improvements to customer service. This was reflected in strong financial results - the result of revenue growth, good cost control and continued efficiency delivery.

In December 2013, South West Water submitted its business plan to the Economic Regulator, Ofwat. The plan was balanced, well evidenced, well supported and met or exceeded all of Ofwat's assessment areas. We were pleased Ofwat assessed the company business plan as 'enhanced', being the only water and sewerage company plan to achieve the top assessment.

A Draft Determination was received on 30 April. This early Draft Determination puts South West Water in a strong position and allows accelerated delivery of key projects. South West Water's track record in delivering efficiency and outperformance provides a strong platform for implementing the plan with the potential to enhance returns on equity.

Financial Highlights

South West Water's operating profit increased by £12.2m (5.7%) to £227.0m.

Revenue increased 4.3% to £520.0m as a result of tariff increases, new connections and higher other sales, offset by an overall reduction in demand and the effects of customers switching to a metered tariff. Approved tariff increases, including the 1.3% K factor, amounted to £25.0m and 6,000 new customer connections contributed £3.7m of additional revenue. 10,100 customers switching from unmeasured to metered charging or assessed charges reduced revenue by £6.5m. Customer demand has fallen by 1.0% from last year, a lower reduction than previous years reflecting the dry summer experienced in 2013. The fall in demand reduced revenue by £2.8m with the largest impacts seen within commercial customers. 78% of South West Water's domestic customers are metered.

Operating costs, including depreciation and restructuring costs, increased by 3.2% from £283.8m to £293.0m, below the allowed price rise of 4.3%. The key movements in costs were:

- £9.0m cost increases (including power, business rates and pension costs). Cumulative cost increases over K5 continue to be lower than average RPI for the same period
- £2.0m increased depreciation and costs of new capital schemes
- £1.8m increased cost of sales from increased developer services and other sales activity
- (£3.6m) additional efficiencies delivered in the year. Cumulative K5 efficiency to date is 14% ahead of target as a result of early delivery.

South West Water's programme of organisational restructuring was weighted towards the beginning of K5. Ongoing operational and organisational changes have continued during 2013/14 with costs of £0.5m (2012/13 - £0.5m).

The net interest charge of £64.5m is lower than 2012/13 (£68.1m; before exceptional net income) predominantly as a result of lower RPI on index-linked facilities.

Excluding exceptional items from the prior year profit before tax increased by 10.8% to £162.5m.

Capital expenditure in the year was £141.6m compared to £116.5m in 2012/13. The increase was driven by key quality schemes and the delivery of additional capacity to meet future growth.

Regulatory net capital expenditure⁽¹⁾ was £160.6m. The focus for the programme remains weighted towards the maintenance of existing assets, increasing infrastructure resilience and delivering environmental improvements. Investments during the year included:

- Improvements in water quality with treatment upgrades at two key sites including Restormel which provides 50% of the water for Cornwall
- Investments in assets to improve bathing water quality to meet revised European Guidelines in 2015
- Delivering additional capacity to meet growth - including supply to two new towns within the region

- Focusing on compliance at waste water sites to manage periods of extreme weather conditions
- Safeguarding water resources - upgrades to four reservoirs across the region
- Innovative investments to reduce flooding for those customers previously highlighted as at risk.

⁽¹⁾ capital expenditure including infrastructure renewals expenditure less grants and contributions

The robustness of our networks and assets is illustrated by South West Water achieving Ofwat's 'stable serviceability' status across all areas.

Regulatory capital value at 31 March 2014 was £2,959m and with an increase in net debt this has led to gearing of 56% (31 March 2013: 55%) - within Ofwat's optimum range for K5.

Increased projected RCV growth of 19% by 2020⁽¹⁾ in K6 reflects the Draft Determination including enhanced assessment benefits.

⁽¹⁾ nominal prices, RPI 3.2% assumed

Efficiencies

South West Water remains ahead of target in delivering the required operating cost efficiencies for K5.

The company has front end loaded delivery of the required 2.8%⁽¹⁾ pa average operating cost efficiencies. Cumulatively, the efficiency delivered for the four years of K5 is 14% ahead of target as a result of early delivery. Annual operating costs are £22.2m lower as a consequence, with £3.6m cost savings delivered in 2013/14. This is being achieved through South West Water's ongoing improvement programmes with specific initiatives this year in the areas of

- Operational ways of working - integration of customer services management and

- asset improvements through the PUROS⁽²⁾ programme
- Energy procurement and usage - energy efficiency schemes alongside additional power generation through renewable sources
- Rationalising administration and support services
- Right-sourcing and innovative contracting - tendering to achieve the 'right price'.

South West Water continues to deliver capital projects in line with Ofwat, Drinking Water Inspectorate and Environment Agency expectations. Expenditure for the K5 period to date is lower than the Capital Incentive Scheme baseline⁽³⁾ and is targeted to achieve 5% outperformance of the Final Determination K5 capital programme⁽⁴⁾. Performance cumulatively to date is in line with expectations.

As outlined previously, South West Water has historically shared the benefits of financial outperformance with customers through re-investment of efficiency and accelerated capital expenditure. The strong operational and financial outperformance to date in K5 is allowing an additional £60m to be invested during the period to improve services to customers, including:

- Upgrading assets in key bathing waters by accelerating capital investment
- Maintaining and enhancing customers private sewers since October 2011
- Tackling customer affordability through debt initiatives.

(1) average over K5 (2010-2015)

(2) PUROS - Phased Utilisation of Remote Operating Systems

(3) based on current published Construction Output Price Index (COPI)

(4) using 2009 Final Determination estimates of COPI

Operational Highlights

The 'Pure Water, Pure Service, Pure Environment' strategy is the cornerstone of South West Water's operations, targeting robust operational performance and high standards of customer service underpinned by strong financial results.

Pure Water

A significant proportion of the company's capital programme is focused on maintaining drinking water quality including an upgrade to its largest water treatment works - Restormel - which provides water to 50% of customers in Cornwall. The delivery of a high level of water quality is fundamental to South West Water's business and compliance of 99.98% was achieved this year in accordance with the tough standards set by the Drinking Water Inspectorate.

South West Water is continuing to deliver industry-leading leakage performance. Leakage targets have been met every year since their introduction.

Despite the drier weather over the summer period, South West Water successfully managed its water resources to enable a continued secure supply of water for the region, resulting in the 17th consecutive summer without a hosepipe ban or drought order. In addition the company is confident that no water restrictions will need to be put in place during 2014/15.

Work continues on South West Water's innovative catchment management programme known as 'Upstream Thinking'. Designed to improve raw water quality and natural water storage in the landscape through improvements to agricultural land and moorland areas, the project remains on track to deliver the required activities for K5.

The project has been recognised for leading the way in business sustainability and for its positive environmental impact. This year it won the 'Living Wetlands Award' from the Chartered Institution of Water and Environmental Management (CIWEM).

Pure Service

South West Water's emphasis on service is delivering tangible improvements for customers. The improving trend has seen South West Water's customer service score (as measured by the Service Improvement Mechanism (SIM)) almost doubled from the opening 2010/11 position for the K5 period, achieving its highest ever qualitative score in quarter four this year.

South West Water continues to build on strategic investment made during the K5 period, such as using its customer relationship system to manage customer contacts through to first time resolution and providing online offerings such as 'My Account' account management and smartphone apps. In addition South West Water is working with the Institute of Customer Service (ICS) to invest in external benchmarked training for staff.

The cost of bad debts is comparable with 2012/13 although the charge, as a proportion of revenue at 1.8%, is a reduction on the previous year. Collection initiatives to further improve the bad debt position include using tracing tools to target former occupiers of newly vacated properties. South West Water continues to fund and promote ways to help customers who struggle to pay their debt through initiatives such as the Restart programme which incentivises customers into regular payment plans. South West Water is one of the few companies to have successfully introduced a social tariff 'WaterCare' during 2013/14 which has already assisted 1,100 customers in the region by reducing their bills to an amount they can better afford to pay. In addition, the implementation of the £50 Government payment was successfully managed for all eligible household customers.

Pure Environment

The 2013 bathing season ended with the best bathing water quality results for seven years, with 132 (91%) of the region's beaches achieving the EU guideline standard (excellent status) and 144 (99%) of beaches achieving the mandatory standard (good status). This is a significant improvement on last year's results when 88 (60%) achieved the guideline and 133 (91%) the mandatory standards.

South West Water is committed to working with other organisations and local communities so that residents and visitors alike can continue to enjoy the region's beautiful beaches:

- The award winning 'Beach Live' service continues to provide beach users with real-time information about bathing water quality with new feeds and features implemented. The number of beaches included has doubled since the service started in 2011.
- South West Water has committed to spend up to £18m on a range of schemes to improve bathing water quality ahead of the European Union's Revised Bathing Water Directive coming into force in 2015.

Following an increase last year in the number of operational incidents giving rise to internal sewer floodings due to extreme wet weather, the company has achieved a major improvement in these results and incidents have fallen from last year, despite the storms and fluvial flooding which occurred over winter 2013/14.

Known as 'Downstream Thinking', a series of pilot schemes are set to be rolled out later this year through cost-effective measures designed to reduce the impact of wet weather on our sewer network and assets.

South West Water has maintained its investment in renewable energy, bringing the total expenditure for K5 to over £4m. Solar energy represents a significant proportion of this expenditure, delivering over one million kilowatt hours of solar energy generated last year.

The company has continued its good performance against a number of Ofwat's Key Performance Indicators (KPIs). Customer service, reliability and availability of supply (including leakage) and greenhouse gas emissions all achieved 'green' status.

Further improvements and investments are targeted at reducing waste water pollution incidents and improving treatment compliance at waste water works, both of which disappointingly fell short of the company's targets this year.

Regulatory and Political Developments

2015-2020 Business Plan

On 2 December 2013 South West Water submitted its K6 (2015-2020) business plan and following Ofwat's risk based review, on 4 April 2014 Ofwat assessed the plan as 'enhanced'. An early Draft Determination was received on 30 April 2014. The Final Determination will follow on 12 December 2014.

The business plan was balanced, well evidenced and well supported and met or exceeded all of Ofwat's assessment areas.

Ofwat commended South West Water on "*achieving enhanced status through an excellent business plan and strong management*". It acknowledged that South West Water had "*risen to the challenge set by the regulatory approach for the 2014 price review*" and the business plan was one "*which can be considered by other companies as an example of good practice*". The Environment Agency "*welcomed the commitment made to meet environmental obligations*".

The benefits received from the 'enhanced' assessment include an initial financial award of £11m reflected as an addition to the RCV with up to 50% reinvested; an enhanced Totex menu with an extra 5% enhanced sharing rate and a 'do no harm' principle as Ofwat and the company work towards the Final Determination.

The 'do no harm' principle ensures that enhanced companies that deliver their business plans should be better off overall than other companies. Examples would include Ofwat policy decisions on the cost of capital and changes in statutory obligations.

The cost bases for both water and waste water have been assessed as efficient and below Ofwat's calculated baseline, resulting in an additional £47m allowed expenditure plus £8m menu incentive award. Investor returns are in line with Ofwat's risk reward guidance issued in January.

The key elements of the Draft Determination for K6 are:

- Appointee vanilla WACC⁽¹⁾ of 3.85%, (3.7% WACC for wholesale only)
- Retail margins of 1.0% and 2.5% for retail household and non-household respectively, equivalent to an RCV return of 0.2%
- Equity returns up to 10% from outperformance of cost base, outcome delivery incentives (ODIs) and financing
- £47m additional allowed expenditure from cost base assessment plus £8m menu incentive award
- RCV growth of 19%⁽²⁾ and no adjustments to the planned K6 capital investment programme of £868m⁽³⁾.

⁽¹⁾ pre tax debt and post-tax equity weighted average cost of capital

⁽²⁾ nominal prices assuming 3.2% pa RPI

⁽³⁾ 2012/13 price base

The company is confident that it can deliver the plan with its track record on outperformance and targeted outcome delivery. There continues to be a challenging but deliverable opportunity for South West Water to outperform the business plan targets and enhance equity returns in K6 through the incentives regime in place.

Customers and the South West region will benefit from the planned improved services and enhancements to the environment. Customers will also benefit from tariffs being frozen in 2014/15, without loss of shareholder value, and the level of average household bills tracking below projected inflation to 2020.

The plan included the following objectives for K6:

- Keep price rises below inflation
- Deliver efficiency through innovation to keep costs and customers bills as low as possible
- Share benefits of success fairly between customers and investors

- Make significant improvements to frontline customer service
- Deliver service and environmental improvements
- Support sustainable regional growth.

Receiving the milestone of a Draft Determination early allows a swift and smooth transition into the K6 period including accelerated delivery of a number of key projects (e.g. bathing water improvements) ahead of significant legislative changes.

Water Act

The new Water Act became a statute on 14 May 2014. As well as setting out a range of reforms for the water sector in England, the Act enables further retail and wholesale competition. Preparations are under way for the retail market opening in April 2017.

South West Water is fully engaged in the 'Open Water' programme, governed by the Department for Environment, Food and Rural Affairs and Ofwat, which will shape market reform in the sector.

Building on the success of the 'Source for Business' range of specialist advice and support measures, the company has been awarded supply licences covering Scotland, England and Wales, which will allow it to retail water to customers outside the region currently served.

South West Water Outlook

South West Water continues to focus on efficient service delivery, improvements in service to customers and the satisfaction of its regulatory and legislative obligations. It is on track to outperform the K5 regulatory contract. 2014/15 profits will be impacted by the 2014/15 tariff freeze already announced. However, the revenues foregone have been taken account in the Draft Determination for K6 on an NPV neutral basis.

With an 'enhanced' business plan for K6, South West Water has already received the Draft Determination for the 2015-20 period. The company is engaged in the development of Ofwat's ongoing regulatory reform agenda and is well positioned for future Government legislative changes.

VIRIDOR

Excellent progress is being made in the strategic re-orientation of the Viridor business model and Viridor is now at the forefront of transforming waste in the UK. The company is building its business by putting waste into action: transforming it into high quality recyclate, raw materials and energy.

Viridor's strategy, **"transforming waste"**, is to add substantial value through

- Recycling. Viridor has substantially increased its recycling business over the past five years. It currently handles volumes approaching 2m tonnes per annum. The focus for recycling activities is on the production of high quality materials, and management of the cost base to improve margins

- Waste-based renewable energy generation. The focus of the landfill energy business is
 - to maximise the value of landfill gas generation across all sites
 - to manage the expected decline in landfill inputs by concentrating on strategic operational sites and
 - to optimise returns on others through alternative uses such as photovoltaic installation
- Public Private Partnership (PPP)/Energy from Waste (EfW). Viridor is continuing to make strong progress on the construction of its growing PPP/EfW asset base - the next phase of the Viridor strategy - with operations expected to commence at five facilities in 2014/15. EfW is central to the UK's waste and renewable energy strategies as the long term low cost alternative to landfill for disposal of residual waste. Viridor expects to have 15% EfW market share by 2020 with a network of strategic facilities which will drive the company's long term profit growth.

An organisational restructuring has recently been implemented to drive, and where possible accelerate, the delivery of the Viridor strategy. Two operating divisions have been created: Recycling & Resources (comprising recycling, contracts and collection); and Energy (comprising EfW, landfill energy and other renewable power).

Financial Highlights

Revenue was up 14.0% to £802.0m. Recycling revenue decreased £17.1m due to lower prices, landfill was up £43.1m due to higher landfill tax, and construction revenues were up reflecting growth in assets under construction.

Before exceptional charges Viridor's earnings before interest, tax, depreciation and amortisation (EBITDA) for the year was broadly flat at £76.3m (2012/13 - £77.7m). PBIT fell £0.4m (1.3%) to £30.2m. PBIT plus joint ventures decreased by £2.1m (4.6%) to £43.6m.

Profit before tax and exceptional charges decreased £6.7m (19.5%) to £27.6m reflecting lower PBIT plus joint ventures and the increased interest charge from higher provisions.

Capital expenditure including spend on service concession arrangements for the year was £292m (2012/13 - £324m) of which circa £254m was for Viridor growth projects (largely EfW) with the balance being maintenance of existing assets.

Exceptional charges

The profitability of the landfill business has declined faster than anticipated due to aggressive pricing from other landfill operators (in response to local authority austerity and increasing levels of landfill tax) who are competing for volume to allow closure of their sites with suitable landforms, and higher ongoing capital costs.

Whilst there will always be a need for strategically located landfill sites, Viridor expects these trends to continue for the foreseeable future. As a result a net pre-tax exceptional impairment charge of £42.9m has been recognised to write-down the carrying value of landfill property, plant and equipment. The impairment charge has no immediate cash impact.

Landfill provisioning has been increased by £5.7m due to revisions to site life costings.

Operational Highlights

UK context

The UK is required under the EU Landfill Directive to reduce the amount of biodegradable municipal waste going to landfill sites. This is being achieved by a major increase in recycling, with residual waste increasingly being used for energy recovery. Energy recovery from waste (both biodegradable and non-biodegradable) accounted for 8% of total UK renewable energy generated in 2012. Viridor believes that by 2020, UK energy recovery from waste could produce 15 Terawatt hours (TWh) of the total forecasted UK renewable energy generation (120 TWh), accounting for 12%. This is particularly significant given predicted future energy capacity shortages.

The Government's main mechanism for diverting waste from landfill and incentivising recycling and EfW facilities remains landfill tax. The Government has confirmed that landfill tax will rise in line with inflation from 1 April 2015 from the current position of £80 per tonne. This continues to influence the long term economics of both recycling and energy recovery. In addition, recycle costs are typically significantly lower than the cost of using virgin materials for manufacturers.

Viridor is clearly focussed on recycling and waste based renewable energy. Investment in technology and operational practices has been successfully made to enhance recycle quality to differentiate Viridor from its competitors. Significant progress has also been made in the development of the EfW business, with a substantial asset base being constructed in conjunction with the development of the associated business capability processes across the whole "source to supply" EfW production.

Recycling and Resources

During the year recycling volumes traded decreased marginally by 63k tonnes (3.0%) to 1.8m tonnes. Recycle prices have stabilised to some degree for most commodities but remain under pressure, reflecting world economic conditions, competitive markets and, in the near term, higher shipping costs. Overall average revenues per tonne from recycle sales and gate fees for the year fell to £93 per tonne, 6.1% lower than for 2012/13.

Action has been, and continues to be, taken to reduce the cost base with average cost per tonne reduced to £83 from last year's total of £93, including the impact of circa £3 per tonne from the 2012/13 impairment charge. Allied to an emphasis on the production of high quality recycle, the business is now benefitting from improvements in margins. The company remains cautious on the prospects for recycle prices and therefore continues to focus on revenue optimisation and facilities rationalisation/cost reduction. Investment is also being made in technology with a new plastic/polymer separation plant at Rochester, costing circa £15m, and a new glass processing plant in Scotland, costing circa £10m. These investments, which are due to become operational in Autumn 2014, will enable Viridor to enhance product quality and continue to differentiate itself in the sector. Viridor now has the most extensive Materials Recycling Facility (MRF) capacity in the UK with accreditations for export to China and is established as a quality brand in other Asian markets.

Profits in "Contracts & Other" were up overall across the 15 local authority contracts around the UK (the more significant contracts include Greater Manchester, Lakeside, Glasgow, Lancashire, Somerset and West Sussex) and the Thames Water contract. The increase also reflected higher profits on property sales. Profits in the collection business were also ahead, reflecting increased management action.

Additional contracts have been won since the year end but profits in H1 2014/15 are expected to be impacted by the expiry of some old contracts.

Renewable Energy

Energy can be recovered in two ways, either via gas (notably landfill gas and AD) or combustion in EfW plants and similar facilities, some of which may be a part of Combined Heat and Power (CHP) schemes. Bioenergy (including landfill gas, biodegradable EfW and Anaerobic Digestion (AD)) and energy recovery from non-biodegradable waste, accounted for 39% of total UK renewable energy in 2012.

(a) Landfill gas power generation

Profit from gas generation was £30.1m, an increase of 26.5% on 2012/13.

Viridor's landfill gas power generation output fell 2.0% to 606 Gigawatt hours (GWh) after reaching peak output in 2012/13 and is expected to reduce gradually over the coming years. However, average revenue per Megawatt hour (MWh) increased reflecting the switch from legacy Non Fossil Fuel Obligation (NFFO) contracts to Renewables Obligation Certificates (ROCs) and average prices therefore increased by 9.2% to £89.74 per MWh. Total landfill gas power generation operational capacity declined 2MW to 105MW (excluding 3MW capacity at sub-contract sites in Suffolk). The proportion of operational capacity eligible for ROCs increased to 85%, with the remaining 15% being on (lower priced) NFFO contracts. Circa 30% of the remaining NFFO contracts migrate to ROCs during 2014/15 with the balance moving across by 2016/17.

Average costs were reduced by 8.4% to £40.05 per MWh, with a continuing focus on managing the cost base.

(b) Energy from Waste (EfW) and Anaerobic Digestion (AD)

As well as the 105MW of landfill gas capacity, Viridor has a further 31MW of renewable energy capacity across its share of the Lakeside EfW, the Bolton EfW facility, the Greater Manchester AD operations and the new Walpole AD plant. In addition, the Exeter EfW plant delivered its first electricity to the Grid after the year end and will generate a further circa 3MW when fully operational.

In addition to the above operational projects, Viridor is pursuing a number of other renewable energy opportunities. Most notably, the company has been successfully implementing its strategic plan to develop the EfW business which will drive long term profit momentum. This includes establishing a significant asset base of EfW plants. Viridor and its partners have a total operational/committed EfW capacity of 2.5m tonnes.

Five plants, being Runcorn I and II, Exeter, Ardley (Oxfordshire) and Cardiff, have reached advanced stages of build with all expected to come on-stream in financial year 2014/15. Two others, Glasgow and Peterborough, commenced construction in the year. 70% of spend on EfW projects under construction is now complete.

At the start of 2014, there was a successful appeal to have the planning restriction on road-borne waste inputs to both phases of Runcorn lifted from 85,000 to 480,000 tonnes pa. Planning consent for the Beddington EfW was issued in March 2014 with 'Notice to Proceed' delayed pending an expected judicial review.

As part of the strategy of continuing to secure waste for the EfW plants, the South East Wales residual waste project (Prosiect Gwyrdd) was signed in December 2013. Viridor has now secured circa 80% of the required waste inputs for the opening of the committed plants, of which circa 60% is from long term contracts.

Viridor has also reached the final bid stage as one of two bidders on the Edinburgh and Midlothian residual waste contract.

The Walpole AD plant, which has a 1MW export capacity, is now producing power. A further 'closed loop' opportunity to use digestate as a biofertiliser is being assessed with the Environment Agency.

Joint Ventures

Total joint ventures' contribution (comprising Lakeside, VLGM and TPSCo), which consists of interest on shareholder loans and share of profit after tax, fell 11.3% to £13.4m (2012/13 - £15.1m) due mainly to the previously reported extended outage at Lakeside.

(a) Lakeside

Lakeside, the first of Viridor's EfW pipeline projects, continues to perform very strongly and is ahead of original expectations in terms of both waste throughputs and energy output. The 2013/14 contribution was £5.9m, comprising interest receivable on shareholder loans unchanged at £1.4m and share of profit after tax from Lakeside £4.5m (down £1.3m on the previous year reflecting higher outage costs). A further £2.9m contribution came from the sub-contract profit (included in the contracts segment above).

(b) Viridor Laing (Greater Manchester) (VLGM)

The 25 year Greater Manchester Waste PFI contract (being delivered through VLGM) is the UK's largest ever combined waste and renewable energy project. VLGM is a joint venture between Viridor and John Laing Infrastructure. Operation of the associated facilities (both existing facilities and those which are to be developed) is being carried out on a sub-contract

basis by Viridor.

As reported previously, solid recovered fuel produced from the waste will be used to generate heat and power at a plant being built at Runcorn in Cheshire. Phase I is being built primarily for the Greater Manchester Waste PFI contract.

As part of the VLGM contract, a separate contractor was mandated to construct 43 facilities. As at 31 March 2014, 42 of these facilities had been formally taken over by Viridor. The 43 facilities include 4 mechanical biological treatment (MBT) plants. Three of these MBTs have been taken over and the remaining one is substantially complete, but has not yet been taken over due to isolated process elements not performing satisfactorily. The delay in takeover of the remaining plant continues to be addressed and is not expected to affect the financing of the project or have a material impact on the performance of the PFI.

Interest receivable on shareholder loans from the VLGM joint venture was £5.3m, up £0.2m (2012/13 - £5.1m). Share of profit after tax from VLGM on an IFRIC 12 basis was a loss of £0.5m, down £0.5m due to a reduction in construction margin profits as construction completes.

(c) Runcorn I (TPSCo)

Interest receivable on shareholder loans from the Runcorn I EfW joint venture was £3.0m, up £0.2m on 2012/13. Share of profit after tax was a loss of £0.3m, down £0.3m on 2012/13.

As flagged in the Interim Management Statement of 14 February 2014, hot commissioning at Runcorn I has now commenced on site and first burn of waste occurred in March 2014 and continues on schedule. Full testing of rail operations has been completed and rail-borne fuel transfer from Greater Manchester is now operational. Viridor does not expect previously outlined delays to have a material impact on the completion and operation of the Greater Manchester PFI or TPSCo.

Landfill

The business continues to be strongly cash generative and contributed £25.3m to EBITDA in the year. Volumes increased marginally (0.8%) to 2,739k tonnes over the year.

However, profits are continuing to decline with average gate fees down by 9.0% to £23.06 per tonne in the year and costs up 19.4% to £21.90 per tonne as a result of higher provisioning.

This trend decline is expected to continue. As advised above, a net exceptional impairment charge of £42.9m has been recognised to write-down the carrying value of landfill property, plant and equipment.

Landfill tax, which is passed directly to the customer, increased to £72 per tonne in April 2013, £80 per tonne in April 2014, and will increase by inflation from 1 April 2015. Consented landfill capacity reduced from 61.5 million cubic metres (mcm) at 31 March 2013 to 58.0mcm at 31 March 2014, reflecting usage during the period. As previously stated and provided for, 39mcm is not expected to be used.

The business plan now being implemented will see operations reduced to a few strategic landfill sites, reflecting the ongoing need for landfilling of certain materials for the foreseeable future. Other sites are being run to closure with an emphasis on maximising the value of electricity

generation from landfill gas. Operations and management are being streamlined across the combined landfill and gas generation facilities.

Future alternative uses for sites are now also being assessed in detail. Early success has been achieved at Westbury with planning permission granted for a 2.75MW photovoltaic installation and construction to begin shortly. In addition an £8m partnership with, and fully funded by, the Department of Energy and Climate Change to deliver a demonstration cryogenic power plant has been signed and construction is scheduled to commence in the next quarter.

Indirect costs

Indirect costs increased by 6.1% from £52.4m to £55.6m due mainly to increased information technology and staffing costs to support systems replacement across the business.

Viridor Outlook

Viridor continues its transformation from predominantly a landfill operator to being one of the country's leading recycling, renewable energy and waste management companies.

While there are some signs of improving economic trends, the company remains appropriately cautious about the future prospects for recycle prices. Viridor remains strongly focused on a stringent programme to optimise revenues and achieve efficiencies through facilities rationalisation/cost reduction to sustain margin improvement.

Excellent progress has been achieved in the realisation of the EfW business. Five major facilities are due to become operational in the current financial year while two others started construction in 2013/14 and the Beddington facility recently gained planning permission.

Viridor's H1 EBITDA figure in 2014/15 is expected to be materially lower than in H1 2013/14 (primarily due to the expected continuation of landfill decline but also the gradual decline in power generation and the near term recycling and contracts factors noted above). However the EfWs coming on stream this year are expected to boost H2 EBITDA and result in 2014/15 full year EBITDA exceeding 2013/14. These assets represent a strategic EfW portfolio which is already making a significant contribution to Viridor's bottom line and reflect the realisation of a strategy which is expected to contribute circa £100m to Viridor's EBITDA within the next three years.

GROUP FINANCIAL POSITION

The Group funding strategy utilises a mix of fixed, floating and index-linked rate borrowings. A substantial portion of debt is finance leasing which provides a long maturity profile and secured credit margins.

Group net debt increased from £2,009m to £2,194m. Gearing remains stable. Group gearing⁽¹⁾

was unchanged at 65%. This includes £663m (2013/14 £438m) for EfW plants under construction (Runcorn II, Exeter, Ardley, Cardiff and Glasgow). South West Water debt to RCV increased marginally from 55% to 56%.

The Group has fixed, or put in place swaps to fix, the interest rate on at least 50% of South West Water's net debt for the entire K5 period. The average rate achieved on fixed rate debt is 3.5%. In addition, £388m of South West Water's debt is index-linked at an overall real rate of 1.7%. The average interest rate for both Pennon Group and South West Water for the year to 31 March 2014 was 3.8%.

Before prior year exceptional net finance income, Group net finance costs decreased by £7.5m to £53.9m from £61.4m (restated for IAS 19 (Revised)). This reduction reflects an £8.2m increase in capitalised interest. The overall interest cost on borrowings remained broadly unchanged compared to last year, due primarily to net cash outflows in the year being funded by the £300m hybrid capital securities raised in March 2013. The associated £15.6m (net of tax) hybrid capital periodic return, paid in March 2014, has been recognised directly in equity.

The Group had a strong liquidity and funding position as at 31 March 2014, with £1.3bn cash and committed facilities comprising

- £613m cash balances (including £173m restricted cash)
- £690m undrawn facilities

During the twelve months to 31 March 2014 the Group raised or renewed £640m facilities

- £235m term loans and revolving credit facilities renewed
- £315m new term loans and RCFs
- £90m of new leases

The £125m Convertible Bond matures in August 2014. It is expected that full conversion to equity will take place and up to 2 June 2014; notices of conversion for £52.1m have already been received.

Since 31 March 2014 a new finance lease has been signed for £50m of which £35m will be used to partially finance an Energy from Waste plant.

The Group is fully funded for the K5 period and has facilities in place to cover the construction of the committed EfWs.

The fair value of the Group's non-current borrowings was £275m lower than the principal value reflecting the benefits of securing interest rates below the current market rate. The Group's average debt maturity is 21 years.

(1) $\text{Net borrowings} / (\text{equity} + \text{net borrowings})$

PENSIONS

The Group's defined benefit pension schemes had a deficit (net of deferred tax) under IAS 19 at 31 March 2014 of circa £63m (£79m gross) a reduction of £17m on the 31 March 2013 balance (as restated for IAS 19 (Revised)).

The net deficit represents circa 2% of the Group's current market capitalisation.

Schemes' assets increased from £580m at 31 March 2013 to £608m at 31 March 2014 due to favourable investment performance. Schemes' liabilities increased from £680m to £687m over the same period.

The revision to IAS 19, effective in 2013/14, resulted in a net finance cost in 2013/14 of circa £4m (2012/13 credit of £4m). A further circa £1m was charged to operating profit to recognise administration costs. Opening pension liabilities reduced by circa £10m as at 31 March 2013 as a result of the change.

South West Water's pension cash contributions remain within the allowance in Ofwat's Final Determination for K5.

The March 2013 actuarial valuation is being finalised.

TAXATION

Pennon takes seriously its responsibility for paying its fair share of tax.

The corporation tax charge for the year (excluding exceptional items) was £35.3m (current year charge - £51.8m, prior year credit - £16.5m). The equivalent figure for 2012/13 was £43.3m (current year charge - £56.3m, prior year credit - £13.0m). The effective current tax current year rate was 25% (2012/13 - 30%). The reduced rate reflects accelerated tax relief on capital expenditure together with the 1% reduction in the corporation tax rate.

Deferred tax for the year (excluding exceptional items) was a credit of £25.8m, current year charge - £2.2m, prior year charge - £12.1m (2012/13 credit - £14.1m, current year credit - £2.8m, prior year charge - £2.3m) and also includes a credit of £40.1m from the impact of the 3% reduction in the rate of corporation tax from April 2014 (2012/13 credit of £13.6m - 1% reduction).

The tax credit on the exceptional items of £48.6m amounted to £8.9m (2012/13 £36.2m) of which £Nil (2012/13 £15.6m) relates to corporation tax.

The statutory tax charge after exceptional and deferred tax credits was £0.6m (2012/13 £7.0m credit⁽¹⁾).

⁽¹⁾ Comparatives restated for IAS 19 (Revised)

CARBON DISCLOSURE PROJECT

For the first time and as noted at the half year, Pennon Group has been commended for the quality of its disclosure of climate change information by the Carbon Disclosure Project

(CDP) and is ranked in the top 10% of FTSE350 CDP respondents. As one of the largest environmental and resource management groups in the UK, Pennon is committed to leading the way in good environmental practice, both in how the Company operates in reducing its carbon emissions and in transparently recording and reporting its energy use.

The Group is featured in the CDP's "Climate Disclosure Leadership Index", a key component of the CDP's annual FTSE350 report which highlights the constituent companies within the FTSE350 Index which have displayed a strong approach to information disclosure regarding climate change. Companies are scored on their climate change disclosure and high scores indicate good internal data management and understanding of climate change-related issues affecting the company.

STRATEGY AND PROSPECTS

The Board's priority continues to be the creation of shareholder value through its strategic focus on: water and sewerage services; and recycling, renewable energy and waste management.

South West Water is continuing its strong performance with robust operational delivery and high standards of customer service and financial performance. It expects to complete the successful delivery of the current five year regulatory contract and has put in place a platform to deliver further efficiencies for K6. Having achieved 'enhanced' status for its Business Plan and as a result received a 'fast tracked' Draft Determination, preparation for 2015-2020 is also progressing well.

Viridor's financial performance over the year has been in line with management's expectations. Excellent progress is being made in the strategic re-orientation of the Viridor business model and Viridor is now at the forefront of transforming waste in the UK. The company continues to make strong progress in establishing its EfW business and securing base-load contracts. The EfW contracts and projects already contribute to Viridor's bottom line and are expected to drive Viridor's long term profit growth. EBITDA is expected to increase in 2014/15 as new EfW plants come on stream.

The Group is well positioned for the future, with efficient long term financing.

Ken Harvey
Chairman
3 June 2014

FINANCIAL TIMETABLE FOR THE YEAR ENDED 31 MARCH 2014

3 June 2014	2013/14 Preliminary Results (unaudited)
Early July 2014	Annual Report & Accounts published
31 July 2014	Annual General Meeting
6 August 2014 *	Ordinary shares quoted ex-dividend
8 August 2014 *	Record date for final cash dividend
Mid August 2014	Interim Management Statement
15 September 2014 *	Scrip election date for final dividend
3 October 2014 *	Final cash dividend paid and Scrip shares issued

* These dates are provisional and, both in the case of the final dividend and offering of a Scrip Dividend Alternative, subject to obtaining shareholder approval at the 2014 Annual General Meeting.

Pennon Group's Half Year Results to 30 September 2014 will be announced on 28 November 2014.

CAUTIONARY STATEMENT IN RESPECT OF FORWARD-LOOKING STATEMENTS

This Report contains forward-looking statements relating to the Pennon Group's operations, performance and financial position based on current expectations of, and assumptions and forecasts made by, Pennon Group management. Forward-looking statements are identified in this Report by words such as "anticipate", "aim", "believe", "continue", "could", "due", "estimate", "expect", "forecast", "goal", "intend", "may", "plan", "project", "remain", "seek", "should", "target", "will" and related and similar expressions, as well as statements in the future tense. Various known and unknown risks, uncertainties and other factors could lead to substantial differences between the actual future results, financial situation development or performance of the Group and the estimates and historical results given herein. Undue reliance should not be placed on forward-looking statements which are made only as of the date of this document. Important risks, uncertainties and other factors that could cause actual results, performance or achievements of Pennon Group to differ materially from any outcomes or results expressed or implied by such forward-looking statements include, among other things, changes in law, regulation or decisions by governmental bodies or regulators including uncertainties arising from market reform affecting South West Water; general business and economic conditions in the UK and globally; the availability and cost of finance; poor operating performance or a failure or interruption of the Group's operating systems or the inability to carry out network operations or damage to infrastructure; failure or increased costs of capital projects or acquisitions or joint ventures not achieving predicted revenues or performance; reduced customer base, increased competition affecting prices or reduced demand for services or over capacity in some markets; and information technology and business continuity systems and processes failing. Risks will be described in greater detail in the Pennon Group Annual Report to be published at the beginning of July 2014. Such forward looking statements should therefore be construed in light of such risks, uncertainties and other factors and undue reliance should not be placed on them. Nothing in this report should be construed as a profit forecast.

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

UNSOLICITED COMMUNICATIONS WITH SHAREHOLDERS

A number of companies, including Pennon Group Plc, continue to be aware that their shareholders have received unsolicited telephone calls or correspondence concerning investment matters which imply a connection to the company concerned. If shareholders have any concerns about any contact they have received then please refer to the Financial Conduct

Authority's [Beware of share fraud leaflet](#). Details of any share dealing facilities that the Company endorses will be included in Company mailings.

Consolidated income statement for the year ended 31 March 2014

		(Unaudited)					Total 2013 (Restated note 4) £m
	Note	Before exceptional items 2014 £m	Exceptional items (note 6) 2014 £m	Total 2014 £m	Before exceptional items 2013 (Restated note 4) £m	Exceptional items (note 6) 2013 £m	
Revenue	5	1,321.2	-	1,321.2	1,201.1	-	1,201.1
Operating costs							
Manpower costs		(161.4)	-	(161.4)	(159.3)	-	(159.3)
Raw materials and consumables used		(111.6)	-	(111.6)	(125.2)	-	(125.2)
Other operating expenses		(640.9)	(5.7)	(646.6)	(521.8)	(104.9)	(626.7)
Depreciation, amortisation and impairment		(149.8)	(42.9)	(192.7)	(149.2)	(84.0)	(233.2)
Operating profit	5	257.5	(48.6)	208.9	245.6	(188.9)	56.7
Finance income	7	43.3	-	43.3	95.3	15.4	110.7
Finance costs	7	(97.2)	-	(97.2)	(156.7)	(2.9)	(159.6)
Net finance costs	7	(53.9)	-	(53.9)	(61.4)	12.5	(48.9)
Share of post-tax profit from joint ventures		3.7	-	3.7	5.8	-	5.8
Profit before tax	5	207.3	(48.6)	158.7	190.0	(176.4)	13.6
Taxation	8	(9.5)	8.9	(0.6)	(29.2)	36.2	7.0
Profit for the year		197.8	(39.7)	158.1	160.8	(140.2)	20.6
Attributable to:							
Ordinary shareholders of the parent		182.2	(39.7)	142.5	160.8	(140.2)	20.6
Perpetual capital security holders		15.6	-	15.6	-	-	-
Earnings per ordinary share	9						
(pence per share)							
- Basic				38.8			5.7
- Diluted				38.6			5.7

Consolidated statement of comprehensive income for the year ended 31 March 2014

	(Unaudited)			Before exceptional items 2013 (Restated note 4)	Exceptional items (note 6) 2013	Total 2013 (Restated note 4)
	Before exceptional items 2014	Exceptional items (note 6) 2014	Total 2014			
	£m	£m	£m	£m	£m	£m
Profit for the year	197.8	(39.7)	158.1	160.8	(140.2)	20.6
Other comprehensive income/ (loss)						
<i>Items that will not be reclassified to profit or loss</i>						
Actuarial gains/ (losses) relating to retirement benefit obligations	26.2	-	26.2	(6.0)	-	(6.0)
Income tax on items that will not be reclassified	(10.2)	-	(10.2)	-	-	-
Total items that will not be reclassified to profit or loss	16.0	-	16.0	(6.0)	-	(6.0)
<i>Items that may be reclassified subsequently to profit or loss</i>						
Share of other comprehensive income from joint ventures	4.8	-	4.8	2.7	-	2.7
Cash flow hedges	32.8	-	32.8	(0.9)	2.9	2.0
Income tax on items that may be reclassified	(7.0)	-	(7.0)	0.7	(0.7)	-
Total items that may be reclassified subsequently to profit or loss	30.6	-	30.6	2.5	2.2	4.7
Other comprehensive income/(loss) for the year net of tax	46.6	-	46.6	(3.5)	2.2	(1.3)
Total comprehensive income for the year	244.4	(39.7)	204.7	157.3	(138.0)	19.3
Total comprehensive income attributable to:						
Ordinary shareholders of the parent	228.8	(39.7)	189.1	157.3	(138.0)	19.3
Perpetual capital security holders	15.6	-	15.6	-	-	-

Consolidated balance sheet at 31 March 2014

	(Unaudited)		
	2014	2013	2012
	£m	(Restated note 4) £m	(Restated note 4) £m
ASSETS			
Non-current assets			
Goodwill	339.3	339.3	326.5
Other intangible assets	30.6	13.7	22.0
Property, plant and equipment	3,450.4	3,278.6	3,083.6
Other non-current assets	230.3	183.3	138.4
Derivative financial instruments	25.9	31.0	21.9

Investments in joint ventures		0.1	0.1	0.1
		4,076.6	3,846.0	3,592.5
Current assets				
Inventories		12.1	10.5	9.0
Trade and other receivables		278.2	267.6	238.5
Derivative financial instruments		2.6	1.2	9.7
Financial assets at fair value through profit		0.4	10.5	0.5
Cash and cash deposits	14	613.1	634.5	425.3
		906.4	924.3	683.0
LIABILITIES				
Current liabilities				
Borrowings	14	(273.9)	(138.6)	(325.5)
Derivative financial instruments		(20.8)	(21.7)	(16.6)
Trade and other payables		(298.8)	(276.7)	(242.5)
Current tax liabilities		(37.7)	(66.9)	(60.3)
Provisions		(33.3)	(41.9)	(26.3)
		(664.5)	(545.8)	(671.2)
Net current assets		241.9	378.5	11.8
Non-current liabilities				
Borrowings	14	(2,533.2)	(2,504.6)	(2,204.4)
Other non-current liabilities		(82.8)	(77.9)	(76.9)
Financial liabilities at fair value through profit		(15.6)	(23.0)	(16.7)
Derivative financial instruments		(3.9)	(31.5)	(32.0)
Retirement benefit obligations		(79.3)	(99.6)	(89.4)
Deferred tax liabilities		(227.1)	(245.1)	(279.5)
Provisions		(179.0)	(170.7)	(76.3)
		(3,120.9)	(3,152.4)	(2,775.2)
Net assets		1,197.6	1,072.1	829.1
Equity				
Share capital	11	151.3	149.2	148.2
Share premium account		4.9	7.0	8.0
Capital redemption reserve		144.2	144.2	144.2
Retained earnings and other reserves		602.4	476.9	528.7
Total ordinary shareholders' equity		902.8	777.3	829.1
Perpetual capital securities	12	294.8	294.8	-
Total equity		1,197.6	1,072.1	829.1

Consolidated statement of changes in equity for the year ended 31 March 2014

	Share capital (note 11) £m	Share premium account £m	Capital redemption reserve £m	Retained earnings and other reserves (Restated note 4) £m	Perpetual capital securities (note 12) £m	Total Equity (Restated note 4) £m
At 1 April 2012	148.2	8.0	144.2	528.7	-	829.1
Profit for the year	-	-	-	20.6	-	20.6
Other comprehensive loss for the year	-	-	-	(1.3)	-	(1.3)
Total comprehensive income for the year	-	-	-	19.3	-	19.3
Transactions with equity shareholders						
Dividends paid or approved	-	-	-	(96.0)	-	(96.0)
Adjustment for shares issued under the scrip dividend alternative	1.0	(1.0)	-	18.1	-	18.1

Adjustment in respect of share-based payments	-	-	-	3.1	-	3.1
Issue of perpetual capital security	-	-	-	-	294.8	294.8
Own shares acquired by the Pennon Employee Share Trust in respect of share options granted	-	-	-	(0.9)	-	(0.9)
Proceeds from treasury shares re-issued	-	-	-	4.6	-	4.6
	1.0	(1.0)	-	(71.1)	294.8	223.7

At 31 March 2013	149.2	7.0	144.2	476.9	294.8	1,072.1
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	Unaudited					
Profit for the year	-	-	-	142.5	15.6	158.1
Other comprehensive income for the year	-	-	-	46.6	-	46.6
Total comprehensive income for the year	-	-	-	189.1	15.6	204.7

Transactions with equity shareholders

Dividends paid or approved	-	-	-	(103.9)	-	(103.9)
Adjustment for shares issued under the scrip dividend alternative	2.1	(2.1)	-	34.5	-	34.5
Adjustment in respect of share-based payments	-	-	-	3.8	-	3.8
Distributions due to perpetual capital security holders	-	-	-	-	(20.3)	(20.3)
Current tax relief on distributions to perpetual capital security holders	-	-	-	-	4.7	4.7
Own shares acquired by the Pennon Employee Share Trust in respect of share options granted	-	-	-	(0.4)	-	(0.4)
Proceeds from treasury shares re-issued	-	-	-	2.4	-	2.4
	2.1	(2.1)	-	(63.6)	(15.6)	(79.2)

At 31 March 2014	151.3	4.9	144.2	602.4	294.8	1,197.6
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Consolidated statement of cash flows for the year ended 31 March 2014

	Note	2014 £m	2013 £m
Cash flows from operating activities			
Cash generated from operations	13	338.0	341.1
Interest paid		(65.3)	(75.8)
Tax paid		(58.1)	(18.5)
Net cash generated from operating activities		214.6	246.8
Cash flows from investing activities			
Interest received		26.5	26.0
Acquisition of subsidiary undertakings (net of cash acquired)		-	(14.8)
Loan repayments received from joint ventures		0.3	0.3
Dividends received from joint ventures		8.5	8.5
Purchase of property, plant and equipment		(346.7)	(397.2)
Proceeds from sale of property, plant and equipment		5.4	4.5
Net cash used in investing activities		(306.0)	(372.7)
Cash flows from financing activities			
Proceeds from treasury shares re-issued	11	2.4	4.6
Proceeds from issue of perpetual capital securities	12	-	294.8
Deposit of restricted funds		(29.6)	(21.0)
Purchase of ordinary shares by the Pennon Employee Share Trust		(0.4)	(0.9)
Proceeds from new borrowing		294.0	409.9
Repayment of borrowings		(146.1)	(267.2)
Finance lease sale and leaseback		40.5	85.0
Finance lease principal repayments		(30.3)	(103.1)
Dividends paid		(69.4)	(77.9)
Perpetual capital securities periodic return		(20.3)	-
Net cash generated from financing activities			

		40.8	324.2
Net (decrease)/ increase in cash and cash equivalents		(50.6)	198.3
Cash and cash equivalents at beginning of year	14	490.5	292.2
Cash and cash equivalents at end of year	14	439.9	490.5

Notes

1. General information

Pennon Group Plc is a company registered in the United Kingdom under the Companies Act 2006. The address of the registered office is given on page 47. Pennon Group's business is operated through two main subsidiaries. South West Water Limited holds the water and sewerage appointments for Devon, Cornwall and parts of Dorset and Somerset. Viridor Limited's business is recycling, renewable energy and waste management.

The financial information for the years ended 31 March 2014 and 31 March 2013 does not constitute full financial statements within the meaning of section 434 of the Companies Act 2006. The full financial statements for 31 March 2013 were approved by the Board of Directors on 25 June 2013 and have been delivered to the Registrar of Companies. The independent auditors' report on these financial statements was unqualified and did not contain a statement under section 498 of the Companies Act 2006.

2. Basis of preparation

The accounting policies adopted in the unaudited financial information are consistent with those applied and set out in the Pennon Group Plc Annual Report and Accounts for the year ended 31 March 2013 (which are available on the Company website www.pennon-group.co.uk), except as described in note 3, and are also in accordance with all International Financial Reporting Standards (IFRS) and interpretations of the IFRS Interpretations Committee applicable for the year ended 31 March 2014 in issue which have been adopted by the European Union.

3. Accounting policies

The following revised standards, which are mandatory for the first time in the financial year beginning 1 April 2013, are relevant to the Group.

IAS 19 (Revised) 'Employee Benefits' adopted by the Group with effect from 1 April 2013, has been applied retrospectively in accordance with the transition provision in the standard. The primary impacts of the revised standard are to increase net finance costs, operating costs and to reduce pension liabilities as disclosed in note 4.

IFRS 13 'Fair Value Measurement' adopted by the Group with effect from 1 April 2013, requires additional disclosures on fair value measurement and categorisation. The Pennon Group Plc Annual Report and Accounts for the year ended 31 March 2014 will reflect these revised disclosure requirements.

Other standards or interpretations which were mandatory for the first time in the year beginning 1 April 2013 did not have a material impact on the net assets or results of the Group.

4. Restatements

IAS 19 (Revised) 'Employee Benefits' has been applied retrospectively in accordance with the transition provision in the standard; comparative information has been restated accordingly.

At 31 March 2013 the accounting for the acquisition of JWT Holdings Limited (renamed Viridor Waste (Atherton) Limited) was provisional. In addition at 31 March 2013 the accounting for the acquisition of Pulp Friction Limited (renamed Viridor (Erith) Limited) and the trade and assets of SBS Paper LLP, a related business, was also provisional. The completion of the accounting for these acquisitions has resulted in changes to comparative amounts.

	2013 (Unaudited)		
	Previously reported £m	Application of IAS 19R £m	Restated now reported £m
INCOME STATEMENT			
Manpower costs	(158.6)	(0.7)	(159.3)

Operating profit	57.4	(0.7)	56.7
Finance income	143.0	(32.3)	110.7
Finance costs	(184.4)	24.8	(159.6)
Profit before tax	21.8	(8.2)	13.6
Taxation - deferred tax	32.8	1.9	34.7
Profit for the year	26.9	(6.3)	20.6
Earnings per share (pence per share)			
- - Basic	7.4	(1.7)	5.7
- - Diluted	7.4	(1.7)	5.7
STATEMENT OF COMPREHENSIVE INCOME			
Other comprehensive loss (net of tax)	(8.4)	7.1	(1.3)
Total comprehensive income	18.5	0.8	19.3

	2013 (Unaudited)				2012 (Unaudited)		
	Previously reported £m	Application of IAS 19R £m	Acquisitions restatements £m	Restated now reported £m	Previously reported £m	Application of IAS 19R £m	Restated now reported £m
BALANCE SHEET							
<u>Non-current assets</u>							
Goodwill	339.0	-	0.3	339.3	326.5	-	326.5
Other intangible assets	12.5	-	1.2	13.7	22.0	-	22.0
Property, plant and equipment	3,279.6	-	(1.0)	3,278.6	3,083.6	-	3,083.6
<u>Current assets</u>							
Trade and other receivables	267.7	-	(0.1)	267.6	238.5	-	238.5
<u>Current liabilities</u>							
Trade and other payables	(277.2)	-	0.5	(276.7)	(242.5)	-	(242.5)
Current tax	(67.0)	-	0.1	(66.9)	(60.3)	-	(60.3)
Provisions	(40.6)	-	(1.3)	(41.9)	(26.3)	-	(26.3)
<u>Non-current liabilities</u>							
Retirement benefit obligations	(109.7)	10.1	-	(99.6)	(98.6)	9.2	(89.4)
Deferred tax	(243.1)	(2.3)	0.3	(245.1)	(277.3)	(2.2)	(279.5)
<u>Equity</u>							
Retained earnings and other reserves	469.1	7.8	-	476.9	521.7	7.0	528.7

5. Segmental information

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

The water and sewerage business comprises the regulated water and sewerage services undertaken by South West Water Limited. The waste management business is the recycling, renewable energy and waste management services provided by Viridor Limited.

	2014 (Unaudited) £m	2013 (Restated note 4) £m
Revenue		
Water and sewerage	520.0	498.6
Waste management	802.0	703.8
Other	11.2	10.8
Less intra-segment trading *	(12.0)	(12.1)
	1,321.2	1,201.1
Segment result		
Operating profit before depreciation, amortisation and exceptional items (EBITDA)		
Water and sewerage	330.9	317.1
Waste management	76.3	77.7
Other	0.1	-
	407.3	394.8
Operating profit before exceptional items		
Water and sewerage	227.0	214.8
Waste management	30.2	30.6
Other	0.3	0.2
	257.5	245.6
Profit before tax and exceptional items		
Water and sewerage	162.5	146.7
Waste management	27.6	34.3
Other	17.2	9.0
	207.3	190.0
Profit/(loss) before tax		
Water and sewerage	162.5	159.2
Waste management	(21.1)	(154.6)
Other	17.3	9.0
	158.7	13.6

* 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.

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

Geographic analysis of revenue based on location of customers

	2014 (Unaudited) £m	2013 £m
UK	1,265.2	1,142.1
Rest of European Union	13.1	11.2
China	35.8	39.7
Rest of World	7.1	8.1
	1,321.2	1,201.1

The UK is the Group's country of domicile and generates the majority of its revenue from external customers in the UK. The Group's non-current assets are located in the UK.

6. Exceptional items

Exceptional items are those that in the Directors' view are required to be separately disclosed by virtue of their size or incidence to enable a full understanding of the Group's financial performance.

2014 (Unaudited) £m	2013 £m
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Operating costs

Impairment of property, plant and equipment (a)	(42.9)	(78.2)
Environmental and landfill restoration provisions (b)	(5.7)	(90.1)
Onerous contracts and other (c)	-	(20.6)
Operating loss	(48.6)	(188.9)

Net finance costs

Receipt on transfer and subsequent termination of lease (d)	-	15.4
Fair value loss on associated interest rate swap transferred from equity on termination of lease (d)	-	(2.9)
	-	12.5
Loss before tax	(48.6)	(176.4)
Tax credit arising on exceptional items (e)	8.9	36.2
Loss for the year	(39.7)	(140.2)

- (a) The 2014 impairment charge relates to write-down of the carrying values of property, plant and equipment in landfill, reflecting reduced prices and higher ongoing capital costs.

The 2013 impairment charge related to a write-down of the carrying values of property, plant and equipment in landfill and recycling activities reflecting reduced landfill volumes and recycle prices. The 2013 impairment charge was net of a credit arising from the reassessment of landfill site residual values linked to gas production at landfill sites post-closure.

- (b) Environmental control and aftercare costs are incurred during the operational life of each landfill site and for a considerable period thereafter. The period of aftercare post-closure and the level of costs expected are uncertain and can vary significantly from site to site. Key factors are the type of waste, the speed at which it decomposes, the volume of leachate requiring treatment and regulatory requirements specific to the site. The amounts expected to be incurred have been re-assessed, re-estimated and aligned to the revised landfill site operating lives established from the anticipated decline in landfill activity.

In 2014 provisioning has been increased by £5.7m due to revisions to site life costings.

The 2013 provision reassessments additionally reflected a change in the estimate of the aftercare period to 60 years after site closure, previously 30 years, to align with updated technical assessment using independent external advice.

- (c) Onerous contracts principally arise from long term contractual obligations to purchase materials for recycling at input prices, which in 2013, lead to an expected loss after reflecting directly attributable and unavoidable costs of processing.
- (d) In 2013 South West Water Limited received a consent fee related to the transfer and subsequent termination of a lease arising from the sale of a finance lease between financial institutions.
- (e) The total tax credit on exceptional items is below the current rate of corporation tax (23%) (2013 24%) due to tax relief falling due in the future when the corporation tax rate will be 20% and tax relief not being available on ineligible expenditure on which no deferred tax has previously been accounted for (principally land and buildings).

7. **Net finance costs**

	2014 (Unaudited)			2013 (Restated note 4)		
	Finance cost £m	Finance income £m	Total £m	Finance cost £m	Finance income £m	Total £m
Cost of servicing debt						
Bank borrowings and overdrafts	(32.5)	-	(32.5)	(40.0)	-	(40.0)
Interest element of finance lease rentals	(35.8)	-	(35.8)	(39.8)	-	(39.8)
Other finance costs	(4.9)	-	(4.9)	(5.4)	-	(5.4)

Interest receivable	-	5.3	5.3	-	5.8	5.8
Interest receivable on shareholder loans to joint ventures	-	9.8	9.8	-	9.3	9.3
	(73.2)	15.1	(58.1)	(85.2)	15.1	(70.1)
Other finance income						
Investment income received	-	11.3	11.3	-	66.8	66.8
Fair value losses on derivative financial instruments providing commercial hedges	(10.7)	-	(10.7)	(63.4)	-	(63.4)
	(10.7)	11.3	0.6	(63.4)	66.8	3.4
Notional interest						
Interest receivable on service concession arrangements	-	8.5	8.5	-	6.0	6.0
Retirement benefit obligations	(4.0)	-	(4.0)	(3.8)	-	(3.8)
Unwinding of discounts on provisions	(9.3)	-	(9.3)	(4.3)	-	(4.3)
	(13.3)	8.5	(4.8)	(8.1)	6.0	(2.1)
Net gains on non-designated financial instruments hedging interest rate risk	-	8.4	8.4	-	7.4	7.4
Net finance costs before exceptional items	(97.2)	43.3	(53.9)	(156.7)	95.3	(61.4)
Exceptional items (note 6)	-	-	-	(2.9)	15.4	12.5
	(97.2)	43.3	(53.9)	(159.6)	110.7	(48.9)

In addition to the above, finance costs of £21.8m (2013 £13.6m) have been capitalised on qualifying assets included in property, plant and equipment.

Other finance income represents enhanced yields from investment income received on deposits held partially offset by fair value losses on derivative financial instruments which provided commercial hedges against these short term structured deposits. These transactions commenced and matured during the year.

8. Taxation

Unaudited			Before exceptional items (Restated note 4) 2013 £m	Exceptional items (note 6) 2013 £m	Total 2013 (Restated note 4) £m
Before exceptional items 2014 £m	Exceptional items (note 6) 2014 £m	Total 2014 £m			

Analysis of charge/(credit) :

Current tax charge	35.3	-	35.3	43.3	(15.6)	27.7
Deferred tax - other	14.3	(10.2)	4.1	(0.5)	(21.5)	(22.0)
Deferred tax arising on change of rate of corporation tax	(40.1)	1.3	(38.8)	(13.6)	0.9	(12.7)
Total deferred tax credit	(25.8)	(8.9)	(34.7)	(14.1)	(20.6)	(34.7)
Tax charge/ (credit)	9.5	(8.9)	0.6	29.2	(36.2)	(7.0)

UK corporation tax is calculated at 23% (2013 24%) of the estimated assessable profit for the year.

UK corporation tax is stated after release of prior year credits of £16.5m (2013 £13.0m).

Deferred tax before exceptional items includes a non-recurring credit of £40.1m (2013 £13.6m) reflecting the reduction in the rate of UK corporation tax to 20%.

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

9. 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 year, 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.

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

	2014 (Unaudited)	2013
Number of shares (millions)		
For basic earnings per share	367.4	363.6
Effect of dilutive potential ordinary shares from share options	1.7	2.2
For diluted earnings per share	369.1	365.8

Basic and diluted earnings per ordinary share before exceptional items and deferred tax

Earnings per share before exceptional items and deferred tax are presented to provide a more useful comparison of business trends and performance, since deferred tax reflects distortive effects of changes in corporation tax rates and the level of long term investment. Earnings per share have been calculated:

	2014 (Unaudited)			2013 (Restated note 4)		
	Profit after tax £m	Earnings per share		Profit after tax £m	Earnings per share	
		Basic p	Diluted p		Basic p	Diluted p
Statutory earnings	142.5	38.8	38.6	20.6	5.7	5.7
Deferred tax	(25.8)	(7.0)	(7.0)	(14.1)	(4.0)	(3.9)
Exceptional items (net of tax)	39.7	10.8	10.8	140.2	38.6	38.3
Earnings before exceptional items and deferred tax	156.4	42.6	42.4	146.7	40.3	40.1

10.

Dividends**Amounts recognised as distributions to equity holders in the year:**

	2014 (Unaudited) £m	2013 £m
Interim dividend paid for the year ended 31 March 2013 : 8.76p (2012 8.22p) per share	31.9	29.7
Final dividend paid for the year ended 31 March 2013 : 19.70p (2012 18.30p) per share	72.0	66.3
	103.9	96.0

Proposed dividends

Proposed interim dividend for the year ended 31 March 2014 : 9.39p (2013 8.76p) per share	34.8	31.9
Proposed final dividend for the year ended 31 March 2014 : 20.92p (2013 19.70p) per share	77.9	72.0
	112.7	103.9

The proposed interim and final dividends have not been included as liabilities in these financial statements. The proposed interim dividend for 2014 was paid on 3 April 2014 and the proposed final dividend is subject to approval by shareholders at the Annual General Meeting on 31 July 2014.

If approved at the Annual General Meeting the final dividend of 20.92p per share will be paid on 3 October 2014 to shareholders on the register on 8 August 2014.

The cost of the proposed final dividend for the year ended 31 March 2014 excludes the impact of any conversion of the £125m convertible bond between the year end and 8 August 2014.

11.

Share capital**Allotted, called up and fully paid**

	Number of shares		£m
	Treasury shares	Ordinary shares	
At 1 April 2012			
Ordinary shares of 40.7p each	3,632,705	360,588,466	148.2

Shares issued under the scrip dividend alternative	-	2,542,187	1.0
Shares re-issued under the Company's Performance and Co-investment Plan	(493,217)	493,217	-
For consideration of £0.9m, shares re-issued to the Pennon Employee Share Trust	(113,957)	113,957	-
For consideration of £3.3m, shares re-issued under the Company's Sharesave Scheme	(843,280)	843,280	-
For consideration of £0.4m, shares re-issued under the Executive Share Option Scheme	(76,415)	76,415	-
At 31 March 2013 ordinary shares of 40.7p each	2,105,836	364,657,522	149.2

	Unaudited		
Shares issued under the scrip dividend alternative	-	5,071,608	2.1
Shares re-issued under the Company's Performance and Co-investment Plan	(304,374)	304,374	-
For consideration of £0.4m, shares re-issued to the Pennon Employee Share Trust	(69,336)	69,336	-
For consideration of £1.9m, shares re-issued under the Company's Sharesave Scheme	(438,302)	438,302	-
For consideration of £0.1m, shares re-issued under the Executive Share Option Scheme	(11,134)	11,134	-
At 31 March 2014 ordinary shares of 40.7p each	1,282,690	370,552,276	151.3

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

12. Perpetual capital securities

	2014 (Unaudited) £m	2013 £m
GBP 300m 6.75% perpetual subordinated capital securities	294.8	294.8

On 8 March 2013 the Company issued £300m perpetual capital securities. Costs directly associated with the issue of £5.2m are set off against the value of the issuance. They have no fixed redemption date but the Company may, at its sole discretion, redeem all, but not part, of these securities at their principal amount on 8 March 2018 or any subsequent periodic return payment date after this.

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

The Company paid a periodic return of £20.3m on 8 March 2014. This payment and the associate tax relief of £4.7m have been recognised directly in the perpetual capital security reserve.

13. **Cash flow from operating activities**

Reconciliation of profit for the year to net cash inflow from operating activities:

	2014 (Unaudited) £m	2013 (Restated note 4) £m
Cash generated from operations		
Profit for the year	158.1	20.6
Adjustments for:		
Share-based payments	3.3	3.6
Profit on disposal of property, plant and equipment	(4.2)	(1.8)
Depreciation charge	147.1	145.5
Amortisation of intangible assets	2.7	3.7
Exceptional impairment of property, plant and equipment	42.9	69.8
Exceptional provision charge	5.7	111.5
Other non cash exceptional charges	-	7.6
Share of post-tax profit from joint ventures	(3.7)	(5.8)
Finance income	(43.3)	(110.7)
Finance costs	97.2	159.6
Taxation charge/(credit)	0.6	(7.0)
Changes in working capital (excluding the effect of the acquisition of subsidiaries):		
Increase in inventories	(1.6)	(1.5)
Increase in trade and other receivables	(13.2)	(27.7)
Increase in service concession arrangements receivable	(47.5)	(31.3)
Increase in trade and other payables	7.3	11.8
Increase in retirement benefit obligations	1.9	0.4
Decrease in provisions	(15.3)	(7.2)
Cash generated from operations	338.0	341.1
Total interest paid		
Interest paid in operating activities	65.3	75.8
Interest paid in investing activities (purchase of property, plant and equipment)	21.8	13.6
Total interest paid	87.1	89.4

14. **Net borrowings**

	2014 (Unaudited) £m	2013 £m
Cash and cash deposits	613.1	634.5
<i>Borrowings - current</i>		
Bank overdrafts	-	(0.4)
Other current borrowings	(155.4)	(97.0)
Finance lease obligations	(118.5)	(41.2)
Total current borrowings	(273.9)	(138.6)
<i>Borrowings - non-current</i>		
Bank and other loans	(1,077.8)	(1,072.5)
Other non-current borrowings	(304.3)	(210.4)
Finance lease obligations	(1,151.1)	(1,221.7)
Total non-current borrowings	(2,533.2)	(2,504.6)
Total net borrowings	(2,194.0)	(2,008.7)

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

	2014 (Unaudited) £m	2013 £m
Cash and cash deposits as above	613.1	634.5
Bank overdrafts as above	-	(0.4)
	613.1	634.1
Less : deposits with a maturity of three months or more (restricted funds)	(173.2)	(143.6)
	439.9	490.5

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