

## SOUTHERN WATER SERVICES LIMITED

### PRELIMINARY RESULTS FOR THE YEAR ENDED 31 MARCH 2010

#### Key Performance Indicators

**Customer Service** – Southern Water's performance for its customers improved, delivering the company's best performance against industry regulator Ofwat's Customer Services measures during 2009/10. The company achieved ISO 9001 Quality Management for the whole of Southern Water's Customer Service operations, demonstrating the company's excellent Customer Service through continuous improvement and robustly implemented processes. Customer complaints fell by 39 per cent and the number of customer enquiries responded to within five working days rose to 99.94 per cent. The number of customers visiting the company's website rose by 9.2 per cent and the site remained in the top three utility websites for usability. The company also raised a record £300,000 for charities in 2009.

**Capital Delivery** – In the final year of the five-year capital programme between 2005 and 2010 the company invested £234.1 million of a total £2 billion investment in water and wastewater infrastructure, improving services for customers. Significant projects included the start of the company's £300 million environmental improvement scheme to bring cleaner seas to Sussex. The scheme will mean that the 95 million litres of wastewater generated each day in the area will be fully treated for the first time, in line with European quality standards. A three-year £15.5 million scheme to replace 46 kilometres of ageing Victorian water mains in Brighton and Hove was also completed in 2009. In Hampshire, a scheme to build a pumping station to help protect Portsmouth from flooding reached its final stages. A £50 million upgrade of the company's wastewater treatment works in Ashford, Kent, was completed as part of wider investment to cater for population growth, along with a £25 million scheme to provide wastewater infrastructure for 250,000 new homes planned for the Thames Gateway. In the Isle of Wight, the company invested £3 million in a flood protection scheme for Cowes.

**Operational Performance** – Southern Water maintained its recent excellent performance at its wastewater treatment works with 98.9 per cent meeting European quality standards. The company's Overall Performance Assessment, as measured by industry regulator Ofwat, continued the company's best ever performance from the previous year. Once again, the quality of the drinking water supplied by Southern Water was among the best in Europe. Southern Water was awarded the Carbon Trust Standard for its efforts to measure and mitigate its carbon emissions and increased the amount of renewable energy generated to meet up to 13 per cent of the electricity used by the company. The company increased the use of its sludge treatment centres and reduced the amount taken to landfill by 75 per cent. An initiative was launched to reduce the number of sewer blockages caused by fat, oil and grease poured down sinks.

**Future Planning** – In November 2009, the water industry regulator Ofwat published a new set of price limits for water companies for the period from 2010 to 2015. The price limits allow for £1.7 billion further investment in the company's water and wastewater infrastructure during the next five years. Key aspects of the plan include completion of the new wastewater treatment works for Brighton and Hove, a universal metering programme to install meters for 92 per cent of customers by 2015, giving them greater control over water bills, mitigating carbon emissions, reducing the number of properties at risk of internal flooding and completing the improvement programme required by the Environment Agency. The company's plans to manage water resources in the South East during the next 25 years were also approved by the Government.

**Awards** – Following the company's record-breaking achievement in 2008/09, the company continued to attract accolades and awards during 2009/10. Southern Water won more than ten national and regional awards, including the Utility Industry Achievement Awards and the Water Industry Achievement Awards. The awards were for health and safety performance, staff training schemes, the innovative use of technology, construction work and community initiatives.

**Interim CEO Howard Goodbourn said: “We have continued to deliver excellent levels of customer service which was recognised in Southern Water being awarded the ISO9001 standard. In addition to this we have invested almost £1,000 per property in the Southern Water region over the last five years demonstrating our commitment to delivering continued service improvements to our customers despite challenging conditions. ”**

## **Financial Highlights**

- £234.1m invested to deliver new and improved water supply and wastewater treatment infrastructure - part of a £2 billion programme across Kent, Sussex, Hampshire and the Isle of Wight between 2005 and 2010.
- Cash flow from income less operating expenditure totalled £389.4m after an exceptional payment to the pension schemes of £56.1m. Cash outflow required to deliver the capital investment programme totalled £213.6m. This resulted in an overall positive cash flow of £12.8m before financing.
- Operating profits decreased by 3.3% to £303.9m.
- Profit after taxation for the financial year was £129.3m.

## **FINANCIAL REVIEW**

### **Profit and Loss Account**

- Turnover increased by 0.2% to £679.1m (2008-09: £677.8m) compared with an average tariff increase of 5.8%. The tariff increase is offset by a decline in demand for water from measured domestic and business customers following the wet summer and resulting from the economic downturn together with the impact of continued high levels of customers switching to measured supplies.
- Cost of sales and administrative expenses increased by 3.2% to £375.4m (2008-09: £363.9m). This increase resulted mainly from the impact of higher depreciation charges and bad debt provision costs partially offset by operating efficiencies.
- The tax on profit on ordinary activities has increased from £52.0m in 2008/09 to £60.8m in 2009/10 largely due to an increase in taxable profits as a result of lower interest charges.
- Profit after taxation for the financial year was £129.3m (2008/09 £97.4m). The retained profit for the year of £88.4 million has been transferred to reserves.

### **Balance Sheet**

- At the end of the year to 31 March 2010, Southern Water had fixed assets of £3,695.8m (2008-09: £3,645.8m) an increase of £50.0m from March 2009. This increase results from the capital investment programme offset by depreciation.
- Debtors falling due within one year increased to £234.5m at 31 March 2010, from £212.6m. This increase is as a result of an increase in prepaid expenses and £17.4m owed by group undertakings.
- As at 31 March 2010 Creditors falling due within one year totalled £194.4m, the reduction from £311.2m at 31 March 2009 results from the repayment of the Mezzanine debt in April 2009.
- Creditors falling due after one year increased by £66.8m to £3,460.0m as at 31 March 2010, this increase principally resulted from inflation on index linked bonds of £13.7m and a deferred swap

credit of £38.3m and an inter company creditor of £14.4m as part of the restructuring of the Mezzanine debt.

- As at 31 March 2010, the SWS defined benefit pension scheme had an accounting deficit net of deferred tax of £65.9m (2008/09: £83.3m) after receiving deficit payments paid early of £56.1m. In accordance with UK GAAP this deficit is included in the balance sheet.
- Overall net assets increased to £810.3m from £761.0m.

### **Cash Flow**

- Net cash inflow from operating activities decreased to £389.4m for 2009-10 from £443.3m in 2008-09. This decrease is principally the result of an exceptional one off lump sum payment of £56.1m made by the company into the Southern Water Pension Scheme.
- The net cash outflow from returns on investment and servicing of finance decreased to £96.6m for 2009-10 from £106.8m in 2008-09, due to lower interest paid following the repayment of the Mezzanine debt in April 2009. This saving has been partially offset by lower interest receivable on cash deposits as a result of the reduction in Bank of England base rates.
- The outflow of cash relating to the purchase of tangible fixed assets was £226.7m (2008-09: £330.6m) and the net cash inflow before financing in 2009-10 was £12.8m (2008-09: £117.1m outflow).
- During the year the net cash outflow from financing was £84.5m mainly as a result of the repayment of the Mezzanine debt and the issuance of a new £50.0m loan facility, as part of the overall company financing strategy.

**PROFIT AND LOSS ACCOUNT**  
For the year ended 31 March 2010

	Notes	2010 £m	2009 £m
<b>Turnover</b>		<b>679.1</b>	677.8
Cost of sales		<b>(348.1)</b>	(337.1)
Gross profit		<u>331.0</u>	<u>340.7</u>
Administrative expenses		<b>(27.3)</b>	(26.8)
Other operating income		<u>0.2</u>	<u>0.3</u>
<b>Operating profit</b>		<b>303.9</b>	314.2
Profit on disposal of fixed assets		1.4	7.6
<b>Profit on ordinary activities before interest and taxation</b>		<b>305.3</b>	321.8
Interest payable and similar charges	2	<b>(177.0)</b>	(240.1)
Interest receivable and similar income	2	<b>61.8</b>	67.7
<b>Profit on ordinary activities before taxation</b>		<u>190.1</u>	<u>149.4</u>
Tax on profit on ordinary activities	3	<b>(60.8)</b>	(52.0)
<b>Profit on ordinary activities after taxation</b>		<u>129.3</u>	<u>97.4</u>
Dividends	4	<b>(40.9)</b>	(120.1)
<b>Profit/(loss) for the financial year</b>		<u><b>88.4</b></u>	<u>(22.7)</u>

The above results relate to continuing operations.

There is no difference between the profit on ordinary activities before taxation and the retained profit for the year stated above and their historical cost equivalents.

## STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES

For the year ended 31 March 2010

	2010 £m	2009 £m
<b>Profit on ordinary activities after taxation</b>	<b>129.3</b>	97.4
Actuarial loss recognised in the pension scheme	<b>(54.3)</b>	(38.5)
Movement on deferred tax relating to pension deficit	<b>10.5</b>	10.8
Movement on current tax relating to pension deficit	<b>4.7</b>	-
<b>Total recognised gains for the year</b>	<b>90.2</b>	<b>69.7</b>

**BALANCE SHEET**  
As at 31 March 2010

	Notes	2010 £m	2009 £m
<b>Fixed assets</b>			
Tangible assets		3,666.6	3,616.6
Investments		29.2	29.2
		<u>3,695.8</u>	<u>3,645.8</u>
<b>Current assets</b>			
Stocks		1.2	1.6
Debtors: amounts falling due within one year		234.5	212.6
Debtors: amounts falling due after one year		812.3	820.3
Cash at bank and in hand		288.7	360.4
		<u>1,336.7</u>	<u>1,394.9</u>
<b>Creditors: amounts falling due within one year</b>		<u>(194.4)</u>	<u>(311.2)</u>
<b>Net current assets</b>		<u>1,142.3</u>	<u>1,083.7</u>
<b>Total assets less current liabilities</b>		<u>4,838.1</u>	<u>4,729.5</u>
<b>Creditors: amounts falling due after more than one year</b>		<u>(3,460.0)</u>	<u>(3,393.2)</u>
<b>Provision for liabilities and charges</b>			
Environmental obligations		(0.3)	(0.4)
Deferred taxation		(451.5)	(440.1)
<b>Grants and contributions</b>		<u>(50.1)</u>	<u>(51.5)</u>
<b>Net assets excluding pension deficit</b>		<u>876.2</u>	<u>844.3</u>
<b>Pension deficit</b>		<u>(65.9)</u>	<u>(83.3)</u>
<b>Net assets including pension deficit</b>		<u>810.3</u>	<u>761.0</u>
<b>Capital and reserves</b>			
Called up share capital	5	0.1	0.1
Share premium	5	46.3	46.3
Profit and loss account	5	763.9	714.6
<b>Total shareholders' funds</b>		<u>810.3</u>	<u>761.0</u>

**CASH FLOW STATEMENT**  
for the year ended 31 March 2010

	2010 £m	2009 £m
<b>Net cash inflow from operating activities</b>	<b>389.4</b>	443.3
<b>Returns on investments and servicing of finance</b>		
Interest received	62.7	70.7
Interest paid	(144.8)	(163.8)
Preference share dividends	(14.5)	(13.7)
<b>Net cash outflow from returns on investments and servicing of finance</b>	<b>(96.6)</b>	(106.8)
<b>Taxation</b>	<b>(25.5)</b>	(21.0)
<b>Capital expenditure and financial investment</b>		
Purchase of tangible fixed assets	(226.7)	(330.6)
Receipt of grants and contributions	10.7	9.6
Sale of tangible assets	2.4	8.5
<b>Net cash outflow for capital expenditure and financial investment</b>	<b>(213.6)</b>	(312.5)
<b>Equity dividends paid</b>	<b>(40.9)</b>	(120.1)
<b>Net cash inflow/(outflow) before financing</b>	<b>12.8</b>	(117.1)
<b>Financing</b>		
Increase in borrowings	50.0	298.3
Repayment of loans	(183.3)	(20.0)
Issue costs of new loans	-	(2.1)
Deferred swap receipts	48.8	-
<b>Net cash (outflow)/inflow from financing</b>	<b>(84.5)</b>	276.2
<b>(Decrease)/increase in net cash</b>	<b>(71.7)</b>	159.1
<b>Reconciliation to net debt</b>		
Net debt at beginning of year	(3,189.8)	(3,014.0)
(Decrease)/increase in net cash	(71.7)	159.1
Movements in borrowings	133.3	(278.3)
Debt issue costs	-	2.1
Deferred swap receipts	(48.8)	-
Other non cash changes	(11.8)	(58.7)
<b>Net debt at end of year</b>	<b>(3,188.8)</b>	(3,189.8)

## Notes to the preliminary results

The financial information set out above does not constitute the Company's statutory financial statements for the year ended 31 March 2010, or for the year ended 31 March 2009, within the meaning of section 435 of the Companies Act 2006. The financial information is based upon the audited statutory financial statements for the year ended 31 March 2010, upon which the auditors have issued an unqualified audit opinion.

The financial statements for the year ended 31 March 2009 have been delivered to the Registrar of Companies. The financial statements for the year ended 31 March 2010 will be delivered to the Registrar of Companies in due course.

### 1. Basis of preparation

The financial statements have been prepared on the going concern basis, under the historical cost convention, and in accordance with applicable accounting standards and, on a consistent basis with prior years as set out in the Companies Statutory Accounts.

### 2 Interest

	2010 £m	2009 £m
<b>Interest payable and similar charges</b>		
Interest payable on other loans	3.6	0.1
Interest paid to group companies	140.3	164.2
Indexation	13.7	56.5
Amortisation of issue costs	2.7	2.5
Amortisation of gilt lock proceeds	(0.1)	(0.1)
Amortisation of deferred credits	(4.2)	-
Amortisation of bond premium	(0.6)	(0.6)
Amortisation of discount	0.3	0.4
Other finance expense	6.8	3.4
Dividends on preference shares- see note below	14.5	13.7
<b>Total interest payable and similar charges</b>	<u>177.0</u>	<u>240.1</u>
<b>Interest receivable</b>		
Interest receivable from Southern Water Services Group Limited	56.9	56.9
Other interest receivable	4.9	10.8
<b>Total interest receivable</b>	<u>61.8</u>	<u>67.7</u>

The preference share dividends were paid on 7 October 09 and 31 March 10 and Class A1 amounted to £40 per share and Class B £70 per share (totalling £13.7m (2009: £13.7m)). A dividend of £0.8m (2009: £nil) was declared and paid to the Class A2 preference shareholders in September 2009 for outperformance in the year ending 31 March 2009.

### 3 Taxation

	2010 £m	2009 £m
<b>Current tax:</b>		
UK corporation tax on profits for the year	49.4	17.2
Adjustment in respect of prior years	-	(1.3)
	<u>49.4</u>	<u>15.9</u>
<b>Deferred tax:</b>		
Origination and reversal of timing differences	12.0	29.7
Adjustment in respect of prior years	(0.6)	5.3
Pension cost relief in excess of pension cost charge	-	1.1
Total deferred tax	<u>11.4</u>	<u>36.1</u>
Total tax on profit on ordinary activities	<u><u>60.8</u></u>	<u><u>52.0</u></u>

The rate of current tax charge on profit on ordinary activities varied from the standard rate of corporation tax due to the following factors:

	2010 £m	2009 £m
<b>Profit on ordinary activities before tax</b>	<u>190.1</u>	<u>149.4</u>
<b>Current tax:</b>		
UK corporation tax on profits for the year at 28% (2009: 28%)	53.2	41.8
Adjustments in respect of prior years	-	(1.3)
Permanent differences	8.2	6.2
<b>Tax charge on ordinary activities</b>	<u>61.4</u>	<u>46.7</u>
Timing differences	(12.0)	(30.8)
<b>Current tax charge for year</b>	<u><u>49.4</u></u>	<u><u>15.9</u></u>

Factors that may affect future tax charges:

Based on current capital investment plans, the Company expects to continue to be able to claim capital allowances in excess of depreciation in future years at a similar level to the current year.

Deferred tax liabilities have not been discounted.

### 4 Dividends

	2010 £ per ordinary share	2009 £ per ordinary share	2010 £m	2009 £m
<b>Ordinary shares</b>				
Interim dividend – 30 Sept	365.57	355.40	20.5	19.8
Interim dividend – 28 Nov	-	1,055.36	-	59.1
Interim dividend – 31 Dec	182.78	177.71	10.2	10.0
Interim dividend – 31 Mar	182.78	177.71	10.2	10.0
Total interim dividend	<u>731.13</u>	<u>1,766.18</u>	<u>40.9</u>	<u>98.9</u>
Final dividend – prior year	-	378.57	-	21.2
<b>Total ordinary dividend</b>	<u><u>731.13</u></u>	<u><u>2,144.75</u></u>	<u><u>40.9</u></u>	<u><u>120.1</u></u>

A final dividend for the year ended 31 March 2010 of £625.00 per ordinary share (£35.0m in total) was declared on 28 April 2010 (2009: £nil).

## 5 Reconciliation of movement in shareholders' funds

	Called up share capital £m	Share premium £m	Profit and loss account £m	Total £m
At 1 April 2009	0.1	46.3	714.6	761.0
Profit after tax	-	-	129.3	129.3
Dividends paid	-	-	(40.9)	(40.9)
Actuarial loss on pension scheme	-	-	(54.3)	(54.3)
Movement on deferred tax relating to pension asset	-	-	10.5	10.5
Movement on current tax relating to pension asset	-	-	4.7	4.7
<b>At 31 March 2010</b>	<b>0.1</b>	<b>46.3</b>	<b>763.9</b>	<b>810.3</b>

The profit and loss reserve includes recognised losses of £108.8m (2009: £115.7m) less deferred taxation of £42.9m (2009: £32.4m) in respect of pension scheme liabilities of the group pension fund.

	Called up share capital £m	Share premium £m	Profit and loss account £m	Total £m
At 1 April 2008	0.1	46.3	765.0	811.4
Profit after tax	-	-	97.4	97.4
Dividends paid	-	-	(120.1)	(120.1)
Actuarial gain on pension scheme	-	-	(38.5)	(38.5)
Movement on deferred tax relating to pension asset	-	-	10.8	10.8
<b>At 31 March 2009</b>	<b>0.1</b>	<b>46.3</b>	<b>714.6</b>	<b>761.0</b>