

PENNON GROUP PLC

PUBLICATION OF ANNUAL REPORT AND ACCOUNTS 2016
AND NOTICE OF ANNUAL GENERAL MEETING

In compliance with Listing Rule 9.6.1 Pennon Group Plc (the "Company") announces that the following documents have been submitted to the Financial Conduct Authority electronically via the National Storage Mechanism and will shortly be available for inspection at www.morningstar.co.uk/uk/NSM

Annual Report and Accounts 2016
Notice of Annual General Meeting
Form of Proxy

The Annual Report and Accounts 2016 and Notice of Annual General Meeting may also be viewed on the Company's website at www.pennon-group.co.uk

The Company will hold its 2016 Annual General Meeting at Sandy Park Conference Centre, Sandy Park, Exeter, Devon, EX2 7NN on Friday 1 July 2016 at 11.00am.

The following information in the Appendix to this announcement is as set out in the Company's Annual Report and Accounts 2016. It should be read in conjunction with the Company's Full Year Results announcement released on 25 May 2016 (and subsequently corrected on 27 May 2016) which included a set of consolidated financial statements, a fair review of the development and performance of the business and the position of the Company and its main trading subsidiary companies. Together these documents constitute the information required by Disclosure and Transparency Rule 6.3.5.

Helen Barrett-Hague
Group Company Secretary

1 June 2016

APPENDIX

PRINCIPAL RISKS AND UNCERTAINTIES

KEY

Risk Level:

| | |
|-------|--------|
| Green | Low |
| Amber | Medium |
| Red | High |

The low, medium and high risk level is our estimate of the **net risk** to the Group after mitigation. It is important to note that risk is difficult to estimate with accuracy and therefore may be more or less than indicated.

Current assessment of direction of travel of risk level:

| | |
|---|------------|
| ↑ | Increasing |
| ↔ | Unchanged |
| ↓ | Decreasing |

| LAW, REGULATION AND FINANCE | | | | |
|--|--|----------|-----------|--|
| RISK | MITIGATION | NET RISK | DIRECTION | RISK APPETITE |
| Compliance with law, regulation or decisions by Government and regulators, including water industry reform | <p>Robust regulatory framework ensures compliance with Ofwat, Environment Agency and other requirements. Full engagement in consultations on reform of policy and legislation, helps influence change through effective stakeholder relationships.</p> <p>Good progress has been made in preparing for regulatory reform. We are fully engaged in the Water 2020 programme including upstream regulatory reform. External reviews support the assurance letters required by the Market Operator.</p> | Green | ↑ | <p>High standards of compliance are sought with no appetite for legal and regulatory breaches.</p> <p>As regulatory reform is progressing, we aim to minimise the impact by targeting changes which are NPV neutral over the longer term, to protect shareholder value and customer affordability.</p> |
| Maintaining sufficient finance and funding to meet ongoing commitments | <p>Clear treasury and funding policies and an effective Group Treasury team.</p> <p>Funding in place at effective average interest rates below many in its sector, with prefunding and headroom, including revolving credit facilities, to meet future funding requirements.</p> | Green | ↔ | Ensure funding requirements are fully met by maintaining prudent headroom. |
| Non-compliance or occurrence of avoidable health | Rigorous health and safety compliance systems, policies and procedures are in place across the Group, supported by a | Amber | ↑ | High standards of compliance are sought with no |

| | | | | |
|---|---|-----------------|------------------|---|
| and safety incident | programme of capital investment to further reduce risk. | | | appetite for compliance breaches within the Group and third party operations. |
| Uncertainty arising from open tax computations where liabilities remain to be agreed | Professionally qualified and experienced in-house tax team, supported by external specialists. A dedicated team is working with HMRC to expedite the agreement of outstanding tax items. | Amber | ↑ | Full compliance with HMRC requirements. Residual risk is higher on some historic arrangements. |
| MARKET AND ECONOMIC CONDITIONS | | | | |
| RISK | MITIGATION | NET RISK | DIRECTION | RISK APPETITE |
| Non-recovery of customer debt. | <p>Water business debt collection strategies kept under review with new initiatives regularly implemented:</p> <ul style="list-style-type: none"> targeting previous occupier debt after customer moves; specific case management and use of court claims; and use of charging orders. <p>Affordability tariffs (e.g. Restart, WaterCare, FreshStart) help to reduce bad debt exposure for customers struggling to pay.</p> <p>Viridor's debt collection risk is lower due to the high proportion of public sector accounts.</p> | Amber | ↔ | Minimise non-recoverable debt. We recognise customer affordability challenges and that given the inability to disconnect domestic customers, some risk of uncollectable debt remains. |
| Macro-economic risks arising from the global and UK economic downturn impacting commodity and power prices. | <p>Viridor is well positioned across the waste hierarchy, with long-term contracts supporting the ERF segment. The ITOO (Input, Throughput and Output Optimisation) programme helps focus on recycling performance in mitigating the impact of global economic conditions on commodity prices.</p> <p>Energy risk management at a Group level acts as a natural hedge between South West Water (SWW) and Viridor, offsetting the drop in power prices. Existing investments that qualified for Renewable Obligation Certificates are protected by the 'grandfathering' procedure.</p> | Amber | ↑ | Taking well-judged risks and having response plans in place to mitigate external macro-economic risk factors down to an acceptable level. |
| OPERATING PERFORMANCE | | | | |
| RISK | MITIGATION | NET RISK | DIRECTION | RISK APPETITE |
| Poor operating performance due to extreme weather or | Contingency plans, emergency resources and investment through a planned capital programme mitigates the risks of extreme weather incidents. | Green | ↔ | Reduce both the likelihood and impact through long term planning and ensuring |

| | | | | |
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| climate change | <p>We prepare a Water Resources Management Plan every five years and review it annually for a range of climate change and demand scenarios, with various schemes promoted to maintain water resources (e.g. pumped storage for reservoirs), conservation and customer water efficiency measures.</p> <p>Viridor has in place a regional adverse weather management strategy, aimed at reducing disruption to site operations and transport logistics.</p> | | | sufficient measures are in place to mitigate risk. |
| Poor customer service/ increased competition leading to loss of customer base | <p>Targeted improvements made to improve customer service and SWW's relative industry standing during the K6 period.</p> <p>Viridor's strategy to diversify into energy recovery has offset the decline in landfill and current challenges in recycling. Viridor is exploring alternative uses for its landfill assets.</p> | Amber | ↑ | <p>Good customer service is at the heart of everything we do. Continually seek to increase customer satisfaction.</p> <p>Minimise the impact of market reform by defending the existing customer base whilst developing further markets.</p> |
| Business interruption or significant operational failures/ incidents | <p>Detailed contingency plans and incident management procedures.</p> <p>Equipment failure is managed through sophisticated planned preventative maintenance regimes. Any disruption is alleviated by good liaison and communication.</p> | Amber | ↑ | Effective business continuity and contingency plans in place to mitigate the risk and accelerate the recovery from an incident, with residual risk covered by insurance. |
| Difficulty in recruitment, retention and development of appropriate skills, which are required to deliver the Group's strategy | Succession plans are in place. The recent Group restructure, Viridor transformation and integration of Bournemouth Water has strengthened the executive team, but in turn have the potential to impact morale. | Green | ↔ | Appropriate skills and experience in place, with good succession plans to mitigate impact on strategic plan. |
| BUSINESS SYSTEMS AND CAPITAL INVESTMENT | | | | |
| RISK | MITIGATION | NET RISK | DIRECTION | RISK APPETITE |
| Failure or increased cost of capital projects/ exposure to contract failures | Skilled project management resource and oversight boards provide rigour to the delivery of major projects. Due diligence on suppliers, technologies and acquisitions. Back-to-back agreements and supplier guarantees provide | Amber | ↔ | Pennon's investment activities are based on taking well-judged risks for appropriate returns. |

| | | | | |
|--|--|--------------|---|--|
| | <p>protection.</p> <p>Regular reporting of performance on major contracts and post project appraisals.</p> | | | |
| Failure of information technology systems, management and protection including cyber risks | <p>Major systems implementation is supported by a formal programme governance framework, supplemented by specialist consultants.</p> <p>Cyber risks are mitigated by a strong information security framework, cyber security awareness campaigns, plus internal and external testing and formal ISO accreditation.</p> | Green | ↑ | Robust systems in place to support business activity, with strong cyber protection to minimise a growing risk. |

DIRECTORS' RESPONSIBILITIES STATEMENTS

(This statement is extracted from the governance section of the Annual Report 2016 and page numbers referred to are those in the Annual Report 2016.)

The Directors are responsible for preparing the annual report, the Directors' remuneration report and the financial statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare financial statements for each financial year. Under that law the Directors have prepared the Group and Company financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union.

Under company law the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Group and the Company and of the profit or loss of the Group for the year.

In preparing these financial statements the Directors are required to:

- select suitable accounting policies and then apply them consistently
- make judgements and accounting estimates which are reasonable and prudent
- state whether applicable IFRSs as adopted by the European Union have been followed, subject to any material departures disclosed and explained in the financial statements.

The Directors confirm that they have complied with the above requirements in preparing the financial statements.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions, and disclose with reasonable accuracy at any time the financial position of the Group and the Company; and enable them to ensure that the financial statements and the Directors' remuneration report comply with the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the International Accounting Standards (IAS) Regulation. They are also responsible for safeguarding the assets of the Group and the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Each of the Directors, whose names and functions are listed on pages 60 and 61, confirms that, to the best of his or her knowledge:

- i) The financial statements, which have been prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union, give a true and fair view of the assets, liabilities, financial position and profit of the Group and of the Company.
- ii) The strategic report (pages 4 to 55) and the Directors' report (pages 99 to 101) include a fair review of the development and performance of the business during the year and the position of the Company and the Group at the year end, together with a description of the principal risks and uncertainties they face.
- iii) Following receipt of advice from the Audit Committee, that the annual report, taken as a whole, is fair, balanced and understandable, and provides the information necessary for the shareholders to assess the Group's performance, business model and strategy.

The Directors are responsible for the maintenance and integrity of the Company's website www.pennon-group.co.uk. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

RELATED PARTY TRANSACTIONS

(The following is Note 46 to the Financial Statements set out in the Annual Report 2016.)

During the year Group companies entered into the following transactions with joint ventures and associate related parties who are not members of the Group:

| | 2016 £m | 2015 £m |
|---|------------|------------|
| Sales of goods and services | | |
| Viridor Laing (Greater Manchester) Limited | 87.3 | 99.0 |
| INEOS Runcorn (TPS) Limited | 18.5 | 5.6 |
| Purchase of goods and services | | |
| Viridor Laing (Greater Manchester) Limited | 0.3 | - |
| Lakeside Energy from Waste Limited | 12.1 | 12.6 |
| INEOS Runcorn (TPS) Limited | 4.3 | 1.1 |
| Dividends received | | |
| Lakeside Energy from Waste Holdings Limited | 6.0 | 6.0 |

Year-end balances

| | 2016 £m | 2015 £m |
|--|------------|------------|
| Receivables due from related parties | | |
| Viridor Laing (Greater Manchester) Limited (loan balance) | 36.8 | 57.2 |
| Lakeside Energy from Waste Limited (loan balance) | 8.9 | 9.3 |
| INEOS Runcorn (TPS) Limited (loan balance) | 35.5 | 31.4 |
| | 81.2 | 97.9 |
| Viridor Laing (Greater Manchester) Limited (trading balance) | 11.3 | 12.8 |
| Lakeside Energy from Waste Limited (trading balance) | 1.0 | 1.0 |
| INEOS Runcorn (TPS) Limited (trading balance) | 2.7 | 5.6 |
| | 15.0 | 19.4 |
| Payables due to related parties | | |
| Lakeside Energy from Waste Limited (trading balance) | 2.3 | 1.1 |
| INEOS Runcorn (TPS) Limited (trading balance) | 1.6 | 0.1 |
| | 3.9 | 1.2 |

The £81.2 million (2015 £97.9 million) receivable relates to loans to related parties included within receivables and due for repayment in instalments between 2016 and 2033. Interest is charged at an average of 13.0% (2015 13.0%).

Company

The following transactions with subsidiary undertakings occurred in the year:

| | 2016 £m | 2015 £m |
|---|------------|------------|
| Sales of goods and services (management fees) | 10.5 | 9.5 |
| Purchase of goods and services (support services) | 0.4 | 0.5 |
| Interest receivable | 38.6 | 35.6 |
| Interest payable | 0.1 | 0.1 |
| Dividends received | 140.7 | 311.6 |

Sales of goods and services to subsidiary undertakings are at cost. Purchases of goods and services from subsidiary undertakings are under normal commercial terms and conditions which would also be available to unrelated third parties.

Year-end balances

| | 2016 £m | 2015 £m |
|---|------------|------------|
| Receivables due from subsidiary undertakings | | |
| Loans | 965.6 | 936.6 |
| Trading balances | 8.6 | 8.5 |

Interest on £70.0 million of the loans has been charged at a fixed rate of 4.5%, on £373.6 million at a fixed rate of 5.0%, on £28.0 million at a fixed rate of 6.0% and on £0.5 million at a fixed rate of 1.4% (2015 £70.5 million at 4.5%, nil at 5.0%, £332.5 million at 6.0% and £0.5 million at 1.4%). Interest on £443.5 million of the loans is charged at 12 month LIBOR +1.0% (2015 £403.1 million). These loans are due for repayment in instalments over the period 2016 to 2043.

Interest on £50.0 million of the loans has been charged at 1 month LIBOR + 1.0% (2015 £130.0 million). This loan is expected to be repaid in 2016/17.

During the year there were no provisions (2015 nil) in respect of loans to subsidiaries not expected to be repaid.

| | 2016 £m | 2015 £m |
|--|------------|------------|
| Payables due to subsidiary undertakings | | |
| Loans | 287.2 | 283.2 |
| Trading balances | 14.6 | 14.6 |

The loans from subsidiary undertakings are unsecured and interest-free without any terms for repayment.

1 June 2016

www.pennon-group.co.uk

End transmission