

## PENNON GROUP PLC

### PUBLICATION OF ANNUAL REPORT AND ACCOUNTS 2012

### 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 UK Listing Authority electronically via the National Storage Mechanism and will shortly be available for inspection at [www.Hemscott.com/nsm.do](http://www.Hemscott.com/nsm.do)

Annual Report and Accounts 2012

Notice of Annual General Meeting

Form of Proxy

The Annual Report and Accounts 2012 and Notice of Annual General Meeting may also be viewed on the Company's website at [www.pennon-group.co.uk](http://www.pennon-group.co.uk)

The Company will hold its 2012 Annual General Meeting at Sandy Park Conference Centre, Sandy Park Way, Exeter, Devon EX2 7NN on Thursday, 26 July 2012 at

11.00 a.m.

The following information in the Appendix to this announcement is provided for the purposes of compliance with Disclosure and Transparency Rule 6.3.5 and is as set out in the Company's Annual Report and Accounts 2012. It should be read in conjunction with the Company's Preliminary Results announcement released on 29 May 2012 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 two main trading subsidiary companies (South West Water Limited and Viridor Limited). Together these constitute the information required by Disclosure and Transparency Rule 6.3.5 to be communicated to the media in full unedited text.

Kenneth D. Woodier

Group Company Secretary

28 June 2012

## APPENDIX

### Director's Responsibilities Statements

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 44 and 45 (*of the Annual Report and Accounts 2012*), confirms that, to the best of their knowledge:

a) the financial statements, which have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU, give a true and fair view of the assets, liabilities, financial position and profit of the Group and of the Company and

b) the Directors' report contained on pages 2 to 41 (*of the Annual Report and Accounts 2012*) includes a fair review of the development and performance of the business and position of the Company and the Group, together with a description of the principal risks and uncertainties they face.

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

## Principal Risks and Uncertainties

| RISK  | COMMENTARY  | MITIGATION   | CHANGE           |
|---|---|--|------------------|
| <b>LAW AND REGULATORY</b>   |   |  |                  |
| Changes in law, regulation or decisions by Governmental bodies or regulators could have a material adverse effect on our financial results or operations. | There is a wide range of laws and regulations and policy decisions of government and regulators which could have a materially adverse effect on the results of operations of both South West Water and Viridor. Examples of laws and regulatory changes include:<br>The transfer of private sewers to South West Water which took place on 1 October 2011 and the further adoption of private pumping stations which is due to take place up to 2016. | The general direction of travel of Government policy in both business areas is known and each company is actively involved in consultations on regulatory changes.<br><br>Operational plans to manage customer contacts and deliver service to customers were implemented smoothly and activity has been at the lower end of the range. Appropriate risk management activities are undertaken to monitor progress and a strategy is in place to manage for the further adoption of pumping. Operating and capital costs incurred efficiently will be funded by future adjustments to price limits. | ↔<br><br>(Amber) |
|   | Performance of South West Water against key regulatory outputs.   | They are monitored on a monthly basis and where performance falls short, corrective programmes are developed and implemented to target recovery in specific areas. Internal monitoring and   | ↓<br><br>(Green) |

|   |  |              |
|---|--|--------------|
|   | assurance programmes are undertaken through the year and annual data is supported by external verification through the South West Water external auditors to provide assurance on compliance.  |              |
| The Government's Water White Paper signals an evolutionary approach to market and regulatory reform over a period to 2025 and beyond. Legislation is required for a number of the changes and draft legislation is anticipated in 2012/13. The development of greater competition in the water industry could reduce South West Water's revenues. | As part of its risk management and business strategic planning processes, the company evaluates developments and proposals for competition which could provide opportunities for business expansion. South West Water is prepared for the development of retail competition, with the launch of 'Source for Business', offering enhanced services to commercial customers. The company has evaluated proposals for regulatory reform and contributed fully to the Ofwat consultations on regulatory price setting and other forms of dialogue with regulators and stakeholders in order to effectively convey its views. | ↔<br>(Amber) |
| Climate change and resulting increased regulatory standards could increase costs for South West Water.  | The company has plans ready and will adapt the way it conducts its business to respond effectively to the changing weather conditions.   | ↔<br>(Green) |
| The UK has landfill diversion, recycling and recovery targets   | Viridor's strategy is to grow in recycling and energy from waste where   | ↔<br>(Green) |

|   |  |
|---|--|
| which, together with the impact of both WEEE Regulations, higher Producer Responsibility obligations and pretreatment requirements, plus rising landfill tax, will continue to further reduce landfill volumes for Viridor and potentially, over time, landfill asset values. | <p>margins per tonne are much higher than in landfill.</p> <p>Increasing landfill tax increases the economic attractiveness of recycling and energy from waste.</p> <p>The new Resource Efficiency Agenda emanating from the EU and the UK Government's attention to resource and electricity security are expected to provide further opportunities for Viridor.</p>  |
| The ever increasing demand for higher standards, in areas such as health and safety, environmental performance and employee welfare increase costs for both South West Water and Viridor.   | <p>These issues for South West Water are addressed in the five-year regulatory price review mechanism through future adjustments to price limits but there is a risk that some additional costs will not be funded immediately, in part or at all.</p> <p>Within Viridor higher costs are sometimes but not always recovered through contractual arrangements with waste authorities and other customers.</p> <p>↔</p> <p>(Green)</p> <p>Additionally Viridor continues to develop its Business Management Systems to address costs and maintain high standards of compliance by improving its management controls. Viridor also maintains a close interest in industry developments via the</p> |

waste sector trade association and therefore is often at the forefront of planned changes.

## ECONOMIC CONDITIONS

Economic conditions could materially affect the Group's revenues and profitability.

The Group does have exposure to reduced economic activity, inflation/deflation and the impact of the current Eurozone uncertainties. However South West Water's revenues are economically regulated through the price review mechanism and Viridor has a diversified revenue stream which includes exports to countries such as China and India whose economies are more buoyant than the UK and Europe. Examples of specific areas of impact are:

South West Water's revenues can be impacted by higher bad debts and customer affordability. In addition to existing debt reduction strategies (such as WaterCare+, Restart and the Fresh Start Fund), which are kept under review, the company continues to implement new initiatives to improve and secure cash collection, including the

↔

(Amber)

use of third party collection agencies and introduction of a new billing and collection

business 'Source Contact Management'. The Government's commitment to tackle 'unfairness' issues for the company's bill payers, where 3% of the population pay for 30% of the UK's bathing waters, has also moved

|   |  |                              |
|---|--|------------------------------|
|   | forward with legislation passed for a £50 reduction in bills for householders from 2013/14.  |                              |
| South West Water has 73.4% of its domestic customer base metered and as a result the revenue from these customers can be more volatile from changes in usage which can  | The financial impact of changes in customer demand are mitigated through the regulatory Revenue Correction Mechanism, whereby shortfalls in revenue in one five year regulatory pricing period are adjusted in the following period. | ↔<br>(Green)<br>↔<br>(Amber) |
| be affected by a number of factors including:   |  |                              |
| -- abnormal weather impacts   | A number of the company's other income streams are vulnerable to downturns in economic activity, particularly in the property market affecting new connections, searches and mains diversion activity.                               |                              |
| -- increased water efficiency   |  |                              |
| -- recession impacting commercial customers.  |  |                              |
| Viridor has seen residual waste landfill and collection volumes reduce due to the recession and the long-term trend towards recycling and energy from waste.  | Viridor's strategy is focused on growing in recycling and energy from waste where margins per tonne are much higher than   | ↔<br>(Amber)                 |
|   | in landfill.   |                              |
| Viridor's commodity trading arm (VRM) trades where the market is most favourable. However, Viridor remains susceptible to global economic demands and the weakness of the Eurozone is having a depressing effect on the prices of internationally traded recyclates. A breakdown of the Eurozone would intensify the downward pressure on | Under the terms of its customer supply contracts and by management action Viridor has been able to offset more than 50% of the impact of price reductions in recyclates.   | ↑<br>(Amber)                 |
| prices. In addition competition for recyclables   |  |                              |



from other contractors via aggressive pricing has been a recent trend.

The Government's spending Review has put pressure on local authority services, including household waste

recycling centre operations which is expected to have a short-term impact.

Viridor provides best value services and competitive procurement bids to its public sector customers. (Green)

## FINANCE AND FUNDING

Access to finance and funding costs may be adversely affected by perceived credit rating and prolonged periods of market volatility or liquidity. There are covenant limits and restrictive obligations on our borrowing and debt

arrangements.

The Group may be unable to raise sufficient funds to finance its activities or such funds may be only available at higher cost.

The Company has robust treasury policies in place which include always having prefunded surplus cash and/or committed facilities to cover at least one year's estimated cash flow and arranging for no more than 20% of net borrowing to mature in any one year. In addition in respect of South West Water the economic regulator has a statutory duty to ensure that it is able to finance its functions in the normal course. The Group has to date obtained funding at lower effective average interest

rates compared to many other companies in its sector and is well placed to meet the funding requirements of both South West Water and Viridor in the foreseeable future. The Group had £1 billion of cash and facilities as at 31 March 2012 including over £0.5 billion of new/refinanced facilities sourced during the year.

## OPERATING

## PERFORMANCE

Poor operating performance

or a failure or interruption of

our operating systems or the

inability to carry out network

operations or damage to

infrastructure may have a fixed costs.

material adverse impact on both our financial position and reputation.

Poor operating performance for both South West Water or Viridor could result in enforcement action,

prosecutions, loss of permits and civil action which could all result in negative publicity, regulatory penalties, loss of customer confidence due to poor performance and eventually, reduced demand for services and increased

Within South West Water a major network failure or interruption may be suffered or the company may not be able to carry out critical network

operations. Operational performance could be materially adversely affected

by a failure to maintain the health of the system or network which could cause South West Water to fail agreed standards of service or specified quality standards.

Specific measures taken by South West Water include: ↔ (Green)

- a number of schemes in place to maintain water resources (such as pumped storage for certain reservoirs) and the promotion of conservation

measures and customer water efficiency measures

- a Water Resources Plan prepared every five years and which is reviewed annually for a range of climate change and demand scenarios. The current Water Resources Plan indicates that no new reservoirs are required

before the planning horizon of 2035. However, due to the impacts of climate change, this position is reviewed frequently

- established procedures and controls in place, as well as contingency plans and incident management procedures. The company also maintains insurance policies in relation to these risks, although there can be no assurance that all or any of the costs associated with these risks would be covered

or that coverage will continue to be available in the future

- monitoring of significant assets by automated and remote operation and routine controls and operating procedures that are constantly kept under review. Asset management

techniques are employed to pre-empt the failure of assets to maintain stable serviceability and avoid regulatory penalties.

From 2011/12 a financial reward/penalty could be applied to South West Water at the next price review under Ofwat's Service Incentive Mechanism (SIM). This

While the company has seen

↑  
(Amber)

improvements in customer service particularly through reduced written

depends on South West Water's customer service

complaints, there is uncertainty over

performance relative to the industry average over the remaining K5 regulatory period.

South West Water's relative position in the industry. However there is a strategy

Viridor operates in a competitive marketplace where price and service are key precursors to success.

for 2012/13 in place to improve customer service further.

Sound policies and accredited procedures are in place with internal and external inspections, to maintain operations and achieve performance standards set. ↔ (Amber)

## CAPITAL INVESTMENT

The failure or increased costs of capital projects or acquisitions or joint ventures not achieving predicted revenues or performance could have a material adverse effect on both our financial position and reputation.

South West Water may not carry out its capital programme within the price limits and with the efficiencies determined by Ofwat.

The company does have a track record of delivering its capital programme in accordance with regulatory requirements and progress is regularly monitored and reviewed. ↔ (Green)

Within Viridor there are risks of project delays, cost overruns or contract failure which could be as a result of failure or insolvency on the part of

The company has experienced and dedicated project/contract teams; detailed due diligence on all projects, supplies, ↑ (Amber)

contractors or their subcontractors, or due to a new technology failing

technologies and acquisitions is carried out by experienced and qualified staff; and wherever possible back-to-back

performance requirements. There is also a risk of overpaying for an acquisition. With the increase in Viridor's project pipeline, Viridor

agreements with and guarantees from suppliers are entered into. There is also

recognises that this risk is increasing and is addressing it.

regular monthly reporting on performance on major contracts and post project appraisals are carried out which all assist in being able to improve future

performance.

## COMPETITIVE PRESSURES

|  |  |  |              |
|--|--|--|--------------|
| A reduced customer base, increased competition affecting prices or reduced demand for services could have a material adverse impact on our financial position. | Viridor is experiencing increased competitive pressures in a number of areas of its business including in particular on recycle volume and prices, landfill gate fees and bidding for Public Private Partnership contracts (PPPs). Recycling has been recognised as an attractive business by an increasing number of competitors. | Viridor provides recycling and waste management services which are locally delivered services from locally managed facilities and a significant proportion of its revenue is contracted over the medium or long-term. With regard to major competitive projects being pursued there are barriers to entry due to planning permissions being difficult to obtain and significant investment requirements. | ↑<br>(Amber) |
|  | Competitive pressures in respect of South West Water are referred to in the first risk set out at the beginning of this section.   |  |              |

## BUSINESS SYSTEMS

|   |  |   |              |
|---|--|---|--------------|
| Information technology and business continuity systems and processes may fail which may cause material disruption to the Group's businesses and could have a material | There always remains a risk of interruption, failure or third party intervention that could have a material adverse impact on the operations of South West Water's business. | The company has well developed IT systems and continuity systems in place. The further impact of a system failure or disruption to the company has been reduced with the refurbishment of the data centre at its head office and the establishment of a geographically separate alternative data centre, which is hosted by a third | ↓<br>(Green) |
|---|--|---|--------------|

adverse

party

impact on both our  
financial

communications provider.

position and reputation.

|                                |                            |         |
|--------------------------------|----------------------------|---------|
| Some of Viridor's IT systems   | Viridor has increased its  | ↔       |
| require replacement,           | IT management and          |         |
| development or upgrading to    | technical resources        | (Amber) |
| meet the growing               | accordingly. It also has a |         |
| requirements of the business   | comprehensive              |         |
| and in some areas new          | development programme      |         |
| technology being introduced    | and plans in place to      |         |
| may not operate                | address the deficiencies   |         |
|                                | identified and seek to     |         |
|                                | ensure business            |         |
| or perform according to stated | continuity in the event of |         |
| specification requirements.    | failure.                   |         |

#### Key

↔ Unchanged during year

↑ Increased during year

↓ Reduced during year

#### Risk Level

Green Low

Amber Medium

Red High

The colouring (red, amber, green) is the Group's estimate of the inherent risk level to the Group after mitigation. It is important to note that risks are difficult to estimate with accuracy and therefore the risks may be more or less significant than indicated.

28 June 2012

[www.pennon-group.co.uk](http://www.pennon-group.co.uk)