Bringing Water to Life

Supporting the lives of people and the places they love for generations to come

Pennon

Annual Report and Accounts

2023

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Our front cover picture of Fernworthy Reservoir was taken by Georgia Hawking, a people admin team leader at Pennon Group.

Fernworthy Reservoir, Dartmoor National Park

Our reporting suite

Clear and transparent reporting is important to us and our stakeholders. Our annual report is supported by additional disclosures contained in our wider corporate reporting suite. These include:

Net Zero plan

Modern slavery statement

ESG Databook 2023

Gender and Ethnicity Pay Gap Report 2023

Visit us online

Our annual report and the other reports in our corporate reporting suite can be found on our website **www.pennon-group.co.uk/investor-information/financial-reports-and-presentations**

Year at a glance

Making progress on our key priorities

Improving the environment

100%
bathing water quality – second consecutive year

c.30% reduction
in storm overflow use

c.50% reduction
in wastewater pollutions in 2 years

Water quality and resilience

Augmented
supply and storage
schemes

New resources
repurposing of quarries

Driving demand-side initiatives

Net zero environmental gains

Sustainable living

Championing renewables

Reversing carbon emissions

Carbon footprint
reduced by c.40%
since 2021

80%
of catchments improved

Addressing customer affordability

Below inflation
bill increases for 2023/24

Second issuance
of

c.£85 million
customer support to date

Record capital investment

c.£358 million
capex in 2022/23

c.50% increase
in 2022/23

Investing over
£750million
over the next two years

Financially resilient

Double digit
RORE

11.1%

4.6%

60.8% gearing
year on year reduction

Pension scheme in
surplus

Chair's letter

Gill Rider
Chair

"We continue to focus on leading a sustainable business that delivers for customers, colleagues, our shareholders and the UK."

Thank you to our employees

I would like to start by recognising everyone who works for Pennon. They deserve credit for what we have achieved this year. With over 3,000 people, and nearly the same number of supply chain partners, it's their dedication, care and consideration for customers and each other, as well as their passion for the places they live and work in, that has enabled us to deliver another year of robust results. It has not always been easy for them with the media headlines shining a spotlight on what we can and need to do better. On behalf of the Board, I thank you all, and we are proud of what you do.

Challenging times for the UK Water sector

We have made steady progress in delivering our strategy, and our operational commitments across all parts of the Group, with strong leadership from our Executive Team. However, there is more we need to do, more rapidly, to modernise our Victorian sewage system, and to protect the environment.

The Board are focused on planning, prioritising and investing in the changes needed. We are listening to our customers, stakeholders and regulators. We all share the same view; this is a multi-generational challenge, and one that will take time to achieve sustainably. We can and must make progress in the short-term too.

Our focus has been on reducing the use of storm overflows and we have seen a 30% fall in numbers. Continuing on this trajectory will achieve our planned 50% reduction by 2025. We also continue to reduce pollution levels with sustained improvements of 50% over each of the past 2 years. This is integral to improving our EPA performance. This remains a key area of focus for the Board.

The effects of climate change have also been felt severely in the South West, given our topography and 860 miles of coastline and adjacency to the Atlantic Ocean. We have experienced extreme weather patterns, from storms to freezing temperatures and sustained periods of drought. It is clear we all need to do more to safeguard the planet for future generations and we are making progress with our Net Zero ambitions to 2030.

The drought has brought into clear focus how important it is that we are able to supply world-class drinking water to all our customers. We are therefore investing in additional water resource capacity for Cornwall and Devon. We are also on track to deliver new water treatment works for Bournemouth customers.

Finally, it has been pleasing to see continued progress and growth in our non-household retail businesses Pennon Water Services and water2business, with strong customer service.

Many are struggling financially in these challenging economic times.

The cost of living crisis has continued to weigh heavy on many. Our region, given its dependency on agriculture and tourism, can experience socio-economic challenges. Our Board commitment to eradicate water poverty has remained a priority. We have kept bill increases below the rate of inflation, lower than the average sector bill rises seen elsewhere and in other utilities. We have focused on those most in need with over 110,000 customers benefiting from our broad range of affordability initiatives.

We also recognise that the same cost of living pressures are being felt by our employees and it was right therefore that we have awarded our highest ever pay award to those earning the least and those focused on delivering for our customers and communities. We also continue to be a living wage foundation employer for all.

Strengthening our Board, championing diversity

This coming year will be my last as Chair, and I am grateful to work alongside a talented and diverse Board. This year we have focused on Board succession, and I am pleased to welcome Dorothy Burwell and Loraine Woodhouse as new independent Non-Executive Directors. Loraine will succeed Neil Cooper as Audit Chair when he steps down this summer, having served on the Board since 2014 alongside me. I would like to thank Neil for his wise counsel and careful stewardship over many years and in his role as Senior Independent Director.

For the first time in Pennon's history, more women now serve on the Board than men, and Susan and I continue to be strong advocates for championing inclusion and diversity. I am encouraged by the good progress being made across the Group, in building a more inclusive culture, and particularly in our graduate and apprenticeship programmes as we build the workforce we need for the future. We are making our largest ever investment in skills and people, with a doubling of apprenticeships and graduates to 1,000 and we will also offer 5,000 work placements over the same period. We do this, because it is important we have people with the right skills to deliver for our customers and the environment, and also in doing what's right in a region where one in three constituencies score above the national average for deprivation.

The Group continues to deliver on its commitments to our wider stakeholders.

We continue to grow a sustainable business that delivers for customers, colleagues, our shareholders and the UK. Our loyal shareholders include UK pension funds, savings funds, charities, employees and customers. Pennon's dividend policy of CPIH + 2% reflects the Board's continuing confidence in the longer-term sustainable growth strategy, and in recognition of the ongoing investment required to deliver for the future.

The Board is recommending a final dividend of 29.77 pence per share for the year ended 31 March 2023. Together with the interim dividend of 12.96 pence per share paid on 5 April 2023, this gives a total dividend for the year of 42.73 pence.

In summary

Pennon is ready to lead through to the next phase of the water sector's evolution. Coupled with our ongoing investments in people, assets and continuing strong financial and operational discipline, we are confident we will continue to grow and deliver for all our stakeholders.

Gill Rider
Chair

31 May 2023

You can read more on how we are engaging with our stakeholders in our Section 172(1) statement on page 112.

c.110,000

customers benefited from our broad range of affordability initiatives

Knapp Mill Water Treatment Works, Bournemouth

Chief Executive Officer's review

Reflections on the Year

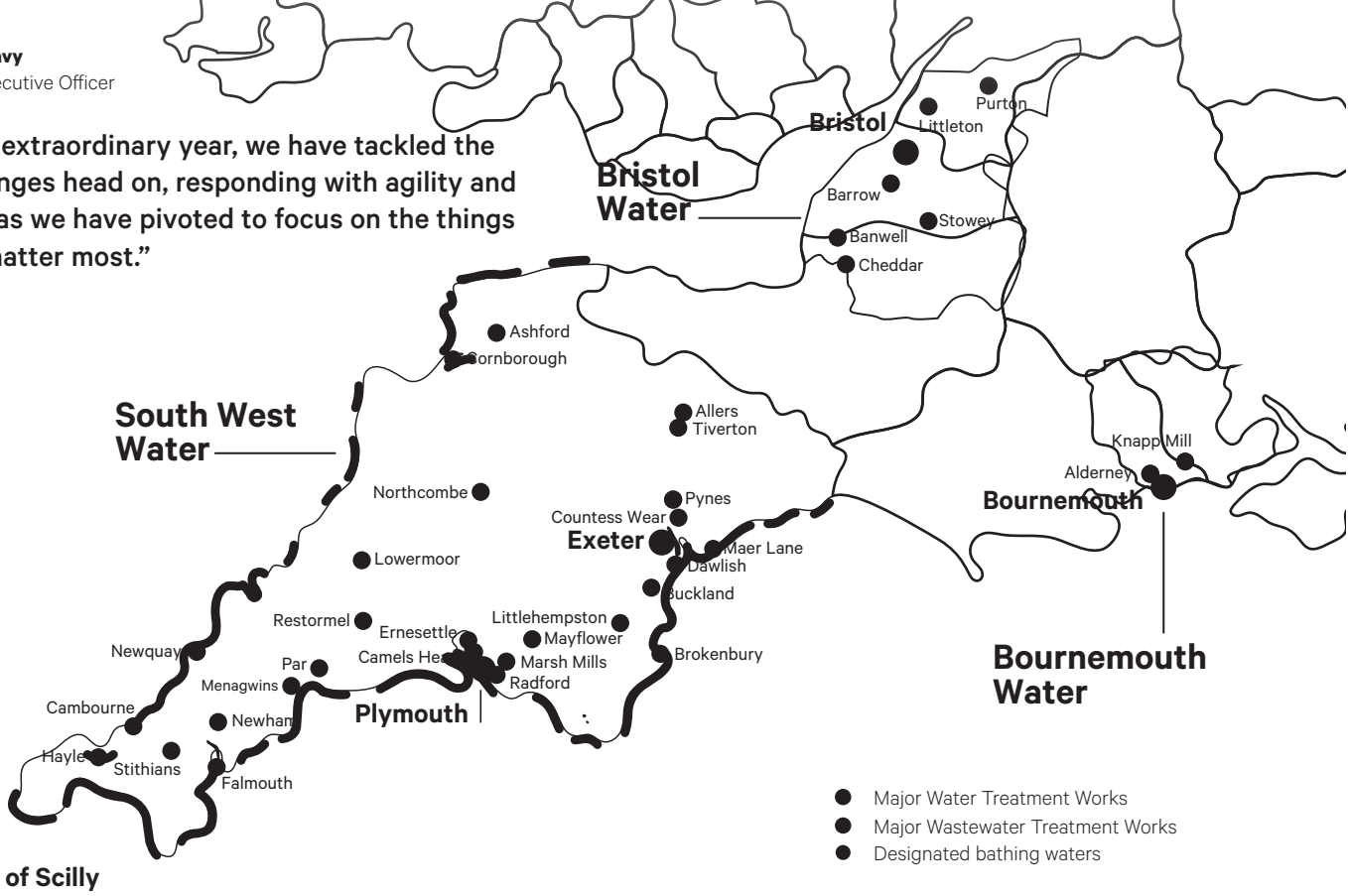
As I reflect back on the year, this has been an extraordinary one, in which extreme weather patterns have tested our operational resilience. At the same time, inflationary pressures have tested our financial resilience. We have been able to respond to both with agility and pace, pivoting to focus on the things that matter right now, and tackling the biggest challenges head on. Whether it's the use of storm overflows, water resilience, the cost of living crisis or climate change, we are investing more than ever before. We couldn't do any of this without the support, dedication and pioneering spirit of our c.3,000 employees, who see opportunities where others see challenges, and I am so proud of 'Team Pennon'. We continue to invest in our leaders of the future, doubling our apprenticeship and graduate schemes to 1,000 by 2030. This year, we were awarded Gold membership of the 5% club, in recognition of our efforts to provide "earning and learning opportunities" to our employees. And we have also strengthened our executive capability across the year, with new appointments, and as we have successfully integrated Bristol Water into the Group.

We have been well placed to respond

Our business model ensures we have the headroom and capacity to be fleet of foot, tackling challenges head-on and taking opportunities when they arise. Overall, we are investing more than ever before, re-baselining our capital investment to over £350 million in the year to become the new normal, and with plans to spend at least the same again, each year, for the remaining period to 2025 and as part of our £1.5 billion environmental investment programme over K7.

Susan Davy
Chief Executive Officer

"In an extraordinary year, we have tackled the challenges head on, responding with agility and pace, as we have pivoted to focus on the things that matter most."



£100m
investment planned to 2025 to protect our coastline and rivers

Living by our values

It's also a year in which the UK Water sector has been rightly challenged to clean up its act. The use of storm overflows has become the unacceptable face of a Victorian sewage system, once revered across the globe. Like all water companies in the UK, we've relied on storm overflows to prevent sewage filling our streets and flooding our houses. The release from storm overflows can result in diluted raw sewage going into our rivers and seas and it is not acceptable, it puts at risk the bathing water quality standards, it is wrong and it must stop.
The Board and I are clear that we can and we need to do more to protect our environment.

As CEO, it's my role to set the tone from the top, to lead by example and champion living our values. It's also right that we reset to build trust in the sector, and for our customers and communities to feel listened to. For this reason, with the full support of the Board, and given the cost-of-living crisis weighing heavy on many customers, I will not be taking either my annual bonus or long-term incentive award for this year. Instead, the funds will go where it's needed most, to our customers, as part of our unique WaterShare+ scheme.

Tackling challenges head on

Looking beyond the headlines, there has been progress. We are building momentum and making record levels of investment. One year ago, we launched WaterFit, our plan for healthy rivers and seas as part of c.£100 million of investment to 2025 focused on the protection of our 860 miles of coastline and rivers in the South West. This includes an additional c.£45m reinvestment of out-performance.

This includes the things our customers care about most such as bathing water quality, where for the second year running, we have achieved 100% as measured by the Environmental Agency, and in their testing of harmful bacteria in our seas. This compares to 70% across the rest of the sector.

For 2022, overflow spills reduced by 30% and we remain on target to reduce spills by 50% by 2025. Whilst undoubtedly the drier weather will have played a part, the majority of the improvements are down to interventions made whether capital investment to increase network capacity or through proactive maintenance.

With 100% monitoring of storm overflows now in place, a year ahead of plan, we launched WaterFit Live, giving customers and visitors near time information about their favourite bathing beach, and storm overflows, as well as the detailed investments we are making to reduce overflow spills across the region's coastline by 2025, with 49 beaches prioritised. Through #Your beach, Your Say, Our investment, we will empower our customers and communities to work together to plan our next phase of improvements.

We continue to drive down pollution levels, as we committed to, with a 50% overall reduction since 2020, a 75% reduction in the number of serious incidents and maintaining our record of zero category 1 incidents. Continuing this trajectory to 2024 will see us achieve the lowest number of absolute pollution numbers. Our focus continues in rising main replacements, installing 9,000 sewer depth monitors and continuing our investment in technology and innovation. We anticipate that this performance will see us regain our EPA rating of 2 star for 2022 and we remain focused on achieving 4 star for 2024.

Against our pledge to reduce our impact on rivers by one third by 2025, we are well on our way to mitigate impacts from our own assets and practices. Through sewer separation and four phosphorous schemes completed during the year our impact has reduced from 19% to 12.6%. In addition, our pilots on the rivers Dart and Tavy to explore how we might achieve the region's first bathing quality river, are well underway. Given this is a community-led designation process, we have been bringing together stakeholders and community groups to work collaboratively.

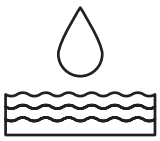
This was also a year where in addition to drought, we saw some of the worst storms, with freezing temperatures, rapid thawing and flooding. It's clear that the impact of climate change is here now, and we all need to play our part in protecting precious resources. Delivering on our Net Zero 2030 commitment is more important than ever, and we are making good progress in all 3 areas of our promise to the planet – sustainable living, championing deliverables and reducing carbon emissions. We are investing c.£160m in renewable energy generation, having made the first acquisition of a PV solar site, with more planned to counteract the ongoing volatility of the energy markets. We have improved 80% of the catchments we work in, through activities such as peatland restoration and tree planting. We have also reduced our carbon emissions by c.40% since 2021.

The weather impacts, and need to pivot, ensuring we have focused on the areas that have mattered most, has impacted our stretching business plan delivery, with SWW at 70%, and Bristol Water at 65% of ODIs.

Water resilience and water quality

Water is essential for life. The supply of clean and safe drinking water remains our top priority and it's easy for this to have become overshadowed in people's minds given the attention on storm overflows. We can never be complacent and it's the reason we take a "quality first" approach to ensuring we can always provide clean and safe drinking water to our customers. We operate across a unique topography where over 90% of water resources are derived from rivers and reservoirs. None of our strategic reservoirs are directly connected to treatment works, and therefore the efficacy is directly driven by the health of the rivers. This means it's the low river flows that will drive the depletion of a reservoir, which act as a storage facility in drier months.

The last six months of 2022 were exceptional. We experienced the hottest, driest, weather on record and a consequence of climate change. A combination of a lack of rain, the fourth driest period in 130 years, extreme heat, with high levels of soil moisture, and increased demand as a result of population growth, uniquely converged to put pressure on one of our five strategic reservoirs. Colliford reservoir, serving Cornwall, was depleted as we sought to continue to protect the river health in the region.



130,000 free water saving devices issued as part of our 'Stop the Drop' campaign

The pace and speed in which we have been able to deploy innovative solutions, using tried and tested models elsewhere in our region, and with shareholder support was key. In the space of less than a year, we have built 25% more expanded capacity for Cornwall and 12% for Devon, and with a £125 million investment to ensure future resilience. Using our learnings from the Isles of Scilly's successful use of desalination, this is now an important component of our future water resource strategy, and we are well into progressing plans. Our proactive and speculative acquisition of disused mining quarries over the past 15 years, re-purposing them as water resources, meant we could provide additional storage in the second half of the year, and we continue to do so, alongside building new pipelines. We have increased our leakage activities, as well as fixing customer side leaks for free, and have routinely fixed three times the planned levels averaging around 2,000 a month.

On the demand side, the success of South West Water's unique and innovative Stop the Drop campaign, where the campaign gained traction as the collective might of the people came together to see a sustained reduction in customer demand (c.5%) over the period, has been a useful learning. We continue to engage with our customers to influence behavioural change, through our now ongoing customer campaign Save Every Drop, and in issuing over 130,000 free water saving devices from water butts to shower heads. At the same time, we are focused on reducing our own usage on our sites.

Against a worse credible planning scenario, we are better positioned because of the actions we have already taken, and what we plan to do. Furthermore, our acquisition of Bristol Water, driven by synergies and strategic water resource benefits, and our commitment to progress the Cheddar 2 reservoir, will bring benefits to the Greater South West over the longer-term including the neighbouring Wessex region.

Susan at the 'Topping Out' ceremony for the Centre for Resilience in Environment, Water and Wastewater (CREWW), Exeter University

Financial Resilience

Driving out-performance give us the flexibility to deliver more within a regulatory delivery period. Our RORE performance for 22/23 continues to be strong with South West Water achieving 11.1% and Bristol Water 4.6%. This supports our cumulative Group RORE position of 8.7%, equating to £192 million and an increase on £149 million in 2021/22. This out-performance, combined with the strength of our balance sheet, is supporting c.£300 million of additional and accelerated initiatives. We have also been able to absorb the impact of elevated inflation on power and interest costs during the year, reducing our gearing to 60.8% as well as ensuring our pension scheme remains in surplus.

We are a stronger business as One Pennon.

In February we successfully concluded the licence and statutory transfer of Bristol Water, successfully TUPEing employees into South West Water. As part of One Pennon, it is now easier to share best practise, for example our approach to Quality First, in ensuring clean and safe drinking water is at the top of our priorities. In April, Ofwat also announced their draft Accelerated Programme, which includes an additional £125 million investment to 2030 and just under half will be delivered in the current regulatory period. This builds on our existing investments in the region including Green Recovery, WaterFit and Stop the Drop initiative.

At the same time, we are making complementary investments in renewal energy generation and storage. Our £160 million investment will significantly accelerate the Group's 2030 Net Zero target for 50% self-generation as well as reducing our reliance on the volatility of global power markets.

Furthermore, our sustainable and profitable B2B businesses, Pennon Water Services and Water2business, with a combined market share of 12% continue to win contracts and are driving strong financial performance.

The Group continues to deliver on its commitments to our wider stakeholders.

Our purpose, Bringing Water to Life, supporting the lives of people and the places they love for generations to come, is at the heart of what we do and why we do it. We continue to focus on being a sustainable business that can deliver for colleagues, customers, our shareholders and the UK as a whole, with sustainable financing and accreditation with the Fair Tax Mark. Our supportive shareholders include UK pension funds, savings funds, charities, employees and uniquely for Pennon, our customers. Across the UK, the number of private individuals with shareholdings has been declining for some years. Last year it was reported that c15% of the UK stock market was held by individual shareholders. In the 1960s, that number was c.50%.

We believe there is a place for both, as do our customers. As a direct result of our innovative WaterShare+ scheme, giving customers a stake and a say in their water company, we now have four times as many customer shareholders as we do institutional shareholders. With our second issuance, 1 in 14 households in the South West Water region opted to take shares as opposed to money off their bill, and we were able to include Bristol Water customers for the first time. With this ownership model, it means that we spend more time directly engaging with our customers, at quarterly public meetings and at our customer AGM, so we can hear directly what matters most. And, in this cost-of-living crisis, we believe every customer should benefit from what we do. We have therefore ensured annual bill levels increases have remained well below inflation levels and the c.7% average annual increases seen across the sector, as we double the number of customers on support tariffs, and in eradicating water poverty.

We also believe in investing for the future for the good of the sector. Our 25-year partnership with the University of Exeter, CREWW – the Centre for Resilience in Environment, Water and Wastewater, is working to resolve some of the most pressing global challenges in the sector, not just in the UK but globally. Bringing together some of the best minds in Geography, Biosciences, Engineering, Economics and Psychology, we are looking to find answers ranging from how we can ensure there is enough water to cope with population growth and climate change, to how we prevent pollution and eliminate micro-plastics in our water supply. Our hope is that CREWW will become a beacon of change for the sector, in the UK and globally, whilst at the same time driving benefit and investment back into the South West as projects incubators for idea generation and commercial opportunities.

Looking ahead

In summary, our full year results reflect resilient performance, in a challenging year and in which we have pivoted to focus on what matters most today, and in building our capabilities for the future.

As we look forward to our next price review, which we submit in October 2023, the Board is very focused on ensuring we can continue to develop innovative and sustainable solutions for the issues the sector faces and in delivering more for our customers, communities and the environment. We are currently undertaking our most comprehensive customer engagement programme ever, as this is the key to unlocking both ambitious and credible plans, supported by our WaterShare+ Advisory Panel.

We want to ensure we continue to deliver world class drinking water, boosting water resources and resilience across the greater South West for the longer term. We also plan to reflect the unique needs of our region, and in particular our 860 miles of coastline, building on our expertise in biodiversity, catchment management and Net Zero capabilities. And, with a focus on ensuring our plans are affordable, we will explore a suite of charging options and tariffs, reflecting our customer demographics, as well as continuing to evolve our affordability toolkit, protecting the most vulnerable and eradicating water poverty.

As One Pennon, with a strong balance sheet, financial and operational resilience, we are well placed to deliver a sustainable future for all.

Susan Davy
Chief Executive Officer

31 May 2023

Susan addressing the annual Pennon Homesafe Conference in Bristol

Our business model

Our business model is shaped by our purpose - Bringing Water to Life, supporting the lives of people and the places they love for generations to come. This means we are not only seeking to create value for our stakeholders today but reinvesting in our business in a carefully planned and sustainable way for the future.

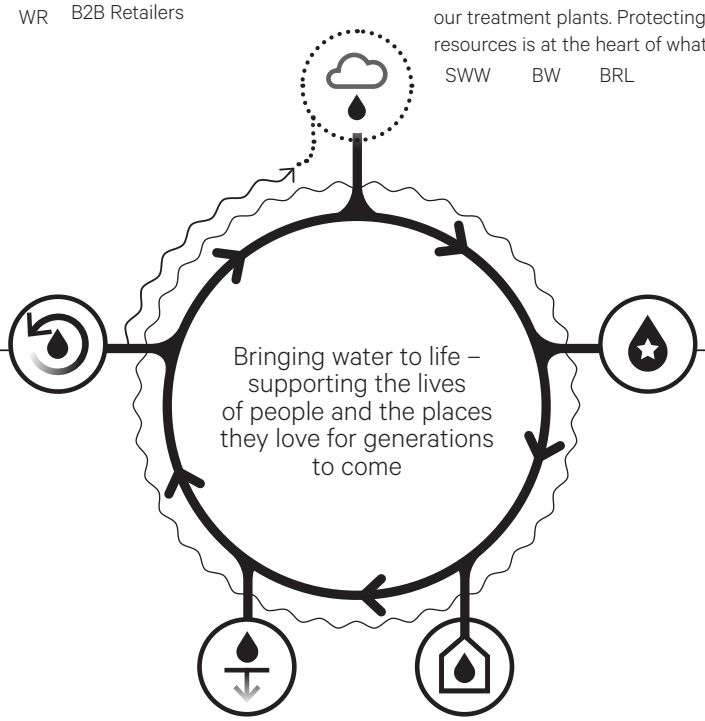
Delivering services through all stages of the natural water cycle

SWW South West Water
BW Bournemouth Water
BRL Bristol Water
WR B2B Retailers

Water resources

Ensuring an available and sufficient supply of raw water is critical to ensuring a continuous supply to customers. Our operations play a vital part in maintaining the level of river flows and their ecological health – from the level of water we release from our reservoirs into rivers, to the level we abstract and take to our treatment plants. Protecting the region's precious natural resources is at the heart of what we do.

SWW BW BRL



Wastewater treatment and recycling

We treat wastewater to a high standard at our 653 wastewater treatment works before returning treated wastewater to the environment, safely. Bioresources created during the treatment process are a valuable source of both nutrients and energy and contributes to a circular economy.

SWW

Water treatment and distribution

We take water from our reservoirs, river and groundwater sources and transport it to our treatment works, where it is treated to a high standard using a number of processes. Once the water is clean, safe and reliable we transport this to customers' homes and businesses through our c.25,000km of water pipes.

SWW BW BRL

Wastewater collection

We maintain and operate c.23,000km of sewers in the South West region, removing waste from the homes and properties of our customers. Through our programme of proactive interventions, informed by extensive data and AI, we keep our network in the best possible condition, identifying and repairing issues alongside an extensive sewer cleaning programme

SWW

Services to homes, businesses and our wider communities

We manage an extensive network to deliver uninterrupted supplies to our customers whilst keeping customers' bills affordable. Our household and business retail contact centres are focused on providing excellent end-to-end customer experiences. From providing water and sanitation, through to environmental protection, recreational facilities, education, local jobs and investment for future generations. The services we provide are essential for the health and economic wellbeing of our local communities.

SWW BW BRL WR

Role of the Group

The Group provides strong pillars of strategic direction, financial management, risk management and governance. Combined with the Group's robust fundamentals this creates resilience in a challenging economic environment and drives long-term sustainable growth.

Our key strengths and resources

Environmental – Natural Capital

High-quality assets

- Investing in world-class facilities and plants, using innovation and technology to help safeguard our natural resources.

Environmental stewardship

- Constantly seeking more sustainable ways of working to protect, enhance and reduce our impact on the natural environment.

Social – Social and Human Capital

Strong reputation and customer service record

- High levels of employee engagement and accreditation as best place to work.

A stake and a say

- Our unique WaterShare+ framework offers customers a greater stake and a say through Pennon share ownership or bill reductions, alongside a dedicated customer AGM.

Governance – Manufactured, Intellectual and Financial Capital

Effective governance

- A strong governance framework, supporting robust decision-making and performance management.
- Comprehensive risk management processes.
- Fair tax mark accreditation.

Efficient financing

- Sustainable financing framework.
- Low effective interest costs.

Strong acquisition expertise

- Track record of success in acquisition integration.

Strong relationships with our suppliers

- Always ensuring their performance meets our expectations, upholds our standards, aligns with our policies, protects human rights and promotes good working conditions.

Benefits and value we create for:

Environment

2030

Net Zero commitment

220,000

trees planted to date, on track to plant 250,000 by 2025

Customers

100%

with an affordable bill by 2025

Communities

>4,000

pupils helped by our educational programmes

Talented people

c.3,000

Largest private sector employer in the region

Investors

>50%

forecast growth to 2025 in our water businesses' regulatory capital value (RCV)

Suppliers

c.2,900

suppliers in our Group supply chain

Regulators

Regular and proactive contact and engagement with Regulators

Find out more about how we engage with our stakeholders on page 27.

Underpinned by our purpose, twin-track growth strategy, continuous innovation and environmental commitments

Our strategic framework

We are continuing to drive progress on our three strategic priorities through our strategic framework.

Our three-pillar strategy

1 Growth in Environmental Infrastructure

Through the successful delivery of our twin-track strategy – driving both organic and acquisitive growth underpinned by our disciplined capital allocation, we will continue to create long-term sustainable value. Our logical and accretive water acquisitions have delivered significant value for our stakeholders along with meaningful benefits for customers and shareholders.

Our value-enhancing investment in renewable energy generation and storage will provide attractive, sustainable returns into the long term, and fast-track the achievement of our Net Zero 2030 commitments.

We are well underway in delivering on our largest environmental investment programme which also reflects the delivery of additional and accelerated investments including Green Recovery, WaterFit, our Save Every Drop water resilience investment and Ofwat's recently announced Accelerated Infrastructure Delivery.

Progress against our strategy

>50%

RCV growth over K7, driven by our twin-track strategy

c.£1.5bn

our largest environmental investment programme, including additional and accelerated initiatives

£160m capital allocation

in renewable energy generation – 1st c.40 GWh site acquired

2 Pioneering Solutions

We continue to pursue a relentless approach to improving operational performance through innovative solutions that drive the best outcomes for all stakeholders. Our pilot, test and deploy approach to innovation helps us to mitigate risk for customers, communities and the environment.

Our new WaterFit Live tool, launched in early 2023, demonstrates our commitment to increased transparency, empowering customers and stakeholders to hold us to account on our performance and allow them to make informed decisions on water-based recreation. It features a new interactive map that provides customers and visitors to the region with more information on the performance and location of storm overflows at all designated bathing waters, as well as the investments South West Water is making now, and in the future, to reduce overflow spills across the region's coastline by 2025.

As a purpose-led business, we think differently about the relationship we have with our customers through our innovative and pioneering WaterShare+ scheme developed to give our customers a greater stake and a say in our business. We are delighted that since 2021 almost 90,000 customers have opted to become shareholders through WaterShare+.

Progress against our strategy

£40m

returned to customers in K7 through our unique customer sharing mechanism WaterShare+

Centre for Resilience in Environment Water and Wastewater – our joint venture with the University of Exeter

Developing innovative solutions to water resources including desalination and re-purposing quarries

3 Leadership in UK water

The Group has continued to deliver resilient services through extreme climate variability and high demand. Alongside this, we have delivered some of our best environmental performance to date, including our best ever wastewater treatment works compliance, a reduction in wastewater pollutions, and outstanding bathing water quality across the region.

Currently, over c.110,000 customers benefit from our broad range of affordability initiatives, and we continue to work hard to deliver quality services at an efficient cost, so that bills remain affordable. In 2022/23, customer bills in the South West Water region were lower than they were 10 years ago, and £10 lower than in 2021/22 and, recognising the cost-of-living pressures customers are facing, bills across the Group for 2023/24 will see below-inflationary increases.

Driving outperformance across the Group gives us the ability to deliver more within a regulatory delivery period. As a Group, we are strategically positioned to outperform in the current macro-economic environment. Our flexible financing strategy and diverse debt portfolio, with a relatively lower level of index-linked debt compared to the industry average allows us to outperform, and is reflected in our strong return on regulated equity, with outperformance enabling reinvestment in additional initiatives.

Progress against our strategy

100%

bathing water quality across the region for the second consecutive year

c.10.5% in 2022/23

Continued doubling of base returns on regulated equity across the Group

c.£85m

of customer support delivered to date

Informed by our engagement with our wider stakeholder group and what they want

Customers	Communities	People	Suppliers	Policy makers	Investors	Regulators
Safe drinking water, clean rivers and seas, continuous supply and an affordable price	Protect the environment and a say in our business	A values-led employer, fair wages and personal advancement	Fair contracts, access to data and opportunities for growth	Investment and support in reaching 2050 targets	Achievement of business plan targets, long-term sustainable growth and a fair return	Innovation in support of the delivery of continually improving targets

Reflected in our approach to sustainability and ESG commitments

65%	c.£700k	31%	100%	£1.5bn	>50%	c.70%
reduction in Scope 2 market-based GHG emissions in 2022/23	investment into our communities	women in leadership roles	of our supply chain engaged with our code of conduct	2020-25 environmental investment programme - our largest to date	202-25 growth in regulated capital value	of ODIs in 2022/23 on track or ahead of target in SWW, with c.65% at Bristol Water

Strategy in action...

Investing in renewables – energy generation

We have set aside £160m to invest in renewable energy and have identified a pipeline of solar opportunities.

In May 2023 we acquired a c.40 GWh site in Dunfermline which is ready to build with consents in place, and is expected to commence generation in 2024. The site also has the capacity for a two-hour 60 MW battery that will support the UK Grid's move to renewables and provide a healthy return.

Read more on the progress we are making to become Net Zero on pages 42 to 43.

WaterFit Live

In March 2023, we launched WaterFit Live, an interactive digital system which shares with customers the status of their local bathing waters and whether there is any impact from a storm overflow.

WaterFit Live is another milestone in our progress to protect the environment by reducing storm overflows, enhanced monitoring, providing clear and transparent reporting for our customers and increasing our investment to improve performance.

Read more on our WaterFit programme progress on page 25.

Driving synergies - Bristol Water acquisition

We are making strong progress with our integration blueprint. Bringing together the two water businesses to improve customer service, strengthen our teams and share and implement learnings.

The licence change and statutory transfer completed on 1 February 2023, bringing Bristol Water under the South West Water licence. Our proven integration blueprint consists of three phases.
The first, focused on integrating our back office teams, is largely complete, and we are well underway in developing a combined plan for PR24 to deliver the best outcomes for all stakeholders. Phases two and three will focus on Operations and Customer Services.

Read more on the integration of our teams in our People section on pages 31 to 39.

Ensuring future water resilience

As part of our continued investment in water resilience, we purchased Hawks Tor Reservoir on Bodmin Moor in Cornwall in March 2022. To tackle the drought we have deployed a twin track approach of demand and supply side investments augmenting storage scheme, expanding the treated water network and repurposing disused quarries. The interventions deliver an increase in supply when it is needed most that equates to 25% of Cornwall's demand and 12% of Devon's demand. To target water efficiency we are deploying initiatives such as 'Stop the Drop' and 'Save every Drop' alongside our broader water efficiency campaigns aimed at helping customer reduce demand.

Read more on how we are tackling climate challenges and water resilience on page 41.

Ambitions to 2050

Our Strategic Direction to 2050 sets out our ambition for the water system of the great South West, the leadership and action we will take, the action needed from others, and the opportunities we must collectively grasp if we are to ensure high-quality, reliable and resilient water services for future generations. Our ambition is to protect and enhance the environment at every stage of our operations and provide a resilient service in the future. Achieving that ambition will also require fundamental changes to the ways that we, our customers and stakeholders all use and interact with our services and the aquatic environment. The ways in which we are meeting these challenges together are described in more detail at https://www.southwestwater.co.uk/about-us/documents/business-plan-2020-2025/.

Water resources

Resilient water resources through healthy catchments

What we will do

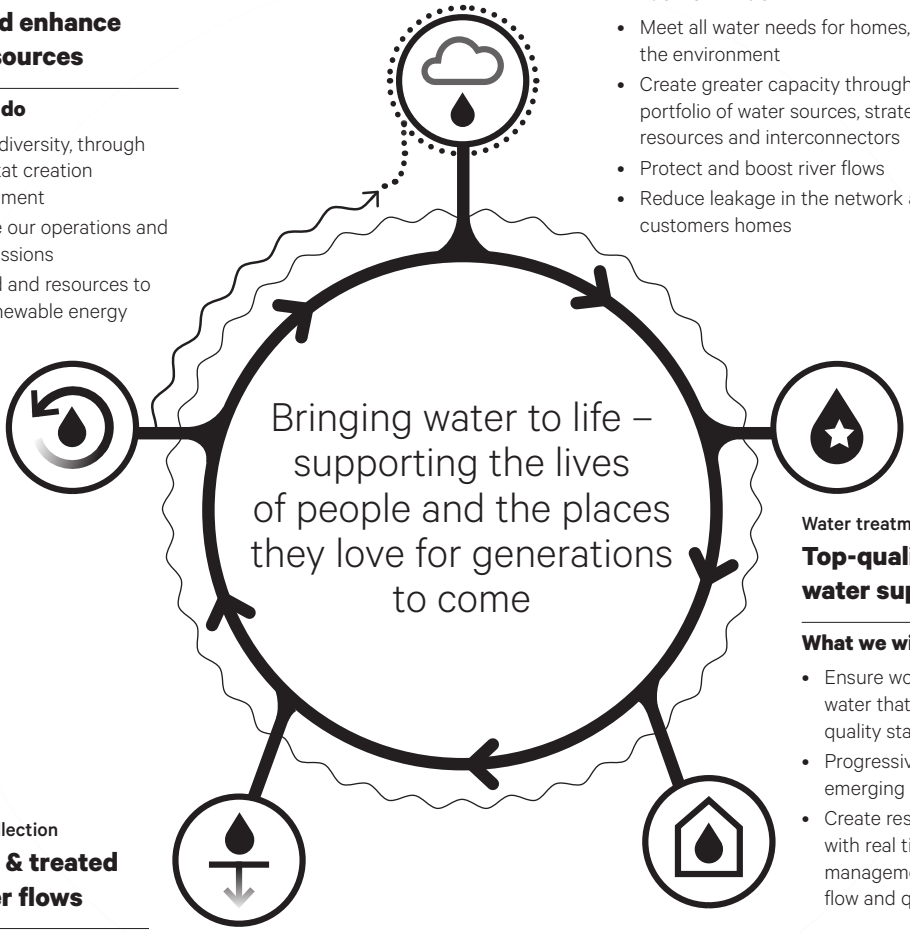
- Meet all water needs for homes, businesses and the environment
- Create greater capacity through a diverse portfolio of water sources, strategic regional resources and interconnectors
- Protect and boost river flows
- Reduce leakage in the network and at customers homes

Services to nature and the environment

Protect and enhance natural resources

What we will do

- Increase biodiversity, through further habitat creation and improvement
- Decarbonise our operations and net zero emissions
- Use our land and resources to generate renewable energy



Water treatment and distribution

Top-quality water supplies

What we will do

- Ensure world-class drinking water that meets stringent water quality standards
- Progressively address emerging risks
- Create resilient, smart networks with real time tracking and management of water pressure, flow and quality

Wastewater collection

Controlled & treated wastewater flows

What we will do

- Evolve our water recycling and sewerage system to meet the needs of our communities and the environment
- Enhance sustainable drainage to reduce risk of flooding and pollution
- Return treated water safely to the environment

Services to homes, businesses and our wider communities

Trusted customer & community experience

What we will do

- Boost active participation of customers and communities in the sector
- Make it easy for customers to reduce their water consumption and manage their water bills
- Promote progressive charging so that every customer has a fair and affordable water bill

Clear near-term environmental targets and milestones contributing to our long-term ambitions to 2050

Underpinned by our ongoing, long-term investment programme

2023

Committed to further enhancing our disclosures consistent with the Task Force on Climate-related Financial Disclosures

Committed to setting both near and long-term Science Based Targets (SBT) in accordance with the Science Based Targets Initiative's Corporate Net Zero Standard

Reinvesting £170m of our current RORE outperformance

Read more:

TCFD disclosures targets page 74

SBT commentary page 43

2025

2025 targets for selected ODIs and operational activities, including commitment to eliminate water poverty by 2025

2025 targets for ESG priority measures

100% bathing water quality standards met all year round

Our WaterFit plan targets significant investment to 2025 to further protect river and coastal water quality

Read more:

ESG priorities targets page 66

ODI targets page 25

WaterFit plan

Our biodiversity strategy page 41

2030

125,000 hectares of habitat and land management improved

Single-digit spills, if any at all coastal locations

2030 Net Zero target for our operational carbon emissions

2030 Net Zero plans published by our regulated water business

TCFD metrics and targets including commitment to self-generate up to 50% of renewable energy by 2030

Read more:

Net Zero strategy pages 42 to 43

TCFD disclosures page 74

WaterFit plan

2045

2045 Race to Zero commitment to reduce greenhouse gas emissions (GHG) across our entire value chain

Read more:

Net Zero strategy and Race to Zero commentary pages to 43

2050

50% leakage reduction and 1/4 consumption reduction

Zero ecological harm from wastewater spills and discharges

375,000 hectares of habitat and land management improved

2050 ambitions working in harmony with the water cycle with near-term targets 2020-2025, medium-term targets 2025-2035 and long-term targets 2035-2050

Read more:

Our 2050 ambitions targets page 12

Market overview

Pennon is one of three FTSE-listed companies supplying water and wastewater services across England and Wales. Pennon's group of companies provides water and wastewater services to a population of c3.5 million across the South West of England. Pennon provides their services in the context of key trends and challenges faced in the local market and by the wider water industry. In 2023, Pennon has noted the following key trends and challenges in the market.

Key – Strategic priorities

1. Growth in Environmental Infrastructure
2. Pioneering Solutions
3. Leadership in UK Water

Accelerating climate change

Link to strategy

1, 2, 3

Impact

We are already experiencing the impact of climate change. These impacts are set to increase, with temperatures anticipated to be at least 1.5-2°C above pre-industrial levels by the end of this century. This is not just a longer-term problem, but a very real issue for us today as the 2022/23 drought in our region has shown.

The South West of England is particularly vulnerable to climate change, given its 860 miles of coastline, and adjacency to the western approaches of the Atlantic Ocean – this exposes the area to impacts from rising sea levels and storm intensity and we are already starting to observe significant and unpredictable impacts on our operations.

How we are responding to 2050

We will need to optimise investment in asset health and resilience, through integrated long-term planning that will deliver the right level of investment to ensure that our assets and networks are able to cope with more extreme weather and demand. We will need to work collaboratively in the building of new developments in our region, optimising local water cycles through investing in re-use and recycling of water, as well as natural assets.

We also need to think about how our infrastructure is impacted by the services we rely on – such as electricity to power our pumps and treatment processes. We have developed a systems thinking approach to consider the resilience of our operations in the context of this wider system.

Rapidly evolving customer expectations

Link to strategy

2, 3

Impact

Putting the customer first has long been a focus of the water sector, as we look to provide excellent service and address issues first time. Customer expectations are rapidly evolving in the following areas:

- **Our operations** – Customers expect a continuous, seamless service with us also being a force for good in our communities.
- **Transparency and ethicalness** – we need to be increasingly transparent about operations, performance, and services.
- **Personalised services** – Customers are more empowered than ever by digital technology, and expect personalised products and services to meet their needs.
- **Smart technology** – Smartphones and social media are transforming how and how often we engage with customers.
- **Environment** – Customers are increasingly environmentally aware and expect us to be custodians of our local environment.

How we are responding to 2050

We will boost active participation of customers and communities in the sector and ensure every customer can afford to pay their water bill.

We will make it easy for customers to reduce their water consumption and manage their water bills.

We will decarbonise our operations and increase biodiversity, using nature-based solutions as a default.

Growing population and changing demographic

Link to strategy

1, 2, 3

Impact

The global and local population and demographic is changing. Official forecasts suggest an additional 530,000 people will be living and working in our region by 2050, adding to the c.3.5 million who currently live in the regions we serve. As a coastal region, our resident population swells during the year as 10 million visitors come to enjoy the South West. During the Covid-19 pandemic, we saw nearly half of the anticipated 2050 growth in population due across the region, concentrated in the tourism areas of Devon and Cornwall due to the increase in home working and an increase in staycations.

How we are responding to 2050

A growing population puts pressures on existing water sources, as more people need access to clean, safe water. Our twin approach is to reduce the demand and leakage of water, whilst also building new sources of water supply. Building on the three disused quarries that have been repurposed into reservoirs for drinking water, we will build new sources from desalination plants through to new reservoirs. We will halve leakage by 2050 and help customers to use less water – as we look to drive consumption down by one quarter through water saving initiatives. The roll out of smart meters will help reduce consumption and address customer side leakage – up to one third of all leakage.

A growing population adds to the loads that our sewers and wastewater recycling centres need to process, and we will invest to meet those demands. As areas become more urbanised due to growth, green spaces do naturally shrink. We have ambitious plans to reverse this trend, and build more green spaces which will allow surface waters to drain away naturally rather than run into our sewerage systems. And by moving small isolated communities from septic tanks and soakaways to full treatment works, we can protect rivers in the local environment.

Desire for environmental improvements

Link to strategy

2, 3

Impact

A healthy environment is important for our region, and in the face of climate change, ecological decline and greater recreational use of rivers and seas, customers and stakeholders rightly tell us that they expect environmental leadership from us as a priority.

Our research tells us that customers have a more positive attitude to companies that support social and environmental issues.

Our customers recognise the value of investment to deliver services which also provide social and environmental benefit.

How we are responding to 2050

Our strategic direction recognises the importance of re-connecting the water cycle, and water cycles operate within catchment.

Catchments are the natural way to consider the marine environment. Better coordinated action at the catchment level by those who use water or nearby land is a great enabler for change.

Engagement and collaboration are at the heart of catchment-based approaches. Catchment work requires joint delivery by all stakeholders within a catchment, supported by regulators and policymakers. This would ensure we address all pressures placed on the water environment including from water company activities, but also diffuse pollution from both agricultural and urban sources.

Changing supply chain

Link to strategy

1, 2, 3

Impact

We serve c.3.5 million people a day, through our 3,000 talented employees and nearly the same number of supply chain partners across the South West. Working together, we have reduced cost and improved service to our customers, keeping increases to customer bills below inflation whilst delivering record levels of investment.

But across the country and in the South West – supply chains are under pressure as they face the twin challenge of:

- Ramping up to deliver boosted investment to deliver improved interconnectivity, transport links, environmental improvements and Net Zero.
- Increasing costs of materials and commodities, higher rates of inflation and the recessionary environment.

How we are responding to 2050

We are focused on working with supply chains to build resilience and work together for success:

- Improving end to end visibility of our future investment plans.

Working collaboratively to build talent, especially specialist skills:

- Adopting innovations, machine learning and AI.
- Building future readiness for potential shocks and uncertainties.

Technology advances

Link to strategy

2, 3

Impact

Big Data, digital technologies and open data are being leveraged to increase reliability, optimise assets, improve supply chains, and boost customer relationships.

Some key technology trends which impact us are:

- The availability and accuracy of sensors that collect and transmit data is improving.
- The ability to collect, store and analyse data has expanded.
- Big Data, digital twins and computing algorithms are being developed which translate unstructured data sets into actionable intelligence.

These trends will only increase as there is more integration of the Internet of Things, faster access to the Internet, and advances in the computational power of computers and mainstream devices.

For customers this means that we can predict operational problems and fix them before they have an impact, it allows us to be transparent, to be agile, and therefore, build trust and legitimacy.

How we are responding to 2050

We will drive technology, leveraging data and the supply chain. We will need to collect and analyse more data to understand better and manage our systems in real time. We will make more data publicly available as a way of stimulating new ideas and partnerships so we can provide better services for customers and better protection of the environment.

We will continue to work with our colleagues across the sector in shared research and learning through organisations such as UKWIR (UK Water Industry Research).

At the very heart of our approach is intelligent asset management – we will invest further in our telemetry, operational control systems, meters and network sensors to provide greater automation, real time system feedback and inform decision-making. We will also replace our asset and work management systems and data analytics capabilities to provide actionable insight, both for us and our customers.

The Upstream Thinking Argal Reservoir project delivered in partnership with the Cornwall Wildlife Trust

Evolving government infrastructure policy

Link to strategy

1, 2, 3

Impact

In just over 30 years, over £200bn of private sector investment has enhanced water sector infrastructure across the UK, benefiting consumers now and for generations to come. But there is more to do as infrastructure continues to form the backbone of a successful modern economy. The government has set out ambitious goals for the economy and environment, putting infrastructure at the heart of its plans. These goals include:

- Environment – a 25-year plan to improve the environment by removing harmful abstractions, improving discharges and reducing water lost through leaks and used by customers.
- Net Zero – ambitious targets have been set, backed by green jobs that can support clean growth.
- Levelling Up – Investing to unlock growth,create opportunities, and jobs, boosting education and living standards, in areas where these are set apart from the rest of the nation.
- Sustainable housing – 250,000 homes need to be built each year across the UK to avoid spiralling prices and maintain affordable homes. These homes need to be sustainable – reducing water and energy use, boosting biodiversity, and minimising waste.

How we are responding to 2050

Our future plans include large-scale infrastructure projects to deliver environmental improvements, including two new reservoirs for the region. We are being clear on the scale of investment that is needed as part of supporting steps to streamline infrastructure decision-making whilst maintaining transparency and objectivity.

Alongside, we are enhancing wastewater treatment as part of government plans to unlock growth in those areas where environmental issues are slowing down development.

Evolving employment market

Link to strategy

1, 3

Impact

Employment market flexibility and diversity has been steadily increasing, with more people than ever working in self-employment, part-time jobs, and under zero-hour contracts.

An important consequence of these changes is ensuring the skills and talent for the future. As sustainability and the environment becomes more important, and as technological advancement and artificial intelligence are increasingly common in the workplace, new and niche skills become more important. STEM based occupations, such as digital literacy and ICT skills, are emerging areas of focus.

Good employers will take ownership for future proofing skills and talent to reflect the new ways of working.

How we are responding to 2050

We plan to harness energy and creativity by creating great spaces to work and promote diversity to bring together a mix of minds and representation of the communities we serve. We recognise the need to deliver on total wellbeing by being at the forefront of mental health as well as a leader in health and safety performance and offering the most flexible family friendly benefits. We will continue to work with schools, colleges, and universities in our region to create Pennon-sponsored skills academies to lead on the skills agenda in the region and across the wider supply chain in building emerging talent pipelines.

Upstream Thinking
Ockerton Peatland Restoration Project

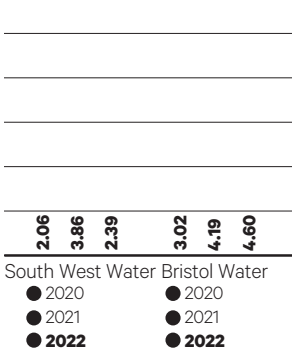
Key Performance Indicators

We measure our performance against our strategy through a range of non-financial and financial metrics. Operating in the UK water sector means we have a number of performance commitments, Outcome Delivery Incentives (ODIs) to meet the requirements of our regulators.

Non-financial metrics

Clean, safe and reliable water

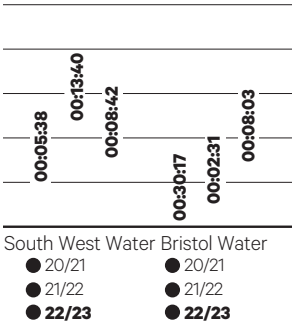
Water quality (CRI score)



Compliance Risk Index (CRI) is the Drinking Water Inspectorate's measure of water quality.

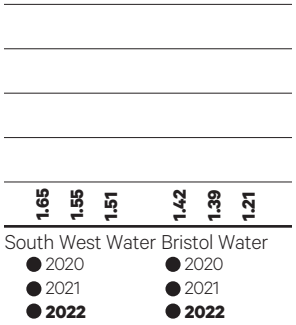
In 2022/23 we have continued with our 'Quality First' transformation programme and performance in South West Water has improved. In Bristol Water, our score has been impacted by the drier summer where demand increased over the summer increasing the output and pressure on our network. Across the Group we continue to invest in advanced treatment including ceramic membranes, granular activated carbon and other innovations to drive improvements.

Supply interruptions (Duration per property per year)



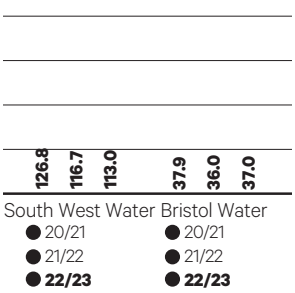
The performance across the Group was impacted by ground movement over the summer months as well as the extreme periods of cold weather and rapid thaw over the winter months. As a result, the number of bursts increased, with a number of larger more complex events to respond to, which increased the duration of interruptions.

Taste, smell and colour (contact per 1,000 population)



We recognise that customers expect their drinking water to look and taste great and this is important in maintaining customers' trust in the quality of our supplies. Across the Group improvements in our treatment processes and managing our network continue to improve performance for customers.

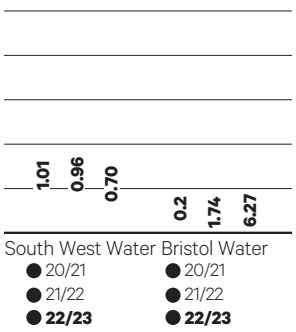
Leakage (3-yr average – Megalitres per day)



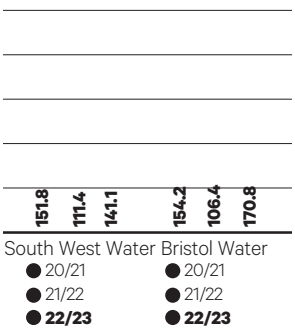
Reducing leaks is a critical component of ensuring a sustainable water supply.

In 2022/23, we enhanced our leakage reduction activities over the summer months to support high demand meeting our regulatory targets despite the colder winter. In Bristol Water, leakage increased in the year driven by an increase in bursts this year.

Unplanned outages (%)



Mains repairs (Number of repairs per 1,000km)



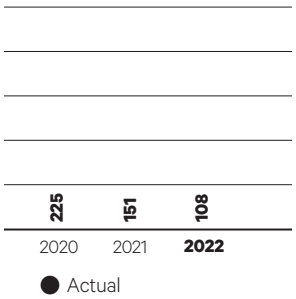
Asset Health is essential for ensuring a robust supply of water to our customers.

2022/23 performance was again impacted by the colder winter weather with mains bursts increasing across the Group. In South West Water our unplanned outages continued to outperform our targets for the year, however an unplanned and complex event at our largest treatment works in Bristol Water increased this measure during 2022/23.

Read more on pages 22 to 26 for further detail on our operational performance.

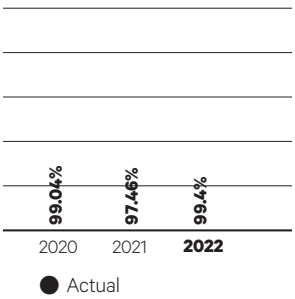
Protecting the environment – robust wastewater delivery

Pollution incidents (number of wastewater incidents)



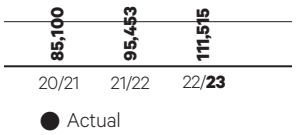
Our targeted Pollutions Incident Reduction Plan is delivering results with a 50% reduction over the last two years – but we know there is more to do and we continue to target a further step change in performance.

Numeric Compliance (%)



We measure the compliance of our discharges against our permits. 2022 has seen our best ever score which is expected to be upper quartile across the industry.

Biodiversity (Hectares)

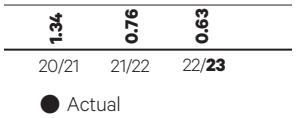


We are continuing our pioneering catchment management approach with over 111,000 hectares of land restored, including 300 hectares of peatland restoration ahead of our target.

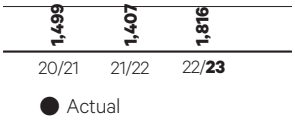
Environmental Performance Assessment

A combination of a basket of measures, the EPA is the Environment Agency's assessment of environmental performance. We have seen improvements across all these measures resulting in a provisional 2 star rating this year; with a planned strategy of achieving 4 star by 2024, there is much to focus on.

Internal sewer flooding (Incidents per 10,000 sewer connections)

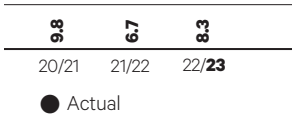


External sewer flooding (Number of incidents)

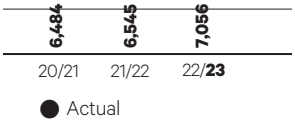


Sewer flooding is a key area that significantly impacts on customers. 2022/23 has continued our positive performance with a further reduction in internal incidents – continuing our best ever performance. External flooding incidents have however increased with the drier weather over the summer increasing the number of blockages and flooding during the wetter winter months.

Sewer collapses (Incidents per 1,000km)



Sewer blockages (Number)

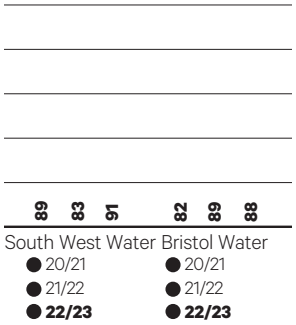


These measures reflect service impacts to our customers as well as being a lead indicator of asset health. We have seen an increase in these measures with the exceptionally dry weather over the summer months increasing blockages – although both measures have met target.

Read more on pages 22 to 26 for further detail on our operational performance.

Delivering for our customers

Overall satisfaction with PSR (%)



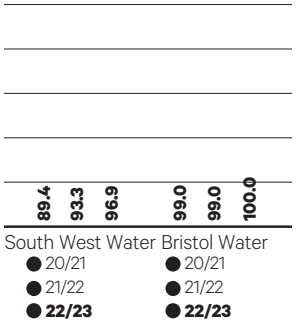
We have over c.112,000 customers on the Priority Services Register (PSR) across the Group and we measure customer satisfaction with these services each year. South West Water at 91% and Bristol Water at 88% are both ahead of our target.

Customer Measure of Experience (C-MeX)

C-MeX is Ofwat's measure for customer experience both for those customers who contact us as well as the perceptions of all our customers. Across the Group, our C-MeX rankings have remained consistent year-on-year.

12th **6th**

Customer affordability (%)



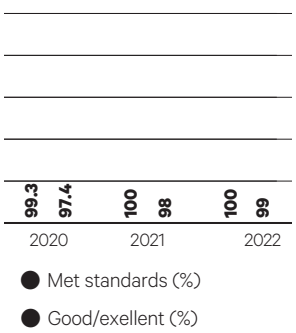
We are targeting zero water poverty by 2025 and our range of affordability schemes are helping around 110,000 customers. South West Water and Bristol Water have a measure which assesses customer affordability which is improving year-on-year.

Developer Measure of Experience (D-MeX)

D-MeX is Ofwat's measure of service experience for developers which directly compares us with our peers.

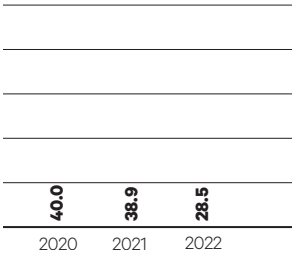
11th **4th**

Bathing waters



South West Water has over 860 miles of coastline to protect, representing over one third of the UK's bathing waters. In 2022, 100% of our bathing beaches met the high standards set for water quality for the second year in a row.

Average Spills

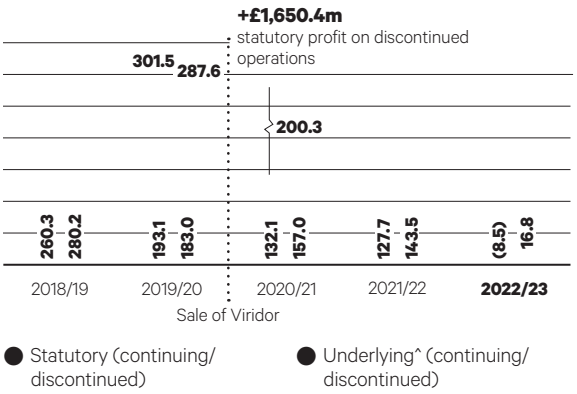


Our new investment programme, 'WaterFit' is focused on protecting rivers and seas. During 2022 the average number of spills reduced by c.27% and we continue to deliver our plans to reduce to an average of 20 spills by 2025.

Financial Metrics

Annual[1]

Operational



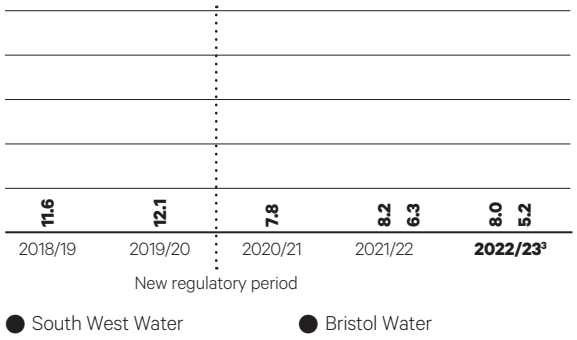
Profit before tax (£m) ①②③

Why is this KPI important to us?

Profit before tax is a key measure of the Group's financial performance after deducting all operating and finance costs. Underlying Profit before tax is measured to exclude any distorting non-underlying items as explained in our Alternative Performance Measures on pages 220 to 223.

Our performance in 2023
Commentary on performance is set out in the Group Chief Financial Officer's report on pages 44 to 51.

Link to remuneration, bonus/LTIP
Annual bonus performance measure.



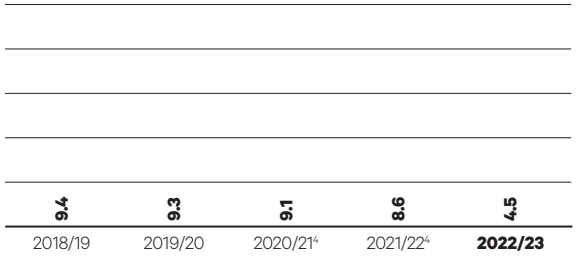
Return on regulated equity (RORE)^[2] (%) ①②③
(WaterShare)

Why is this KPI important to us?

Return on regulated equity (RORE) expresses the return the water businesses have managed to earn above and beyond expectations set by the regulator through financial and operational performance as explained in our Alternative Performance Measures on pages 220 to 223.

Our performance in 2023
This reflects a doubling of base returns. Commentary on performance is set out in the operational performance review on pages 22 to 26.

Link to remuneration, bonus/LTIP
LTIP performance measure.



Return on capital employed (ROCE) (%) ①②③

Why is this KPI important to us?

ROCE provides a measure of the return being generated by the Group compared to the total equity and debt capital deployed to generate that return.

Our performance in 2023
Commentary on performance is set out in the Group Chief Financial Officer's report on pages 44 to 51.

Link to remuneration, bonus/LTIP
LTIP performance measure.

Alignment with strategy

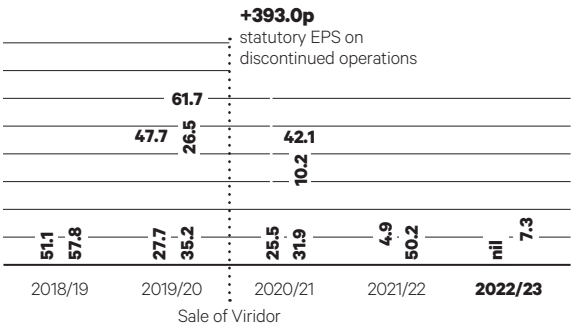
Our KPIs are aligned to our three long-term strategic priorities.

① Growth in Environmental Infrastructure
② Pioneering Solutions
③ Leadership in UK Water

^ Measures with this symbol are defined in the Alternative Performance Measures (APMs) as outlined on pages 220 to 223

1. For further information on the relevance to Executive Directors' remuneration see page 134
2. Calculated using WaterShare methodology using K7 CPIH forecasts.
3. Cumulative K7 measure.
4. South West Water ROCE measure used for 2020/21 and 2021/22. This provides a comparative figure to previous Group performance. See calculations provided in the alternative performance measures section on pages 220 to 223.

Long-term



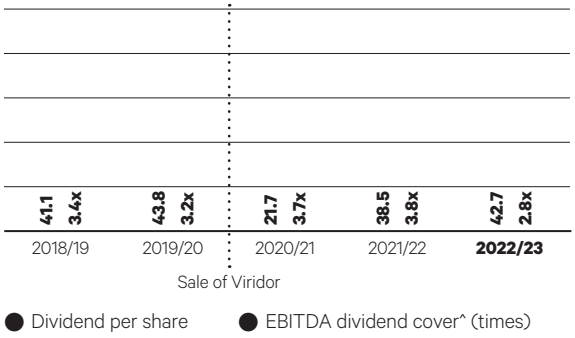
Earnings per share (pence) ①②③

Why is this KPI important to us?

Earnings per share (EPS) is a key financial metric indicating the Group's profitability after tax and provides a relative measure of profitability in comparison to the Group's share price. Underlying^ EPS excludes the impact of potentially distorting non-underlying items as explained in our Alternative Performance Measures on pages 220 to 223.

Our performance in 2023
Commentary on performance is set out in the Group Chief Financial Officer's report on pages 44 to 51.

Link to remuneration, bonus/LTIP
LTIP performance measure.



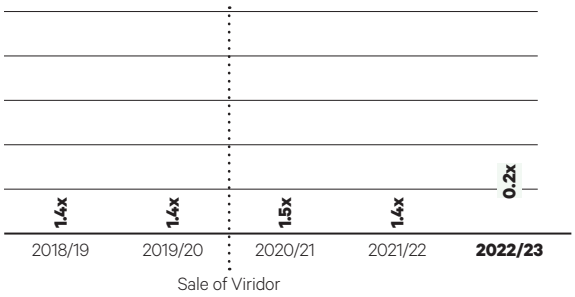
Dividend per share (pence) ①②③

Why is this KPI important to us?

Our sector-leading dividend policy is a key measure of the success of our sustainable growth strategy.

Our performance in 2023
Commentary on performance is set out in the Group Chief Financial Officer's report on pages 44 to 51.

Link to remuneration, bonus/LTIP
LTIP sustainable dividend measure.



Group dividend cover (times) ①②③

Why is this KPI important to us

Group dividend cover, ensures that the profitability of the Group supports the sustainable delivery of our dividend policy.

Our performance in 2023
Commentary on performance is set out in the Group Chief Financial Officer's report on pages 44 to 51.

Link to remuneration, bonus/LTIP
LTIP sustainable dividend measure.

Operational review

Performance as measured by our outcome delivery incentives (ODIs) was c.70% for South West Water, and c.65% for Bristol Water.

2022/23 has been dominated by the weather, with some of the hottest, driest, weather on record seen over the summer months, followed by rapid periods of extreme low temperatures over the winter months. The impact of the extreme weather varied across our regions – with a focus on water resources in Cornwall, whilst temperatures were coldest in the east of our region.

Our plans to improve our environmental performance continue at pace and our dedicated plans saw pollutions reducing by 50% over the first two years and our treatment works compliance improving to our best ever score.

Both regions have delivered cumulative RORE outperformance with South West Water's cumulative RORE of 8.0% representing a more than doubling of base returns, and Bristol Water's cumulative RORE achieving 5.2% also higher than base returns

Regulated Water

Clean, safe, reliable drinking water

Across the Group, we are committed to ensuring the continuous supply of clean, safe, and reliable drinking water, whilst preserving the natural resources within the South West. The hot, dry summer has impacted the outcome of some of our water measures, however our dedicated teams and ongoing investments ensure that we are able to respond to challenges now and into the future.

Water quality

CRI
The Compliance Risk Index (CRI) score as reported by the Drinking Water Inspectorate (DWI) measures water quality compliance.

In South West Water CRI was 2.39, and whilst above the industry target of 2, is an improvement from 3.86 last year and expected to be better than the industry average. Our 'Quality First' transformation programme is delivering results and the continued investment in advanced treatment technologies, including ceramic membranes and granular activated carbon, is designed to ensure compliance measures improve in future years.

CRI in Bristol Water at 4.60 is ahead of last year impacted by the drier summer where demand increased over the summer increasing the output from our works to near capacity levels and placing pressure on our network. Further enhanced maintenance and resilience improvements are being delivered across our water treatment works with specific sites targeted for improvement.

Taste, smell, and colour contacts
We recognise that consumers expect their drinking water to look and taste great and that this is important in maintaining consumers' trust in the quality of our supplies and we continue to invest in all aspects of our operations from source to tap to maintain that trust.

South West Water contacts per 1,000 population continue to decrease to 1.51 from 1.55 and achieved the performance commitment target, despite our maintenance flushing programmes being temporarily suspended in the region over the hot dry summer to reduce demand on our water supplies. Bristol Water performance at 1.21 shows a continuing improvement but is adverse to their target of 0.98 with increased contacts due to air in supply. We continue to progress well in delivering enhanced manganese removal schemes at Restormel and St. Cleer in Cornwall. To address taste and smell, we are progressing further significant investments in advanced granular activated carbon treatment at Stithians in Cornwall and Littlehempston in South Devon, and are installing temporary GAC treatment at Horedown in North Devon to provide great resilience over the coming summer.

The Postbridge Herbal Ley soil sampling & surveying trial funded through the Pennon Green Recovery catchment management programme in partnership with the Westcountry Rivers Trust

100%

monitoring of storm overflows in place

220,000

trees planted towards our 2025 target

79%

Reservoir storage at the end of March 2023

Pennon and Devon Wildlife Trust visiting a South West Water Green Recovery Upstream Thinking project in the Exe Catchment

Bournemouth Water treatment upgrades
As part of our business plan, we committed to building two state of the art water treatment works in the Bournemouth area. Good progress continues on both of these schemes. At Alderney work has continued on site clearance, building foundations, and enabling works as well as advanced procurement. Further design and piloting have been completed at Knapp Mill to reduce power demand and chemical consumption of the proposed scheme, as well as optimising the scope. Working with the local council we expect to secure Planning Permission by the end of June 2023.

Reducing leakage and supply interruptions

Leakage
We recognise that the prevention of water being lost in leakage from our pipes and assets is a key issue for all customers and is something we work continuously to reduce.

At South West Water, the specific investments made since the start of the regulatory period, teamed with the launch of our targeted action plan, are delivering results. Knowing this is a priority area, we have financed £100m on activities that reduce leakage over the last three years. In 2022, we targeted further leakage activities, focused on the Cornwall region to support supplies during the hot dry summer, which included offering free leak repairs to customers, increasing detection and repair resources in the region as well as using innovative techniques to identify leaks – including satellite scanning. The rapid periods of extreme cold inevitably increased leakage over the winter, however the focus on activity earlier in the year resulted in achieving our three-year average target, even with a year-on-year increase in leakage. Whilst we know there is still more to do to find, fix and prevent leaks on our network, we are encouraged by the progress made to date, and continue to focus on delivering further improvements to achieve a 15% reduction over the K7 period.

In Bristol Water, we also experienced a significant increase in the number of major bursts in December when a deep freeze and subsequent thaw put a strain on the water network. However, this leak outbreak was more prolonged in its effect with a marked increase in customer supply pipe leakage. As a result, the three-year rolling average target was missed.

Our Awesome Water display at the Cornwall Show, Summer 2022

Minimising customer supply interruptions
We understand the inconvenience that supply interruptions can cause. The importance of 'always on' supplies, maintaining both public health and customer confidence is one of our key priorities. Across the Group the hot dry summer followed by the extreme cold following by rapid thaw has resulted in performance below target of 5 minutes 45 seconds for both South West Water and Bristol at 8 minutes 42 seconds and 8 minutes 3 seconds respectively.

At South West Water, this weather caused an increase in the number of bursts and interruptions during December, and two large diameter, complex trunk mains failures accounted for c.14% of the total interruptions. This reflects the way in which performance against this target can be impacted by a one-off issue. We have set out an action plan to improve performance with our strategy of dedicated, in-house supply continuity and alternative water supply team making long-term improvements to customers and our innovative network training centre ensuring we are managing our network effectively following repairs.

Bristol Water was also impacted by the freeze/thaw as well as increased bursts over the summer months as the network was tested by extreme demand and ground movement. Two significant mains burst events accounted for c.42% of the total interruptions.

Investing to secure resilience, now and into the future

Per capita consumption (PCC)
This is an important metric to help the industry be more resilient into the future and help incentivise companies to conserve the natural resources around us. Per capita consumption is measured in percentage terms from a baseline.

In the year, South West Water has targeted demand reductions through our extensive water efficiency programmes – giving away over 130,000 free water saving devices, successfully reducing demand in Cornwall through our 'Stop the Drop' incentive and ongoing 'Save Every Drop' campaign. Overall consumption has reduced, driven by lower numbers of visitors to the region, although still significantly higher than historical levels but the remaining demand from households has increased due to the hot dry summer.

For Bristol Water, the impact of the hot dry summer continues to drive high levels of household demand driving per capita consumption higher than the target.

To help customers reduce their consumption, we provide free water saving devices as well as donations to charities supporting water conservation to help promote and educate customers. This is in addition to our schools outreach programme, which aims to teach children about the importance of looking after our natural resources.

Water availability
In 2022, some of the hottest, driest weather on record, coupled with elevated demand from customers and tourism in the region placed significant pressure on our water resources. As a result of this, for the first time in 25 years, South West Water placed water restrictions, through 'Temporary use bans' on customers in our Colliford water resource zone in Cornwall. All other areas, including Bristol Water had no water restrictions.

Despite the challenging conditions, positively no customers were without water, and we have established robust plans to recover reservoir storage and manage supplies during this year (as set out on page 41) including a new reservoir on Bodmin Moor, winter recharges for Roadford reservoir and a new treatment works and recommissioning abstractions at Newquay in Cornwall.

Bristol Water's water resources were robust to the hot dry summer with reservoir storage at c.100% at the end of March 2023.

Smarter healthier homes

As part of our Green Recovery plan, "Smarter, healthier homes" focuses on investments that directly benefit our customers and help improve supply resilience focused on installation of smart meters – enhancing customer engagement to help them manage their water use and bills more easily, carrying out a supply pipe 'adoption' trial, to relieve the worry of sudden unplanned financial demands arising from leaking and/or failed service pipes and embarking on a proactive lead pipe replacement programme.

As part of the acceleration investment ahead of the next regulatory period, we are expanding this programme into the Colliford area with an additional 40,000 smart meters and supply pipe replacements, with plans in the Bristol region to deliver around 2,000 lead and supply pipe replacements

Maintaining asset health

Mains repairs
The ground movement and pressure on the network during the hot dry summer, and the colder winter weather, particularly the 'freeze/thaw' experience in December has impacted the number of mains bursts this year.

In South West Water the work to optimise the operation and control of our network by pressure management and other 'network calming' activities, particularly in the Colliford area to support drought activities, meant that whilst the number of bursts significantly increased above historical levels in December 2022 and early 2023 our target for mains repairs was met at 141.1 repairs per 1,000 km of mains.

The weather impacts in Bristol Water, have been similar, and whilst we have continued to minimise high pressure risks where we can and monitor the network for 'transient' pressure spikes that can lead to mains failures the impact of the weather resulted in a significant increase in mains bursts, missing the target for the year.

Unplanned outages
Water treatment unplanned outage provides a means of assessing reliability of our water treatment works. It tracks the temporary loss of production capacity across all water treatment works, resulting from unplanned breakdowns and asset failure.

South West Water's performance in 2022/23 has remained strong, despite the significant challenges of high demand over the hot dry summer and compares favourably with the rest of the industry. Our 'summer preparedness' programme alongside our demand and supply management during the challenging summer resulted in unplanned outages reducing again this year with a figure of 0.70% compared to the industry wide target of 2.34%.

At Bristol Water, unplanned outage has increased in 2022/23 primarily because of outages at our largest water treatment works, Purton, due to pump failures when the treatment works was operating at near capacity to manage supplies during drought conditions. These asset failures account for 5.69% of the total 6.27% unplanned outage in 2022/23. However, despite the higher level of unplanned outage during an exceptionally dry year, customers were not impacted with any restrictions.

Mayflower Water Treatment Works in Plymouth

Regulated Wastewater

Protecting the environment – robust wastewater delivery

At South West Water, we continue to target and drive improvements in wastewater services through innovation by constantly seeking out new ideas, pioneering and piloting new technologies with a focus on nature-based solutions where possible and by enhancing governance and working in partnership with others.

Reducing flooding incidents
During 2022/23, the number of internal sewer flooding cases decreased again from last year with 0.63 incidents per 10,000 sewer connections (50 individual incidents). This is a significant outperformance against target and places us as one of the best performers in the industry on this measure. External sewer flooding events were impacted by the dry summer which led to debris within the network that increased the number of flooding incidents during the periods of significant rainfall from November onwards. The largest increase was on transferred sewers where smaller supply pipes were more impacted by these blockages.

Improving asset health

Sewer collapses & blockages
The dry summer weather has also increased the number of sewer collapses and blockages that are a key cause of flooding, pollutions, and service impacts to our customers as well as a lead indicator of assets health.

We have seen collapses increase to 8.3 (from 6.7) collapses per 1,000km of sewers ahead of target for the year. Whilst blockages also increased to 7,056 (from 6,545) marginally adverse to the 7,020 target. We will continue with the proactive management of our network, including a relentless drive to investigate, clean, and repair sewers. This is supported by an enhanced programme of educational visits to commercial premises over sewer misuse (fats, oils, and grease) and we are developing our approach to target those properties that habitually block our sewers with debris.

Pioneering catchment management for over 15 years
We maintain that our pioneering catchment management approach for over 15 years is fundamental to help unlock the environmental challenge we all face. Approximately 111,000 hectares have been improved to date with catchment management being undertaken across 80% of our region, working with over 1,700 farmers. Our continued commitment to tree planting is ahead of plan with over 220,000 trees planted towards our 250,000 target by 2025.

The additional catchment management targeted in our Green Recovery initiative is also progressing well with 350 hectares of peatland restored on Dartmoor and delivered with farmers.

Targeting improvements in EPA

A combination of a basket of measures, the EPA is the Environment Agency's assessment of environmental performance. We have seen improvements across all these measures this year with a provisional rating of 2 star this year. With our strategy of achieving 4 star by 2024, there is much to focus on.

Pollution incident reduction plan delivering results

South West Water's Wastewater Pollutions Incident Reduction Plan continues to deliver results after being launched in September 2020 – with a 50% reduction in incidents over the last 2 years. In 2022/23 there were 108 Category 1-3 incidents – our lowest ever level. In addition, our more serious Category 2 incidents reduced by 75% and positively we again had none of the most serious (Category 1) events.

Whilst we have seen improvements our focus remains to continue this step change in performance.

Our ongoing Pollution Incident Reduction Plan (PIRP) has continued to deliver with key activities including additional telemetry on our infrastructure with 1,440 sewer depth monitors installed in the year, continued investment at around 50 pollution hotspots to prevent repeat events, MOT investment at pumping stations and treatment works and using predictive analytics to support operations in managing issues before they arise. Our targeted rising mains replacement programme has delivered at 18 higher risk locations with a further 18 planned for 2023.

Numeric compliance

Numeric permits place measurable conditions on the final effluent discharged to the environment and measure compliance with these conditions. This year our MOT programme, investment plans and targeting third-party compliance have delivered our best ever score at 99.4% and is expected to be in the top quartile for the industry.

Rivers and coastal water quality

Our WaterFit programme launched in April 2022 is focused on nurturing healthy rivers and seas through reducing the number of storm overflow spills, reducing our impact on rivers by one-third by 2025, maintaining our excellent bathing water quality standards all year round and developing plans to target zero harm on river quality by 2030 with six pledges underpinned by specific targets.

One year into our plan and we have been making great strides towards our 2025 targets.

Reducing spills from storm overflows

With 100% monitoring of storm overflows now in place, a year ahead of plan, we have launched WaterFit Live, giving customers and visitors live information about the storm overflows which impact the region's 90 bathing beaches, as well as the detailed investments we are making to reduce overflow spills across the region's coastline by 2025. Through our latest campaign #Your beach, Your Say, Our investment, we are empowering customers and communities in working together to plan our next phase of improvements. In 2023, we are expanding WaterFit Live to all storm overflows across our assets.

For 2022, overflow spills have reduced by 30% on average (from 38.9 to 28.5), and we remain on target to deliver an average of no more than 20 spills across storm overflows by 2025. Whilst undoubtedly the dry weather will have played a part, over half of the improvements seen in the year are due to interventions we have made - whether capital investment to increase network capacity or through proactive maintenance.

Record quality levels recorded at our bathing waters

South West Water has over 860 miles of coastline to protect, representing over one-third of the UK's bathing waters. This is something we, and our customers, have always valued and prioritised. In 2022 we achieved 100% bathing water quality – for the second year running, with 99% meeting the more stringent good or excellent levels.

We have continued to deliver our planned bathing water investment schemes with 10 schemes at two sites in Bude, Cornwall, and Galmpton in Devon delivery this year.

Driving river water quality improvements

As part of our Green Recovery investments, we have started our three-year Rivers Dart and Tavy Inland Bathing Waters Pilot. The pilot aims to increase our understanding of the water quality of these two iconic rivers and build stronger relationships and collaborations with river users, local communities, and stakeholders – with over 50 stakeholders joining our Steering Group for the project.

We have developed an innovative approach to engaging with rivers users through the 'Hello Lamp Post' platform – using QR codes located at potential inland bathing sites and in other riverside locations to raise awareness of river water quality issues and capture people's perceptions of the river throughout the year. In addition, monitoring of the first bathing season has been completed through the use of real-time river monitors and 'spotsamples' and in summer 2023, we will also be using a state-of-the-art genetic monitoring technique to determine which types of animals are contributing bacteria to the river water.

Delivering for shareholders

Continued RORE outperformance underpins the Group's sustainable dividend policy whilst enabling the reinvestment of efficiencies and keeping customer bills low, with a double-digit RORE for South West Water for 2022/23 of 11.1% and Bristol Water of 4.6%. During K7 to date we have delivered Group RORE outperformance of 8.7% cumulatively, equating to c.£192 million – an increase on £149 million in 2021/22. This consists of c.£13[1] million – Totex^, c.£200 million financing, net of c.£21 million ODI penalty[2]. This has enabled the funding of additional initiatives, that are now well underway including:

- WaterFit - c.£45 million reinvestment of efficiencies to enhance coastal and river water quality.
- Green Recovery – c.£82 million accelerated and additional spend on initiatives delivering environmental benefits, including river water quality pilots, smart metering, and peatland restoration.
- WaterShare+ – acceleration of c.£20 million returns to customers through our second issuance in K7.

ODI performance across the Group in 2022/23 has been impacted by the freeze/thaw conditions across the region over the winter months. South West Water continues to build on its strong ODI performance, with c.70%[3] either on track, or ahead of target across a broad range of challenging bespoke, common, and comparative measures. ODI performance for South West Water during 2022/23 has resulted in a penalty of c.£4.2 million (2021/22 net reward c.£0.6 million). Bristol Water is on track to achieve c.65% of its ODIs and has resulted in a net financial penalty of c.£5.9 million.

Our flexible financing strategy and the company's diverse debt portfolio, with a relatively lower level of index-linked debt compared to the industry average allows us to outperform the cost of debt allowances. Our efficient financing strategy continues to drive significant outperformance with South West Water's effective interest rate at 5.5% (2021/22 3.9%[4]).

Whilst the elevated inflationary environment is placing significant pressure on costs, including wholesale power, we continue to focus on efficient Totex delivery, supported by our pioneering approach to innovation across the Group.

1. Includes c.£18 million tax
2. Excludes the impact of the third-party Carland Cross event in 2021 which we are seeking to recover from the third-party
3. ODIs on track or within regulatory tolerances
4. 2021/22 water business comparator of 3.7% re-analysed to provide comparative performance under post-integration South West Water Limited group of companies' structure

B2B retail services

Pennon Water Services (PWS)

PWS continued to deliver for business Customers via a suite of attractive contracted dual retail tariffs, loyalty bonuses and value-added services, whilst also delivering year-on-year improvements in its revenue, EBITDA and PBT.

Serving its customers

PWS maintained its focus upon high quality customer interactions, resulting in a Trustscore of 4.8 out of 5 measured through the independent review platform Trustpilot, comparing favourably to its peers. Its large strategic users of water rated the quality of service from their account team at 4.95 out of 5, demonstrating its ability to provide tailored support services to meet varying business needs. Its customer service teams issued over 300,000 customer bills in the year and answered over 90,000 phone calls, assisting with simple queries as well as complex customer challenges relating to their site and its future requirements. Its focus upon root causes of complaints into its own service and those it recorded against wholesalers has supported a 15% reduction in its volume of complaints compared to the prior year and a 24% reduction in escalated complaints.

Revenue Growth	PBT
12%	**£1.8m**
EBITDA Growth	**Trustpilot**
26%	**4.8/5**

Financial performance

Revenue increased by 12% from £195 million in 2021/22 to £218 million in 2022/23. A direct result of continued customer growth, low customer attrition and customer consumption increasing.

EBITDA and PBT grew by 26% and 80% in the year respectively, demonstrating operational efficiency against its higher revenues and the success of its focus upon customer debt recovery and the support of wholesaler incentive schemes, improving the accuracy and efficiency of the deregulated market.

Since the competitive market opened in 2017 PWS has switched over 21,000 supply points. Its simple, clear and transparent approach to pricing has proven popular with businesses of all sizes, especially strategic users of water who value its expertise and support in developing water strategies encompassing contingency plans and measures designed to reduce consumption, save money and minimise carbon impact. New contracts in the year included Places for People, Frasers Hospitality and Frank Roberts & Sons.

Whilst growth in new contracts continued PWS maintained its low levels of customer attrition. Since 2017 just over 11% of its deemed contract customers have switched to another supplier, many a result of National tendered procurement exercises at unfavourable margins where we opted not to compete. Our continued focus upon value and service to customers ensured we renewed 100% of our own tendered customer base including the extension of contracts with amongst others Princes Foods, ExxonMobil, Unilever, Walkers and Nuffield Health.

As a result of new contract growth and low levels of attrition, PWS' share of market consumption grew by over 9,000 megalitres, taking its cumulative position since the market opened to almost 50,000 megalitres, the equivalent of 20,000 Olympic sized swimming pools.

Delivering Innovation

The deregulated market was in part set up to drive innovation through competition. PWS has continued to seek solutions to lower business consumption over and above its package of leakage detection and repair products.

Following a successful bid to MOSL's inaugural Marketing Improvement Fund, PWS were awarded £150,000 to fund innovation projects for sustainable projects to save water. In partnership with SDS a sustainable drainage company PWS led a pioneering Rainwater Recovery project which will see businesses benefitting from a free installation of retro fitted, monitored rainwater recovery systems. These systems will store and filter rainwater collected from underground attenuation tanks for non-potable business use. The project offers a solution to a long-standing UK sustainability challenge by using less potable water for non-potable purposes such as vehicle washdown, irrigation and toilet flushing. This will reduce the amount of water wholesalers need to treat and distribute whilst saving customers money by using less treated water. Two systems for Plymouth Argyle and The Headland Hotel have been commissioned and are in operation with 40,000 litres of potable water saved to date.

Non-potable water is captured from existing underground assets and is filtered, pumped and stored aboveground ready for non-potable business use.

Outlook

Pennon Water Services remains well placed to deliver against its long-term strategic objectives, growing organically and sustainably, investing in its people, systems, processes and innovative customer solutions.

Water2business

Through our acquisition of Bristol Water, we acquired a 30% share in water2business – led by a strong team who are also focused on delivering an outstanding customer experience, with a Trustpilot score of 4.9/5. With a c.6% market share, water2business offers tailored water and wastewater management helping customers improve efficiency and deliver savings. Water2business delivered resilient financial performance during the year, contributing c.£0.3 million of associated companies' profit after tax to the Group's results, supported by the addition of c.4,400 new customers this year.

PWS took an active role in engaging with Ofwat, MOSL and Defra to continue to evolve the water market for all stakeholders

How we do business

We believe that ESG is not a bolt on, it's woven into how we do business.

We understand that we don't have all the answers and are here to serve our customers and local stakeholders; hence, we have created a framework to ensure that all voices are heard. This framework is underpinned by our innovative WaterShare+ scheme, which was developed in direct response to feedback from customers who said that they would like to share in our successes and have a greater say in our business.

In 2023, 1 in 14 customers in the South West Water region are Pennon shareholders and have the ability to have their say at our unique Customer AGM with further challenge coming from the independent WaterShare+ Advisory Panel. Those customers who are not shareholders and local interest groups have the ability to voice their concerns and share ideas at our periodic Stakeholder Engagement Forums - see the spotlight section below.

Our approach to business is based on a bedrock of good governance and a desire to be an exemplar of corporate citizenship. To this end:

- We are proud of the continued progress we have made this year to diversify our Board through the appointments of Dorothy Burwell and Loraine Woodhouse.;
- We continue to commit to procuring 100% of our financing needs through our Sustainable Finance Framework which aligns with the ICMA Green Bond Principles, Social Bond Principles and the LMA Green Loan Principles; and
- We were the first company operating in the water industry to be awarded Fair Tax status and have maintained this accreditation ever since.

Now is the time to double down on our integrated approach to ESG in order to meet the challenges faced in the communities we serve. Our impact is greater when we work in partnership and we have developed collaborative solutions to address issues, working with our customers, our people and landowners, some of which are highlighted in following pages.

Susan attending a Stakeholder Engagement Forum

Spotlight on...
Stakeholder engagement forum

In 2022, we developed a Stakeholder Engagement Forum. The Forum brings together all of our stakeholders to listen, collaborate, understand and knowledge share to make improvements across the Great South West. As a result of the Forum, we aim to:

- develop trust and confidence in Pennon Group as an organisation, genuinely committed to protecting and improving the environment, raising awareness of the activity already being delivered;
- ensure that our Group companies continue to be regarded by our delivery partners as a credible and suitable funder (in particular the Farming and Wildlife Advisory Group, Devon and Cornwall Wildlife Trusts, Westcountry Rivers Trust) as we seek to expand our collaboration with them;
- understand priorities, concerns and project pipelines of our stakeholders in order to reflect and respond in our strategic plans, and identifying opportunities for our involvement;
- identify and develop partnership collaboration opportunities to tackle local wastewater, flooding and drinking water challenges, including nature-based solutions, including delivery partners and landowners; and
- identify and create new forums where required and to respond positively to invitation

Read more about how our Board and Executive engage with our stakeholders in the Governance section which includes our Section 172(1) statement on pages 112 and 113.

Delivering more for our customers

Sustainable Development Goals

2022/23 highlights

- Average bills in the South West Water region reduced in the year (< 10 years ago) whilst investing at record levels
- Further significant progress vs target of eradicating water poverty by 2025 (c.110,000 customers helped this year)
- Significant funding since 2021 (£375k) for organisations that support the community by saving water, and neighbourhood community projects (146)
- 246 relationships established with local organisations to deliver support to vulnerable customers

2023/24 priorities

- Deliver value-for-money for customers - annual bill increase below inflation in year ahead
- Maintain investment in projects in our communities
- Increase our support for our vulnerable customers

Placing our customers at the centre of what we do

Stretching from Bristol to Bournemouth, Devon, and Cornwall, including the Isles of Scilly, we serve a unique population. Our region, given its dependency on agriculture and tourism, experiences large socio-economic challenges, particularly in urban and coastal areas.

School outreach

In the year we launched our WaterFit Warriors programme, to inspire thousands of water quality champions in schools and communities across the region. Our Pennon educational team spanning the Great South West has worked in 83 schools teaching 4,051 pupils, and helped over 280 students through its school talks, work experience and mentoring programmes.

We have seen the cost of living crisis put many of our customers in extremely challenging financial circumstances, some for the first time, placing even greater responsibility on the Group, to develop new, inclusive and creative solutions.

Keeping Bills as Low as Possible: We continue to keep bills as lows as possible with bills in the South West Water region being down £10 in 2022/23 and remaining lower than 10 years ago, whilst the acquisition of Bristol Water by Pennon has enabled us to deliver a reduction in customer bills, further aided by an innovative smoothing of bill increases across future periods to mitigate pressure on customers. Despite record levels of investment the annual increase for 2023/24 will be below inflation.

Sharing progress and innovation: We have accelerated innovative, inclusive projects to reduce bills and support our customers – our unique industry leading programmes, Watershare+ and our Stop the Drop targeted water efficiency incentive in Cornwall, has given nearly £50m back to customers through reduced bills during these difficult times, whilst also giving customers a greater say in our business and incentivising lower water use to protect our environment for the longer term.

Eradicate Water Poverty: We continue to target support to those who need it the most as measured through our industry leading ambition to eradicate water poverty by 2025, which we are on track to achieve. This is at the heart of our approach and we have already made great strides with nearly 65,000 customers being helped through one of our schemes from April 2020 to March 2023, with over £30m of support provided over the same period.

The innovative use of data is at the forefront of eradicating poverty, allowing us to identify and reach out to the 'struggling silent'. During 2022-23 we have developed a cross sector leading data suite and approach which has given us the ability proactively to identify customers at risk of being in water poverty. This coupled with information provided through our data sharing agreements with government bodies and local councils, has for the first time allowed us to auto-enrol customers onto support tariffs removing the need for customers to apply.

This has reduced the barriers for customers in getting the right support, allows us to reach the 'struggling silent' and ensures we are helping more customers than ever before. The success of this approach can be seen through the in year growth of number of customers on support tariffs by 12,452k (23%) with this set to further increase by 17,331 (26%) in 2023-24 across both South West Water and Bristol Water.

Our Affordability Toolkit: Goes beyond support tariffs and provides a range of measures for all customers designed to lower customers' bills and provide support to those who need it the most. Metering and giving customers the tools, advice and opportunity to save water and save money has not only bill but also environmental benefits with over 133,000 South West Water saving devices issued in 2022-23 alone.

Supporting Customers in Vulnerable Circumstances: We have empowered our staff to identify all types of vulnerability, from transient to long-term, to find the right support for our customers through enhanced, innovative training and ongoing support. We have been supported in the development of our Affordability and Vulnerability Training program, delivered to both Contact Centre and Field Staff, by external partners such as the mental health charity MIND and Dementia Friends. This has enabled us to provide additional insight and awareness for all customer service staff so that they are able to recognise potential and emerging vulnerabilities.

Going Further: To date over 110,000 customers have accessed or unlocked financial support from our support tariffs, company funded debt write off schemes and income maximisation but we know there is more to do as all customers are impacted by cost-of-living pressures. However, it remains vital that the most financially vulnerable in our society receive the support they need and to do this we expect the number of customers benefiting from support to grow by more than 50% to over 150k to 2025.

The Waterfit River Dart bathing water pilot with the Friends of the River Dart and MP for Totnes, Anthony Mangnall

Supporting our local communities

The need to reach and support our communities when they need our help the most only strengthens our resolve to work harder. To help us do this, we have launched our largest ever community outreach programme with our significantly expanded Community Team. This team attended 247 events across the South West Water region in the year, where our presence is most needed offering support and education and the opportunity to engage face to face.

One of the measures of success of our Community Outreach programme is the number of our most vulnerable customers who are on our Priority Services Register. This currently stands at 8% for South West Water customers and 6.5% for Bristol Water, with customer awareness of PSR and the extra support and assistance we offer leading the industry as measured by the CCW.

Our wider understanding of the affordability crisis and where we can help extends to our community teams, who are constantly being trained to have a deeper understanding of energy and other bills so that they can also offer holistic advice.

Through the Bristol Resource West Partnership, a partnership with Wales & West Utilities and National Grid, we are launching a trial of how energy and water messaging and support can be delivered together allowing us to reach even more customers.

Community Funding

South West Water have launched two community funds which, since 2020/21, have already provided £375k of funding and will continue to provide support in the months and years ahead:

- Water Saving Fund - a first of its kind £75,000-a-year Fund designed to support community groups and registered non-profit organisations within SWW's service area who can provide a benefit to the community by saving tap water and demonstrating a reduction in water use. This saving not only positively impacts the environment but saves customers money on their bills.
- Neighbourhood Fund - is all about supporting our local community. We have made £100,000-a-year funding available for neighbourhood community groups which inspire physical activities, education, health and wellbeing and deliver positive environmental outcomes.

To date we have funded 146 neighbourhood projects with the aim of:

- Protecting nature for the benefit of community health and well-being.
- Providing new opportunities for people to learn and develop.
- Assisting local projects which bring communities together.
- Supporting upkeep neighbourhood centres and facilities to keep communities strong.

Our team ready to meet customers at the at the Trevithick Day, Camborne, Cornwall

Partnerships

We understand the value of partnership working to deliver support to our financially and non-financially vulnerable customers and have over 170 relationships in place with a variety of organisations across our regions. These can be split into six key groups:

So we can expand our partnerships, which have never been so important, increase the support help us to reach out to the 'struggling silent' who would not otherwise realise they are entitled to support we have initiated the facility for local partnerships/charities to apply for support on behalf of customers through a personalised web page called our 'WaterCare Hub' which also incorporates our affordability toolkit.

Some examples of the work we are undertaking with our partners in response to the affordability challenge all customers are facing include the support we are providing to North Somerset Council's public living rooms, which are warm spaces for our most vulnerable customers. We are providing funding to help run some of these living rooms.

With the cost of energy soaring, we recognise that our most vulnerable in society will be choosing between heating and eating, or even both.

We have also partnered with Bournemouth and Poole Citizen's Advice Bureau and Wessex Water to jointly fund a 'Water Guru', who works with customers in-person to advise if they might be eligible for support.

Through our partnerships our community teams have also set up regular stalls in local food banks, job centres and community affordability events, as well as in public living rooms, to increase our visibility and awareness in local communities and have agreed with local food banks to provide information packs on our affordability support in food bank parcels.

64

local community groups and foodbanks

40

council and government groups

40

charities

20

housing associations

9

debt support partnerships

3

NHS surgeries

The Deaf Hub receiving funding from our Neighbourhood Fund scheme

We want to be the best place to work for our people

Sustainable Development Goals

Our People Strategy is all about, 'talented people doing great things for customers and each other'

2022/23 highlights

- Ranked 1st in the utility section of the FTSE Women Leaders Review
- Achieved external accreditation as a Great Place To Work
- Announced plans to double down on apprenticeships/graduate opportunities and work placements to 1,000 and 5,000 respectively by 2030

2023/24 priorities

For 2023/24 we will continue to deliver in line with our Group People Strategy and our Priority Areas. These include:

- Developing out leadership and management capability
- Refreshing our Group Values
- Continuing to invest apprentices and graduates

Pennon Achieves Gold Status

We were delighted to be awarded Gold Membership status into the 5% Club, where members are united in addressing the issue of poverty, a result of high youth unemployment and in ensuring the right skills in the workplace.

We are the only utility sector company to achieve the Gold Membership accolade.

Achieving Gold status demonstrates our long-term commitment to investing in structured Apprenticeship and Graduate programmes for our employees.

As one of the largest employers in the region, with over 3,000 colleagues, we have a responsibility and duty to make a positive societal contribution. Our goal is to be the Employer of Choice across our region through promoting social mobility, prioritising Diversity and Inclusion by addressing racial and gender inequality, and in providing safe, secure and meaningful employment where all employees are paid fairly for the work they do and where trust is high.

Over the past 10 years the South West has seen significant population growth. It's been estimated that more people moved to the region during the pandemic and just after than had been anticipated by 2050. This increase in population has an impact on many different areas of society, including employment, housing and opportunities for young people.

Our Reward Strategy continues to evolve each year, noting the feedback we receive from colleagues ensuring it aligns to our People Strategy. The key focus for this year has been on supporting colleagues during the cost-of-living crisis. Prioritising those colleagues that need it most: those earning up to £40,000 (over 80% of colleagues) were awarded an annual pay increase of 7% as well as a one-off lump sum equivalent to three months backdated pay increase and an additional day's holiday for this year, giving a total value of 9.2%. Those earning above £40,000 have received a tapering award with employees earning over £80,000 awarded 4.6%. During 2022/23, as part of the Bristol Water integration work, we have used the strategy to review the remuneration elements received by Bristol Water colleagues ensuring parity across the organisation at total remuneration level. All colleagues are now able to participate in the all company share arrangements following the roll out of the Share Incentive Plan across Bristol Water and the Sharesave schemes.

With a double coastline and dispersed population, many coastal towns around the South West suffer from high rates of poverty, unemployment and health risk factors, together with poor housing and public service provision, poor public transport and communication connections.

One of our customer service advisors discussing the benefits of smart meters and affordability initiatives with a customer

All this goes to show that whilst the greater South West region has traditionally had a reputation as a well-off area, in reality the picture is far more complex. This places an even greater responsibility on Pennon, as the largest private sector employer in the region, and given the wider supply chain we support.

At Pennon we take our social stewardship role seriously, whether that's through supporting the Green Recovery of our region with a £82million investment in economic and public health projects, and in creating up to 500 jobs directly and in the supply chain. Bristol Water's Social Contract seeks to do the same. Established in 2019 it looks at the key community wellbeing challenges and identifies specific projects in response. It aims to have a positive impact on customers, communities, colleagues and the environment.

Our approach to Human Capital seeks to go further; supporting Community Investment and social mobility across the Greater South West by creating education and employment opportunities across our region; ensuring we pay our employees a fair wage for doing a fair day's work and therefore be well placed to be able to make a wider societal contribution; and delivering our Diversity and Inclusion strategy by prioritising diversity of thought, gender and ethnicity to promote social mobility and opportunity for all.

This is all part of a wider strategy to be the employer of choice in the region, and in creating a Great Place to Work.

Over 100

Mental Health First Aiders trained

1,000

new apprentices and graduates by 2030

Across the Group we have developed a coherent approach to leadership, culture, talent, and skills development which will not only help us unlock the full potential in our business, ensuring we are match fit today, but also in anticipation of future challenges.

Over the past two years, we have been focused on making a step change in our approach to leadership, culture, talent, and skills. This ensures we are well placed to meet the challenges of today and also in anticipation of future challenges, as the Group evolves.

Ensuring our people are at the heart of all these key areas of focus will mean we continue to successfully deliver for all our customers and stakeholders that rely on us. Our people are our greatest asset. We are proud of the values we live by in all that we do and we have been delighted in how our employees have risen to the challenges we have faced throughout the last year and in going above and beyond to deliver for our business and our customers.

We continue to deliver across all areas of our Group People Strategy, ensuring we remain focused on the right areas and meet both the external and internal opportunities and challenges we face. In the battle for talent, it's clear that the most successful organisations will be those who can lead and galvanise others around a sense of mission, offer purposeful opportunities at work, make a broader societal contribution with strong values, and have the appropriate infrastructure in place to invest heavily in skills and development programmes.

On 1 February 2023, Bristol Water colleagues officially became part of the Group, helping us transition into the new One Pennon team as we successfully transferred our Bristol Water colleagues into South West Water. As One Pennon, we have brought together the best-of-the-best to share our expertise and best practices, building on our respective strengths and our strong heritage in delivering our essential water services for those who rely on us every day.

The integration of Bristol Water has acted as the springboard to review and restructure our organisation design across the business to ensure

Onsite at Mayflower Water Treatment Works in Plymouth, Devon

we develop the most efficient operating model for the future, while embracing the best of both Bristol Water and South West Water.

We continue to work to develop strong relationships with our employees and Trade Union Partners, ensuring we are engaging with these important stakeholders in our business in all aspects of our People Strategy.

As a purpose-led organisation, Pennon has strong values and ethics which are important barometers in fostering the culture and beliefs that we require to be successful. One of the key reasons why we use Great Place to Work to survey our employees is that it is one of the few providers that seeks to measure values and ethics. These are notoriously difficult areas to measure as they are impacted by individual's personal values and ethics.

Our focus in 2023 will be to engage with colleagues to redefine our values, in support of the Group's Strategic Direction following our acquisition of Bristol Water there is an opportunity to review both organisations' current values and develop a combined set of values.

Our 2022/23 Great Place To Work (GPTW) Colleague Survey took place for all Pennon Group employees. With a record participation rate of 85%, and a trust index score of 65%, Pennon has successfully achieved GPTW accreditation for the second time in a row. This is a strong result, given that typically, whilst the journey to becoming a GPTW is generally associated with big picture actions, maintenance is harder, with more targeted interventions.

We are delighted to be formally recognised as a Great Place To Work for the last two years, but we are determined to keep improving and we are focusing on colleagues 'doing the right thing' across all areas of the business through:

- our Speak Up process where employees can highlight a potential problem or issue
- our improved disciplinary and grievance processes
- our Quality First Drinking Water Services programme prioritises always doing the right thing and never compromising on quality
- our HomeSafe programme that is focused on the non-negotiables around safety
- our new STREAM performance review process encourages quarterly review meetings, helping ensure we deal with problems quickly and effectively
- the launch of three internal training programmes designed to help in this area, covering People Management, Inclusive Leadership and Bullying and Harassment.

Listening and acting on employees' views

Under the Financial Reporting Council's (FRC) code of standards, companies are required to explain how they are incorporating employee views in Board decisions. You can read more on how the Board are engaging and making decisions in our Section 172(1) statement on pages 114 and 115.

Over the course of this year, we have continued to develop and evolve the opportunities for employees' views and input, as well as enabling employee forums across the Group to ensure employees are represented and have opportunities to understand and feed into discussions on matters that impact them and the work they do.

RISE - Our Employee Engagement panel

During the year we have embedded our relaunched Employee Engagement panel, RISE. The new RISE forum is inclusive and employee-led, with each area of the business establishing its own panel that feeds into a larger, Group-wide panel chaired by the Group Chief Executive Officer. During the year we have integrated Bristol Water employee members into the forum and addressed important topics including cost-of-living, our future working arrangements: onboarding, induction and colleague communications. Throughout the year, we have increased our RISE members to over 100 members, giving employees an even stronger voice.

Speak Up

Our Speak Up whistleblowing policy continued to operate throughout the year, providing another engagement channel. Speak Up helps to create an open, transparent and safe working environment, where employees feel able to speak up and are supported if they do so. Read more on Speak Up on page 119 in the Corporate Governance Report.

Additionally, all employees are invited to pose questions or comments to our senior leaders through our new Open Door communication channels. This new approach brings together several employee communication channels and encourages employees and senior leaders to keep connecting more.

Enhancing our employee communications

During the year, we have enhanced and grown many of our employee communications and engagement channels.

Our regular Big Chat video calls with our CEO and the Executive team continue to be very well supported by employees with strong engagement. Items discussed largely focus on the topical business issues of the time plus key employee highlights. We have also broadened the group of speakers, involving colleagues from all areas and levels across the company.

Our Time to Talk sessions focus on a broad range of topics and are supported by many external specialist speakers and facilitators. Topics discussed include mental health, the cost-of-living crisis, financial wellbeing, apprenticeships and business specific initiatives including nature and catchment management.

Our internal communications tool and discussion platform, Yammer, is growing in popularity and is now used regularly by over 2,000 Group employees.

For our remote teams working tirelessly around the clock, we host regular breakfast meetings supported by our senior leaders. These have proved to be helpful in promoting more effective two-way communication with front-line operational teams.

WaterWorks is a new monthly performance measures dashboard which helps employees keep updated on how we are delivering for our customers, communities and the environment.

We continue to recognise our HomeSafe Heroes and celebrate the work of our colleagues across the business who make sure that everyone goes home safe every day.

Customer Service heroes at the Royal Cornwall Show, Summer 2022

We have a strong commitment to investing in the development of our employees and in building and recognising talent across the Group. Training and development are available for employees at all levels within the Group and are actively encouraged to participate. Our aim is to increase productivity, job satisfaction and safety, and to equip the next generation of leaders and employees with appropriate knowledge, skills and the competencies they need to thrive.

As a business we joined the 5% Club, an organisation with over 750 members that aims to address the issue of poverty arising from high youth unemployment and a shortage of the right skills for the workplace of today and tomorrow. This year, we were delighted to be awarded Gold Membership status into the 5% Club as we have around 10% of our employees undertaking apprenticeships or on a formal structured graduate programme. We were the only utility sector company to achieve the Gold Membership accolade. Achieving Gold status demonstrates our long-term commitment to investing in structured Apprenticeship and Graduate programmes for our employees.

During the year, Pennon also scooped two awards at the National Apprenticeship Awards. Pennon won Large Employer of the Year at the regional finals and was also awarded Highly Commended in Recruitment Excellent category. We are delighted that our apprenticeship programme was recognised for these awards as it confirms the high quality programme we offer and showcases the talented apprentices we have.

Throughout 2023/24, we delivered 15,458 training days for our 3,143 employees, ensuring that on average each employee received 36 hours of training - 5 days.

Our Graduate programme

In our 2022 Annual Report, we explained how we had launched our new Graduate Management Programme and set a long-term commitment to recruit 100 graduates by 2025. The programme has proved such a success in attracting both female and ethnically diverse talented graduates, we have doubled our commitment to recruiting 200 graduates by 2030.

Since the launch two years ago, the graduate programme has recruited 55 talented graduates, with over half being female and almost 60% being ethnically diverse or international graduates. Attracting larger numbers of female and ethnically diverse employees has been a core part of our People Strategy. We are delighted our graduate programme is helping deliver this outcome whilst providing high-quality career opportunities for all these individuals.

Apprenticeships

In addition to our graduate programme, we have a long-standing commitment to apprenticeships. This year we have doubled our commitment and target for apprenticeships/graduate opportunities and now pledge to support 1,000 roles by 2030. Attracting and developing the next generation of talented employees is vital in building resilience in our workforce and ensuring we can deliver the essential services our customers and communities deserve.

Last year we supported a further 141 new apprentices across the Group. This brings the total number of new apprentices we have supported since 2021 to 342, we are ahead of schedule to achieve our 2030 target.

Leadership development

We have continued to invest in our senior leaders to provide structured assessment and development opportunities for our senior leaders. This programme supports leaders across the whole Group and was one of the first activities offered to Bristol Water employees as part of the integration.

One of our hard working apprentices

Prioritising health and wellbeing

Our Wellbeing strategy is a core area in our People Strategy to ensure our people know that we care about them. It is estimated that in any given week, one in six people of working age experiences a common mental health problem like stress, depression or anxiety. Most of us will understand, from personal experiences or friends and family, the huge personal cost that this can bring.

Our Wellbeing strategy focuses on the following four main areas:

Mental

Taking care of our minds, coping effectively with life and creating satisfying relationships

Physical

Taking care of our bodies, acknowledging the importance of activity, nutrition and sleep

Financial

Taking care of our financial wellbeing, being in control over our financial future

Community

Encompassing the major external and internal factors such as social health

Separately, data from Champion Health, our online wellbeing platform provider, supports the outcomes from the Great Place to Work survey. 93% of employees who completed the Health Assessment were motivated to change, with their three key areas being improving energy levels, reducing stress and improving mental wellbeing.

Our approach to wellbeing, incorporates a number of initiatives including:

- **Mental Health First Aiders:** We have trained over 100 Mental Health First Aiders across the Group – one for every 30 employees, ahead of our target of one for every 50 employees.
- **Wellbeing Champions:** We have established a network of wellbeing champions across the business to help us engage colleagues.
- **Time To Talk:** Regular sessions where colleagues are invited to join online webinars focusing on a range of health and wellbeing issues, primarily focused on mental health.
- **This is Me:** a podcast with colleagues talking about their own health and wellbeing experiences and how they have dealt with them.
- **Champion Health:** Our Champion Health portal gives colleagues a broad range of resources, advice and guidance across all areas of wellbeing from healthy recipes to fitness regimes, mental health support and health assessments. It is free to both employees and their families.
- **FinWell partnership:** We have launched a new partnership with FinWell, a financial wellness organisation to provide employees with help, support and advice about their personal finances.
- **Inside Out partnership:** Our close partnership with the Inside Out Leaderboard provides a tangible way of demonstrating leadership, commitment and action to the mental health agenda.
- **EAP Helpline:** Our Employee Assistance Programme (EAP) had a 6% uptake compared to the industry average of 1.39%. The service is also available for employees' families.

HomeSafe – our flagship health and safety programme

The Group's flagship health and safety programme, HomeSafe, continues to provide the framework for driving significant improvements in all health and safety activities., delivering a 14% reduction in our Lost Time Injury Frequency Rate (LTIFR) in the year.

We continue to drive a culture where every person takes ownership to ensure they and their colleagues go home safe every day. After delivering our best performance in 2021/22 recording the lowest number of lost time incidents ever, we set the ambitious target to have our best year ever once again, while continuing to drive change and improvement against each of the six HomeSafe strategic pillars, improving risk management and reducing harm.

Our Leakage Detection Team in the field

We set out to achieve this through:

- continued Senior Manager face-to-face engagement.
- implementing a robust and consistent approach to incident investigations leading to improved identification of the root cause of incidents, tackling these quickly.
- integrating best practice knowledge with Bristol Water and implementing these quickly across the Group.

We have taken the best-of-the-best approach in many areas including improved minimum PPE standards and HomeSafe concepts. Two areas in particular we have quickly standardised are the approach to point of work risk assessment and investigations accountability.

Managing risk

Sharing and learning

Working together

Protecting health

Enabling leaders

Being resilient

HomeSafe Heroes

We are proud of our people and celebrate positive health and safety behaviours through our HomeSafe Heroes programme. To supplement this, at our inaugural HomeSafe conference we invited our teams and our supply chain to nominate people for a variety of awards. In the category for 'HomeSafe champion', Owen Lovegrove was nominated by several members of his team. Owen joined us in June 2022 and has brought a fresh energy to health and safety within his team. Owen constantly questions why things are done the way they are, to ensure that he knows how to carry out the work safely, and also to try and find better, safer ways of working. Owen has led from the front with the Take 5 approach to completing tasks, ensuring that methodology is both safe and efficient. Owen ensures the right tools and equipment are available and in good condition before starting the task. This leadership has had a positive impact on the wider team.

Through Owen's relentless pursuit of safety improvements the whole team and now more engaged with identifying further health and safety improvements. Owen was presented with his HomeSafe Champion award at the Health and Safety conference in February, receiving his trophy from Adele Barker, Group Chief People Officer.

Our Bristol Water Bar at the North Somerset Show, Summer 2022

We implemented the Take 5 for Safety approach to point of work risk assessment that was active and delivering benefits In Bristol Water. We launched this to the Group at our inaugural Group Health and Safety Conference in February 2023. This saw over 170 colleagues and members of our supply chain come together for an interactive day focused on the Take 5 concept and the fact that, while no one believes an incident will happen to them, it really can. The audience enjoyed a presentation by the Pennon Board Health and Safety Committee Chair, Jon Butterworth, who shared his safety expertise and experience to help enthuse everyone to be a driver of change and become HomeSafe pioneers.

The second area is bringing in the simple 2:2:2 approach to investigations ensuring a timely response to incidents, investigations, learning and improvement, with a two-hour notification, two-day initial investigation and two-week finalised report and action plan developed. We have developed and refined our HomeSafe bitesize programme across the year and now have active modules for employees to use to increase knowledge, awareness and accountability to ensure everyone goes home safe every day. These modules are manager-led within teams, focused on the core principles, while supporting managers to focus these on specific activities their teams carry out. The bitesize programmes work for all employees, regardless of role or location.

We have increased our assurance through the year with our health and safety experts completing over 500 individual unannounced site and activity audits across Bristol Bournemouth, Devon, Cornwall and the Isles of Scilly. These audits focused on adherence with our Life Saving Rules in HomeSafe as part of our Managing Risk Strategic Pillar. Minor improvements were identified and resolved with the local teams immediately, with no major non-conformances found.

Lost Time Injury Frequency Rate (LTIFR) continues to be the Group's primary measure of health & safety performance. Against our ambition of our best year ever for the new Group composition, we delivered a 12.5% reduction in actual LTI numbers, with 28 LTIs in the year, compared to 32 last year and an LTIFR of 0.59.

In addition to our supply chain partners' involvement and support at the health and safety conference, we have held two dedicated Tier 1 and Tier 2 supplier health and safety days in the year, improving

collaboration and showcasing innovations to reduce risk and increase productivity. One of our Strategic Partners, Kier, hosted a 'Kier Live' event at Exeter Racecourse in August to showcase innovations in health and safety aligned to improved productivity, with particular focus on excavation safety and working in the highway.

Future plans

Our targets are ambitious, however ensuring everyone who works for us, with us or interacts with us goes HomeSafe every day is paramount, and that requires us to have ambitious plans. HomeSafe is not a project to be completed. It continues to be the way we work and deliver all our performance commitments. We recognise any injury is one too many and have very ambitious HomeSafe 2025 plans to improve health and safety across the Group, requiring us to have our best year ever, year-on-year. We have delivered on this for two consecutive years. We have set out our roadmap to 2025 that becomes ever more challenging and ambitious. However, we will relentlessly pursue improvement towards ensuring everyone goes home safe every day.

Diversity, equity and inclusion

As one of the largest employers in the Great South West, we have a responsibility to promote social mobility, address inequality and drive inclusivity across our region.

We continue to champion diversity and promote an inclusive workplace. We have published our Gender Pay Gap report for the sixth year and are delighted to voluntarily publish our very first Ethnicity Pay Gap report. These can both be found on our website: www.pennon-group.co.uk

It is important to be open and transparent about the gender and ethnic diversity of our employees and this report is a key tool for us to do that, whilst also allowing us to share the measures we have taken and will be taking to continue to create a more diverse workforce across all roles and levels within the organisation.

We also understand the importance of inclusion in retaining our people, ensuring our employees feel valued, have a sense of belonging and feel able to be themselves.

Following the acquisition of Bristol Water, we are now working to build a sustainable workforce underpinned by our investment in new talent programmes, with focused support and development for our female colleagues and colleagues from underrepresented backgrounds.

WorkFit candidate Hannah celebrating 1 year working as a Customer Service Administrator

It takes time to build representation at management and senior levels, which can often be one of the causes of a pay gap, but we are committed to attracting, retaining and developing talent from all backgrounds.

We are delighted to have been highly commended in the finals in the Balance in Business Awards. These awards focus on gender balance at Executive and Senior Leadership level with support of the FTSE Women Leaders Review.

We are pleased with the recent progress made but know there is more to do in increasing the diversity of our workforce during the coming year.

Creating a diverse workforce

If there was ever a time for us to put gender and ethnic diversity at the top of our agenda, then that time is now. Building a sustainable, agile and diverse workforce is a key pillar of our People Strategy.

We are one of a handful of top FTSE businesses to have both a female CEO and Chair and have more women on the Board than men for the first time in Pennon's history. Ranking in first position in the Utilities section of the FTSE Women Leaders Review, we are exceeding the 40% target. We are pleased to have made further improvements during the last year in two primary metrics - the percentage of the Executive Committee and direct reports (increasing to 47.2% from 44.4%) and the percentage of women on the Board (increasing to 55.6% from 42.9%), and we achieved the 7th highest score in the FTSE 250. Our all-employee female representation across the whole group has increased to 31.4% this year from 29.5%.

Once again, we were listed in the 2023 Bloomberg Gender Equality Index, as one of almost 500 companies globally committed to disclosing their efforts to support gender equality through policy development, representation and transparency. We have continued to make further progress against this measure for transparency in gender data reporting. Our overall score increased to 70% from 65% last year with our disclosure score exceeding 97%.

Pennon largely operates and employs people in the South West of England which traditionally has some of the lowest proportions of ethnic diversity in the country. However, as a responsible business, we believe we have an important role in ensuring we support mobility of all types. Over the last two years, we have increased our proportion of ethnically diverse employees significantly, from c.0.5% to 3%. This increase has come from our more-targeted recruitment approaches clearly acknowledging we welcome applications from ethnically diverse applicants, as well as from the Bristol Water acquisition. Despite the good progress we have made during the last year, there is still much more to do if we are to achieve our ambition to have a much more diverse workforce.

Recruitment

During the last year, we have redefined our Employer Value Proposition to be more attractive to a wider range of talent pools. We launched our new recruitment campaign #justaddwater as well as our new careers website to attract a more diverse applicant group.

We have also reviewed our approach to monitoring diversity and inclusion with a specific focus on job applications. We use a software gender decoder tool which allows us to check all our job adverts for masculinity to reduce the potential risk of alienating female applicants. Similarly, we ensure a large proportion of our images used in the adverts are of ethnically diverse employees, which encourages more diverse candidates to apply. We are pleased that we are seeing significant increases in the number of applications we are receiving from ethnically diverse applicants and females into what is still a male-dominated industry. Last year, around 28% of job applicants were female and around 26% were ethnically diverse. Additionally, offering dedicated support to new employees through the graduate programme and supporting the 10,000 Black Interns Programme have further bolstered these numbers.

Our employee network groups

We recognise and appreciate the importance of creating an environment in which all employees feel valued, included, and empowered to do their best and share new ideas. Employee networks play a key role in encouraging and supporting employees in bringing the best version of themselves to work, contributing to an inclusive environment and building a sense of community. Our employee networks provide peer-to-peer support and improved awareness, contribute to the broader Diversity, Equity and Inclusion enhancements and have delivered business improvements in how we work together. The employee network groups support: Race, Ethnicity and Cultural Heritage, LGBTQ+, Women, Menopause, Grief, Financial Wellbeing, New Parents, Carers and New Starters.

Change the Race Ratio initiative

In 2020, Pennon pledged its support to the Change the Race Ratio initiative, a campaign to increase racial and ethnic participation in the senior leadership of companies, as a route to encouraging more diversity at all levels and was the first water company to do so. During 2022/23, our pledge and ongoing commitment continued to help shape our business activities and decisions.

10,000 Black Interns initiative

We are pleased to be a proud supporter and sponsoring business of the 10,000 Black Interns initiative. During 2022, we successfully completed nine internships which provided opportunities for individuals to experience working in their chosen career functions. Following successful completion of their internships, most students returned to university to complete their degrees. Two have already graduated, and we were delighted to see them successfully apply for roles on our graduate programme. This important scheme not only offers black students an opportunity to understand our business but also to improve the levels of ethnic diversity across our industry.

Diversity awareness and training

We have continued our programme of Unconscious Bias training and have rolled this out to the majority of our senior leadership and hiring managers during the year. We have held Lived Experience group sessions to understand what it is like to work at Pennon for employees from minority groups. The outputs have been shared with our Diversity Committee to understand these perspectives and consider appropriate actions when issues are raised.

Our Gender Pay Gap

Since our last report, the composition of the Group has further evolved with the acquisition of Bristol Water plc. Shortly after the 2021 snapshot date, the Group completed the purchase, welcoming over 500 additional colleagues. This is therefore the first year of including Bristol Water in the Pennon Group results.

Our 2022 mean and median pay gaps have both seen an improvement since 2021 which shows positive steps in the right direction.

One of our water treatment technicians onsite

Highlights include:

Improvement of nearly 10% in the mean gender pay gap in Pennon Water Services

Improvement of 1.38% in the mean gender pay gap in South West Water

This has led to a mean gender pay gap of 8.41% for Pennon Group overall, with our median gender pay gap improving 3%. More can be read on our performance and plans on our website.

Ethnicity Pay Gap

In 2022, we have voluntarily produced and published our Ethnicity Pay Gap for the first time, which shows a pay gap of 10.3%. There is still more for us to do in this area, including increasing the employee self-disclosure diversity rates across the Company and continuing to attract more ethnically diverse candidates at all levels across the Group.

Furthermore, by offering dedicated support to new employees through the graduate programme and supporting the 10,000 Black Interns Programme, these approaches have both helped to further attract ethnically diverse applicants. As many of these applicants are recruited and progress their careers, we anticipate them having a further positive impact on our ethnicity pay gap.

Social Mobility Pledge

We continue to be a proud signatory of the Social Mobility Pledge and have set further commitments across the Group during this year to strengthen our resolve to deliver for our customers and communities and support the drive to address social injustice. During the year we have doubled our commitment to apprentice and graduate recruitment and set new targets to support 1,000 apprentices and 200 graduates on structured programmes by 2030. We have set a new commitment and target to offer 5,000 work placements for young people by 2030, significantly growing our previous work in this area but, we believe this is vitally important in helping young people understand our Company and the water industry and supporting them in their early careers.

One of our skilled lab technicians

Slave-Free Alliance membership

Pennon has maintained its membership of the Slave-Free Alliance, which is part of Hope for Justice, the global anti-slavery charity. Our membership demonstrates our commitment to the highest employment standards for both our direct employees and those within our supply chain. Our Modern Slavery Report is published annually and can be found on our website www.pennon-group.co.uk

Human rights

We are fully supportive of the principles set out in the UN Declaration of Human Rights, and the Group ethics policy outlines the high standards of employment practice with which all employees of Pennon Group are expected to comply. The Group also supports the International Labour Organization's core conventions for the protection and safety of employees wherever they may work throughout the Group. These standards are also embedded in our sustainable supply chain and documented in our procurement policy and Code of Conduct for supply chain partners.

Onsite at Banwell Water Treatment Works, North Somerset

The natural environment of the South West is incredibly special. From our precious National Parks and Areas of Outstanding Natural Beauty, to beautiful beaches. We're proud to call it home.

Focused on initiatives to improve the

environment

Sustainable Development Goals

2022/23 highlights

- 15,696 hectares of land management was improved, including over 300 hectares of peatland restoration. This now brings the cumulative total to 111,515 ha, as of the end of financial year 22/23, bringing us closer to our end of AMP7 target of 123,209 ha.
- With the help of our delivery partners we planted a total of 72,398 trees, far exceeding our annual target by nearly 50%. This now brings the cumulative total to 220,187 trees planted, well on our way to achieving our end of AMP7 target of 250,000 trees planted.
- We published our Biodiversity Strategy called "Growing Nature" which is a strategy to grow nature on our land and beyond
- We are becoming increasingly transparent, including increased Sustainability Reporting, which can be found on pages 67 to 95

2023/24 priorities

- Continuing to deliver land management, peatland restoration and tree planting targets in collaboration with our delivery partners
- Delivering a new programme of biodiversity enhancement schemes at targeted sites across the region, including the creation of wet woodland
- Continuing to improve the environmental impacts of water company operations across the region, including the installation of eel screens, eel and fish passes and the exemplary control of invasive non-native species

Drought presented opportunities for Pennon to further expand our control of invasive non-native species (INNs)

Burrator reservoir levels dropped to under 40%, which increased the risk of stress in the population of American signal crayfish in the reservoir which could cause them to move and spread, something which landowners are legally obliged to take action to prevent. Pennon worked with leading crayfish specialists and carried out a pilot large scale control of these highly invasive animals. With 2,470 trap days, nearly 6,000 crayfish were caught. This control programme will be repeated next year.

The Bude canal was virtually devoid of water, presenting an unusual opportunity to carry out Zebra mussel surveys to determine their exact location along the canal. We used novel methods to promote awareness of INNS and biosecurity, including sniffer dogs to locate invasive species. Pennon is proud to have the most sites in the AQUA (Aquatic Quality Award) biosecurity accreditation scheme and remains the only organisation to have any gold Awards - at Roadford and Burrator reservoirs. We also have 7 silver and 22 bronze accreditations. We continue to work with a range of stakeholders, especially supporting INNS Site Guardians, anglers and watercraft users (boats, canoes, wind surfers, stand up paddleboarders), both locally and nationally.

Water resilience and drought

2022 saw some of the hottest, driest, weather on record as a consequence of climate change. A combination of a lack of rain – the 4th driest summer in 130 years, the hottest summer, low levels of soil moisture and increased demand exacerbated by the impact of the pandemic and heatwaves, uniquely converged to put pressure at just one of our five strategic reservoirs, at Colliford. Importantly, no-one served by Colliford, or across our region, or visiting our region, suffered a loss of supply or dips in water quality.

At the same time, we maintained the environmental compensation releases from our reservoirs throughout 2022, essential to river health, and have continued to do so in dry periods of 2023. We are investing £125m to increase our access to water suppliers when we need them most. In 2022/23 we have invested to secure the equivalent of 25% demand in Cornwall and 12% in Devon. We can show that, whilst the circumstances in this one area were challenging, culminating in a worse than 1 in 200-year event, our actions were appropriately timed, and we are now more resilient across the region as a consequence.

Despite a lack of new reservoir capacity across the sector in the last 30 years, over the last 15 years we have been focused on building additional capacity. As early as 2007, Pennon invested in disused quarries in Cornwall to repurpose as water resources. Building on this, our proactive acquisition of Hawks Tor in March 2022, was an important mitigation, providing additional storage, and coming online in October 2022. Together with drought permits and focusing on demand side actions, such as 'Stop the Drop' and fixing of customer side leaks for free, has meant that from the lowest point of water resources levels at the end of October 2022, we are now sitting at 76% and 99% respectively for South West Water and Bristol Water. Bournemouth and the Isles of Scilly are also in a better position heading into spring/summer 2023.

We are not being complacent as we look forward for the rest of the year to 2024 and beyond. Our acquisition of Bristol Water, driven by synergies and strategic water resources benefits, and our active progression of the need for the new Cheddar 2 reservoir, brings benefits to all of the wider south west region, including the Wessex region.

In the meantime, we are focused on building further resilience into our region, Colliford Water Resource Zone and Roadford Water Resource Zone, and by 2025 we will secure resources to access when we need it most that is equivalent to 45% of Cornwall's demand and 30% of Devon's demand, and this is proactively being managed as part of a Drought and Resilience Programme, led by our new Group Drought and Resilience Director, David Harris. David has significant experience in managing water resources, and in managing through drought in one of the hottest climates in the world. Our objectives are to ensure that by 31 March 2024 Colliford and Roadford strategic storages both reach 90% storage to ensure that we do not have the risk of either dropping into Drought Level 3 during 2024 and therefore that we can break the "drought cycle".

Hawks Tor Reservoir, Bodmin Moor, Cornwall

Our Partnerships

Pennon is engaged and participating in the range of local and regional public, private and third sector partnerships tacking action to tackle climate change and nature recovery. We also convene a number of forums and events to engage partners and share best practice and we together reflect on progress and develop shared plans for the future. We are proud of the delivery partnerships with whom we monitor, collaborate and deliver our environmental improvement and biodiversity enhancement activities.

Biodiversity enhancement

Catchment management protects and improves river quality and critical water abstraction sources to provide clean, safe drinking water without the need to provide additional infrastructure. It is supported by our customers as part of Pennon's commitment to protect and enhance the environment in the catchments in which we operate. This performance commitment is designed to incentivise an increase in the area of land under active improved catchment management as part of the 'Upstream Thinking' and the more recent 'Green Recovery' project interventions. The annual target for Upstream Thinking is 10,000 hectares of new land under active improved catchment management (50,000 more hectares over the five-year regulatory period). The Green Recovery programme will deliver a further 10,000 hectares of new land under active management during the four years it will be active leading up to 2025. In 2022/23 a further 12,282 hectares of land were added to our Upstream Thinking project whilst a further 3,414 hectares were added to the Green Recovery programme, resulting in an annual delivery of 15,696 against an annual combined target of 12,000 ha. This brings our cumulative position to 111,515 ha of new areas under active catchment management since April 2015. This is above our performance commitment position of 95,209ha.

Biodiversity compliance

In order for Pennon to avoid pollution harming the most special and rare habitats and species present across the Great South West, we have a particular focus on freshwater locations. This includes sites which are designated as a Site of Special Scientific Interest, as a Special Area of Conservation, as a Special Protected Area, or as a County Wildlife Site. During 2022, there were no pollutions events at any of these locations and therefore, as in the previous 2 years, the target was met. This outcome supports the Pennon commitment to achieving the outcomes of the Government Environmental Improvement plan and its ambitions to improve the condition of all Sites of Special Scientific Interest in the next 10 years.

Preventing biodiversity deterioration

The maritime nature, climate and geography of the Great South West means that wildlife and nature are particularly under threat of deterioration from the presence and spread of invasive non-native species (INNS). Invasive non-native species (INNS) can impact on all aspects of the business with significant operational, compliance, reputational and financial risks and are considered to be one of the most significant causes of biodiversity loss globally. This measure is to incentivise the delivery of biosecurity installations at Pennon sites, to prevent the introduction of new and spread of existing INNS and over the last year we have accelerated our delivery of guidance and awareness raising signage which are now installed at 90 sites. We have also installed 11 biosecurity wash down facilities and are scoping two further watercraft washdowns. Our exemplar biosecurity wash down facilities at Roadford, includes a pressure washer for watercraft, an angling dip tank and a boot scrub.

Net Zero – our promise to the planet

In 2021, we published our Promise to the Planet - our ambitious plan to reduce our operational carbon emissions to Net Zero by 2030. At the same time, we joined the UN backed Race to Zero commitment which aims to tackle GHG emissions across our entire value chain by 2045.

Pillar	Our three-pillar strategy remains unchanged	Progress against our three-pillar strategy
1 Sustainable living	• Reducing emissions through changes to operational practices, increasing energy efficiency, and switching to lower carbon fuel sources. • Meeting our commitments to reduce leaks and help customers to use less water – protecting the environment and saving carbon.	• Our fleet transition plans have begun with the first 53 EV vans delivered. • We have partnered with Drax to deliver the charging infrastructure required with 15 new 22KW charge points installed across our sites. • Our energy efficiency programme has audited 19 of our treatment sites which has identified significant savings of nearly 1,175tCO_2e. • Across our offices and depots, we've implemented a number of energy efficiency projects including LED lighting at our Exewater site with an aim to expand our office energy efficiency projects over the coming year as part of our Net Zero plan.
2 Championing renewables	Maximising self-generation from renewables at our sites across the South West – working with partnerships and utilising our expertise. • Where we cannot generate enough electricity to meet all our needs ourselves, 100% of what we purchase will be from renewable sources.	• From April 2022, South West Water (excluding the acquired Bristol Water business) switched to 100% renewable sourced electricity as part of its new energy supply contract. • We are targeting to produce 50% of our own energy by 2030 from a mix of embedded onsite Solar PV, floating Solar PV, grid connected Solar PV, along with other renewables such as hydroelectricity and making more use of our bioresources for generating energy. • Our on-site renewable assets have been significantly enhanced, with 2MW of new solar capacity installed. • We've expanded our renewable energy team to support project delivery whilst maximising performance of our existing renewable assets. • The Group are also in advanced discussions with a range of counterparties offering large scale solar development opportunities at sites situated across the UK. These opportunities, which would be initially funded through the Group capital allocation of c.£160 million, offer the potential for attractive commercial returns, with actionable near-term development timelines. In May 2023 we acquired a c.40 GWh site in Dunfermline for a total acquisition and build cost of £35m. This site has potential for a 2-hour 60MW battery storage facility at a cost of £25m, which would support the broader UK grid's move to renewables and provide healthy returns.
3 Reversing carbon emissions	• Reversing carbon emissions from our core activities. • Working in partnership to ensure our core activities reverse carbon emissions through solutions such as peatland restoration. • Supporting the development of innovative solutions to develop low carbon footprint processes through research and development.	• Our catchment management programmes include peatland restoration, improving soil management, tree planting, creating wetlands and buffer strips and other nature-based solutions. These all lead to more carbon being stored in the landscape and less loss to the atmosphere. It's also good for water storage in the catchments and long-term resilience. • We have planted 72,398 trees against annual target of 50,000 trees and restored 303 hectares of peatland. Our current peatland programme aims to restore 2,800 hectares of peat bog across the South West by 2025. Our peatland restoration in AMP7 is expected to save around 650,000 tCO_2e over the next 50 years. Meanwhile the 250k trees we aim to plant by 2025 will save a further 100,000tCO_2e. • Looking forward, South West Water is developing an ambitious program of nature-based solutions for the PR24 Business Plan submission (2025-2030) to include investigating how WaterFit can support the improvement and opportunity for carbon sequestration in estuarine and marine environments.

As a Group, we have also committed to setting both near and long-term Science Based Targets (SBT).

Further details of how we are integrating climate into our business and readying for a low carbon future can be found in our TCFD report on pages 74 to 95.

GHG emissions performance

In line with good practice and to reflect the outcome of our 2021/22 materiality assessment, we set new interim Net Zero targets in 2022. Our 2022/23 performance is presented below.

Net Zero target	2022/23 Performance*	2022/23 Target*	2025 Target*	2030 Target
% Energy usage from renewable generation	6.8%	7%	13%	50%
Reducing GHG emissions (%)*	65.7%	65%	70%	100%

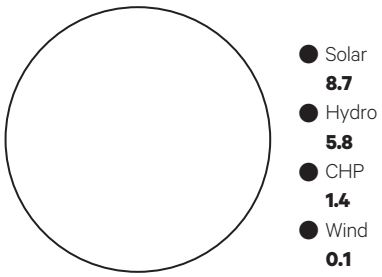
A – Externally Assured by DNV

* Scope 2 market-based emissions only

Renewable energy

- A key pillar of our Net Zero strategy, we are targeting 50% of our net energy use from renewable sources by 2030.
- We've made strong progress against our interim target of 13% in 2025 and achieved 6.8 % across the group in 2022/23. In particular we have increased our installed on-site Solar PV capacity to 5.5MW and solar and wind generation overall has increased 5.2% from 2021/22. Overall our renewables capacity now totals 17MW.
- In spite of this progress, increased overall energy demand, largely driven additional pumping required as part of our drought response, combined with the impact of the drought conditions on our hydropower generation (down 8% from 2021/22) meant we fell marginally short of the 2022/23 target.

Renewable energy capacity (MW)



GHG Emissions

- Scope 2 market-based GHG emissions have reduced from 89,434 tCO_2e to 31,321 tCO_2e this year from our 2020/21 baseline equating to a 65% reduction.
- Overall GHG emissions against our Net Zero 2030 scope[1] have decreased by 40%.

Full details of our 2022/23 GHG emissions are provided in our SECR report from page 67.

Process emissions

Process and fugitive emissions, mainly in the form of methane (CH4) and nitrous oxide (N2O), arise from our wastewater treatment processes. Worldwide there is difficulty in measuring process emissions and as a sector we are working together to update the calculated carbon aspects of our processes. As part of the sustainable operations pillar, we are doing two things:

- Investing in measurement - we can only manage what we can measure. This includes collaboration with industry partners to set up onsite emissions monitoring trials, as well as partnering with the University of Exeter, through our CREWW partnership, to analyse the data outputs from those trials.
- Investigating the opportunities to mitigate process emissions from our wastewater treatment by optimising our processes to minimise the formation of emissions, as well as exploring the potential for longer-term mitigation strategies such as using more innovative approaches to cover processes and capture emissions.

Transition Plan

Through our established strategies, plans and policies, we are preparing for a changing climate and lower carbon economy. Our annual TCFD response on pages 74 to 95 sets out further details of this in accordance with the TCFD recommendations. This identifies one of our key transition risks as rising energy costs. Through our planned investment in renewable energy alongside our dynamic hedging strategy we are managing this risk. We are aware of the work of the newly established Transition Plan Taskforce (TPT) to develop a 'gold standard' framework for transition plans. We are considering the TPT's guidance and will look to publish our Group Transition Plan in due course.

For further information, please see our Taskforce on Nature-related Financial Disclosures on page 73

1. Net Zero Plan scope includes Scope 1 & 2 (market based) GHG emissions and the following Scope 3 activities: outsourced activities; power transmission & distribution, business travel, grey fleet (private vehicles used on Company business)

Group Chief Financial Officer's report

Paul Boote
Group Chief Financial Officer

During 2022/23, volatility in the global economy, reflecting the geopolitical situation and economic difficulties arising from the global pandemic, has continued. We started to experience the impact of this in the second half of the financial year ended 31 March 2022 and, as expected, the impact of elevated inflation on power and interest costs has reduced our near-term earnings. The second half of this financial year has also been impacted by the drought in the South West, which has resulted in increased levels of operating costs and capital expenditure. Where appropriate, specifically identifiable operating costs have been treated as non-underlying given the unprecedented summer weather conditions with 2022 being one of the hottest, driest years on record.

Over the long term the elevated inflationary environment provides the Group with additional growth in long-term sustainable value with revenues and RCV linked to November and March CPIH inflation, respectively.

Bristol Water has contributed to the Group's financial results since 3 June 2021 with full clearance for the merger of our wholesale water businesses granted on 7 March 2022. The merger of South West Water and Bristol Water completed on 1 February 2023 with the combined water business now operating under one licence held by South West Water Limited. Within this report, to aid comparability both now and ongoing, the results of South West Water include the operating performance of Bristol Water in the current year and in the prior year. The results in the comparative financial year ended 31 March 2022 only include Bristol Water for ten months from the date of acquisition.

Financial highlights of the year

Resilient financial fundamentals

Future revenues linked to inflation, offsetting increased cost base, including significant increase in power costs in 2022/23.

More information on pages 44 to 47

Efficient financing strategy

Well placed in elevated inflationary environment as a result of our diverse debt portfolio.

More information on page 47

Increasing environmental investment

49% increase in capital investment compared to FY 2022.

More information on page 48

Investing in renewable energy generation

First site acquired in May 2023 to provide 36GWh of generation.

More information on page 51

The Group's statutory revenue for 2022/23 of £797.2 million included non-underlying revenue reductions of £27.8 million in respect of the second issuance under WaterShare+ (£20.2 million) and our "Stop The Drop" demand reduction incentive (£7.6 million).

The Group's underlying revenue has increased from £792.3 million to £825.0 million, an increase of 4.1%, with South West Water increasing by £13.5 million and Pennon Water Services delivering further external revenue growth, predominantly outside South West Water's regions, of c.£19 million.

Overall, underlying EBITDA has reduced 19.8% from £383.9 million to £307.8 million with the increase in power costs being the most significant contributing factor to this reduction.

Further details of the performance of South West Water and Pennon Water Services is outlined below.

We recognise the pressure the cost-of-living crisis poses to our customers and we are focused on providing a broad range of affordability measures to support those in financial need. Across all Group businesses, the potential impact of significant increases in the cost of living on affordability has been considered in assessing our expected credit loss charges.

Cash collections throughout the Group have remained robust during the financial year. Underlying expected credit loss charges for 2022/23 of £7.0 million for South West Water (1.0% of revenue) are in line with previous levels (2021/22 0.8%[1]). For Pennon Water Services, the expected credit loss charge of £0.8 million (0.4% of revenue) is also in line with previous levels (2021/22 of 0.3% of revenue).

The Group reported a statutory loss before tax of £8.5 million (2021/22 profit £127.7 million) after net non-underlying costs of £25.3 million (2021/22 £15.8 million). Group underlying profit before tax decreased to £16.8 million from £143.5 million in 2021/22. This outturn reflects the significant near-term pressures on earnings from elevated power pricing, financing costs and revenue reductions in the water business through lower customer demand as a result of continued water efficiency promotion and mechanistic regulatory adjustments[2].

South West Water

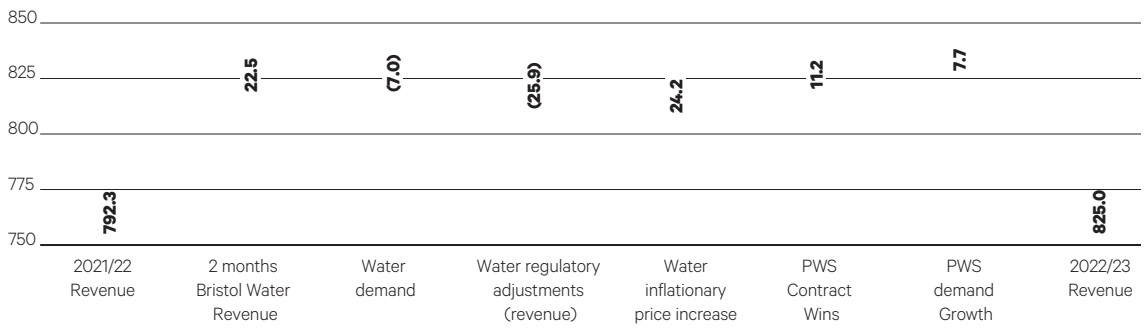
Since 1 February 2023, the trade and the significant majority of assets and liabilities of Bristol Water plc were transferred to South West Water Limited under a statutory transfer mechanism set out in the Water Industry Act. The Bristol Water brand will continue as a trading name of South West Water. As noted above the financial performance of South West Water includes the performance of Bristol Water in both this financial year and the comparative year.

Underlying revenue of £701.3 million for 2022/23 has increased by 2.0% (£13.5 million) compared with the prior year (2021/22 £687.8 million). Adjusting for the additional two months of revenue in this financial year from the Bristol Water region (£22.5 million), revenue on a like-for-like basis has reduced by £9.0 million, with the inflationary impact on tariffs being more than offset by the reduction in demand and regulatory adjustments to revenue, including in-year ODI penalties from 2020/21. South West Water's statutory revenue for 2022/23 includes a non-underlying reduction of £27.8 million in respect of the second WaterShare+ issuance and our "Stop The Drop" demand reduction incentive.

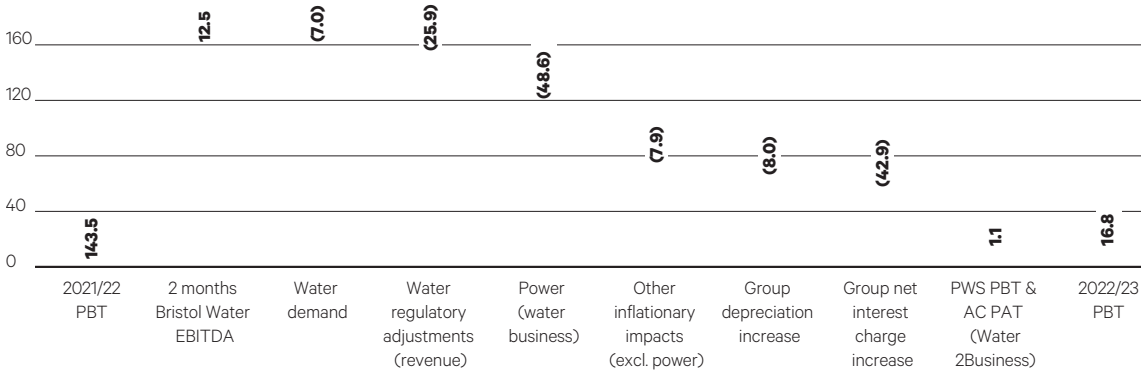
Underlying operating costs of £392.9 million increased by £89.9 million (2021/22 £303.0 million) reflecting the following significant factors:

- Inflationary and other macro-economic impacts on wholesale energy market prices and transmission costs (£48.6 million).
- Additional two months of operating costs (not including power) for Bristol Water (£10.0 million).
- Responding to operational drivers including continued elevated demand prolonging high production volumes, supporting improvements to leakage and pollutions performance, and underlying cost increases to address the extreme operating conditions including the freeze/thaw event to ensure resilience of water supply (£5.9 million).
- Increased costs relating to the price review for the next regulatory period

Revenue underlying^ (£m)



Profit before tax (PBT) underlying^ (£m)



^ Measures with this symbol are defined in the alternative performance measures section of the annual report on pages 220 to 223.

1. Includes full 12 month Bristol Water performance during 2021/22
2. Includes ODI penalties and revenue forecast incentive adjustment

- Pay increases of between 3-5% across the Group, with the majority at 5%.

South West Water's underlying EBITDA and underlying operating profit reduced by 19.9% and 34.6% respectively. Despite the level of inflation in tariffs lagging behind actual cost inflation in the year, overall increases in operating costs excluding power were carefully managed to remain broadly in line with the inflation embedded in tariffs.

The net interest charge of £145.3 million is £47.3 million higher than prior year (2021/22 £98.0 million) primarily reflecting the impact of higher RPI and CPI rates on index-linked debt. The Group's efficient funding mix, which includes a relatively low proportion of index-linked debt, and hedging strategy minimises these market effects resulting in an Effective interest rate^ of 5.5% (2021/22 3.9%[1]).

South West Water's capital expenditure was £358.2 million, an increase of £117.8 million (49.0%) on the prior year (2021/22 £240.4 million), primarily due to water resources investments to boost supplies and enhance water quality, including GAC schemes to provide further resilience, and development work at the new Alderney water treatment works in the Bournemouth region. Wastewater investments included the roll out of our WaterFit programme, targeted investments in wastewater pollutions hotspots and the installation of event duration monitors on our storm overflows to achieve 100% coverage in 2022. The increase also includes the additional two months of capital expenditure in the Bristol Water region in this year compared to last.

Pennon Water Services

Pennon Water Services has once again performed strongly this financial year through its disciplined approach to winning new business and benefited from higher demand.

Non-household demand has continued to recover, up 5.8% on 2021/22, and consumption is approaching pre-covid levels, with recovery predominantly in the hospitality, tourism and manufacturing sectors. New contract wins have contributed £11.2 million of additional revenue compared to last year. The overall growth rate in this financial year was 11.6% and compares to 2021/22 levels of 19.9%.

Underlying operating costs have grown marginally behind the improving revenues and the business has boosted its underlying EBITDA by 26.5% to £4.3 million (2021/22 £3.4 million). This strong performance has resulted in the business reporting a profit before tax of £1.8 million (2021/22 £1.0 million), a significant 80% increase on the previous year.

The business continues to maintain its focus on targeting high quality, sustainable customers who will benefit from the value-added services that form part of Pennon Water Services' differentiated service proposition, with new annualised contract wins of c.£14 million secured during the year.

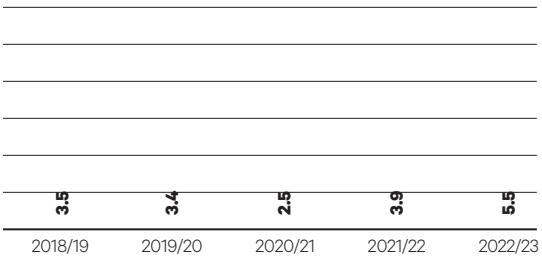
Group net finance costs

Total net finance costs for the Group of £118.2 million include £18.4 million non-underlying gain resulting from the repayment of the Bristol Water plc index-linked bond due 2041. Underlying net finance costs for the Group of £136.6 million are £42.9 million higher than last year (2021/22 £93.7 million), driven largely by the current high levels of inflation impacting index-linked debt charges but also includes an additional two months' finance cost contribution from Bristol Water in 2022/23. Whilst the Group benefits from a lower proportion of index-linked debt compared to the water industry average, following the Bristol Water acquisition c.30% of Pennon's regulated water businesses' gross debt was index linked. Actions have been taken during the second half of the year to smooth both inflation volatility over the period to 2025 and lower our level of index-linked debt over the long-term to around 20-25%. The non-cash element of our finance charges, which accretes to the debt principal, was c.£84 million (2021/22 c.£36 million).

The Group continues to efficiently secure funding for South West Water through its Sustainable Financing Framework and to ensure c.60% of its interest rate risk is mitigated in line with the Group treasury policy, which is achieved through issuing both fixed rate debt and effective interest rate hedging, with a further element being index-linked. Prior to the acquisition of Bristol Water, the index-linked proportion of debt had been maintained at a relatively stable proportion of c.25%.

In the second half of the year, the Group reduced its proportion of index linked debt by repaying the Bristol Water plc index-linked bond due 2041 and entered into £300 million of RPI to fixed rate swaps to fix the interest charge over the period to 2025 to smooth the impact of inflation over K7. These changes have helped to manage the Group's exposure to the current volatility in its finance costs.

Effective Interest Rate^ (%)



Share of post-tax profit from associated companies

As part of the acquisition of Bristol Water in June 2021, we obtained a 30% interest in Water 2 Business Limited (W2B), a water retailer joint venture with Wessex Water. This investment is accounted for under the equity method and following a period of losses, as the business reached scale, we are pleased to recognise £0.3 million of profit after tax from associated companies in this year's results.

Non-underlying items and acquisition accounting

Non-underlying items for 2022/23 total a charge before tax of £25.3 million (2021/22 charge of £15.8 million). Non-underlying items are those that in the Directors' view should be separately identified by virtue of their size, nature or incidence and where they believe excluding non-underlying items provides a more useful comparison of business trends and performance.

The non-underlying charge of £25.3 million consists of:

- £20.2 million reduction in revenue being the recognition in full of the second issuance of our WaterShare+ scheme, which has been extended to include Bristol Water customers and £2.2 million of associated costs.
- A combination of elevated demand from increased tourism and record-breaking extremes of prolonged dry and hot weather led to extremely low water storage levels in the Cornwall region. Drought permits were issued allowing increased extractions and water saving measures were issued for the South West Water region for the first time since 1995. To ensure the region could be supplied with water over the summer and continuing into 2023, South West Water has instigated a series of mitigating measures and one-off expenditure to address the situation. Due to the exceptional combination of these events and the significance of the mitigating actions this has resulted in the recognition of £7.6 million revenue reduction from the Stop the Drop discount incentive to reduce water consumption and £9.4 million of specific costs relating to the measures being treated as non-underlying.
- £4.3 million of costs in connection with the merger, statutory licence transfer and integration of Bristol Water into South West Water.
- £18.4 million gain resulting from the repayment of the Bristol Water plc index-linked bond due 2041, as part of re-balancing the proportions of index-linked debt in the Group debt portfolio.

The non-underlying charges in 2022/23 give rise to a net tax credit of £5.3 million in relation to the above items. In 2021/22 the total non-underlying tax charge was £98.2 million, including a credit of £1.3 million in connection with non-underlying pre-tax items and a £99.5 million non-underlying deferred tax charge, recognised for the change in future tax rate which was substantively enacted during the previous financial year.

As part of the requirements of acquisition accounting, we have finalised the fair values of the acquired balance sheet of Bristol Water. The provisional values reported in the Group's results to 31 March 2022 have been revised to reflect a £5.5 million increase in the fair value of the acquired deferred tax liabilities with a corresponding increase in Goodwill.

Goodwill arising from the acquisition of £121.6 million has been recorded in the Group consolidated balance sheet and is attributed to the synergies expected to be derived from the combination and the value of the workforce which cannot be recognised as a separately identifiable intangible asset.

Responsible approach to tax

The Group is pleased to confirm it has once again maintained the Fair Tax Mark accreditation for the year. This is the fifth year in succession that the Group has been awarded the accreditation and we are proud of our responsible approach to tax.

The overall 2022/23 tax credit for the Group is £8.9 million (2021/22 charge of £112.1 million). On an underlying basis, the net tax credit for 2022/23 for the Group of £3.6 million (2021/22 charge of £13.9 million) consists of:

- Current tax credit of £2.7 million, reflecting an effective tax credit rate of 16.1% (2021/22 charge of £5.0 million, 3.5%). This reflects a £2.7 million current tax credit in respect of the prior year as a result of additional super deductions and lower non-deductible expenditure following the preparation and submission of the 2022 corporate tax computations.
- Deferred tax credit of £0.9 million (2021/22 charge of £8.9 million). This reflects a current year deferred tax credit of £1.6 million in relation to capital allowances in excess of depreciation charged across the Group, largely due to super-deductions, offset by tax losses carried forward for utilisation in later periods. A £0.3 million credit also arises as a result of the change in tax rate, on current year items (including tax losses generated in the year carried forward for future relief) which will crystallise at 25% rather than 19%. It also includes a deferred tax charge in respect of the prior year of £1.0 million which arises largely due to additional super deductions.

There is also a non-underlying tax credit of £5.3 million in 2022/23 relating to the non-underlying items set out above. This includes a current tax credit of £2.8 million in relation to losses to be carried back to relieve against prior year profits, and a deferred tax credit of £2.5 million which relates to losses carried forward for utilisation in later years and the unwind of the fair value adjustment in relation to the Bristol Water bond terminated in the year.

The Chancellor announced in the March Budget, that the 130% super-deduction on plant and machinery will be replaced with full expensing deductions for the next three years from 1 April 2023 to 31 March 2026, with a plan to make this permanent when fiscal conditions allow. Without this change, the writing down allowance would have reverted to the previous rate of 18% on plant and machinery (where the expected life is less than 25 years). The 50% first year allowance on long life assets and integral features has been extended for the same three-year period, again with the aim to make this a permanent change. Without this, relief would have reverted to 6% per annum on a reducing balance basis. Given the Group's continued capital investment programme, these changes mean that the Group anticipates generating tax losses in the remaining years of K7, and therefore does not expect to make any corporation tax payments during this time.

Earnings per share

The Group has recorded a statutory earnings per share of nil pence per share for the year ended 31 March 2023 (2021/22 4.9 pence per share). This includes a net non-underlying charge before tax of £25.3 million and a net non-underlying tax credit of £5.3 million. Statutory earnings per share for 2021/22 were impacted by the significant non-underlying deferred tax charge in respect of the change in corporation tax rate and also the average number of shares used to derive the earnings per share were impacted by the share consolidation in July 2021.

Our adjusted earnings per share^ excludes the impact of deferred tax charges and non-underlying items. For the Group, we have generated adjusted earnings per share^ for 2022/23 of 7.3 pence (2021/22 50.2 pence), with this reduction in earnings reflecting the significant impacts from higher power costs and the impacts of inflation on finance costs and operating costs more generally.

Sustainable net debt position

The Group's cash flow from operating activities for 2022/23 was £313.7 million (2021/22 £334.2 million). Cash collections have remained robust and we continue to monitor cash collections closely and are focused on providing a broad range of affordability measures to support those in need of support.

Net interest payments were £154.8 million (2021/22 £72.0 million) within the increase driven by £51.5 million of interest paid on lease settlements relating to interest accreted to the lease principal and a full 12-month impact of Bristol Water. A significant element of the increased income statement finance charges arises from our index-linked debt, and is non-cash, as the indexation element accretes to the debt principal repayable on maturity.

Our accelerated environmental investment programme has resulted in an increase in capital investment cash outflows of £102.9 million to £330.5 million (2021/22 £227.6 million).

Other significant movements in net debt in 2022/23 include the final tranche of the share buy-back programme of c.£40 million, payment of our interim and final dividends for 2021/22 and £84.3 million of non-cash indexation on our loan instruments. Other movements of £116.4 million arise in the main from a reduction of debt associated with historically accreted lease interest (£51.5 million), the unwinding of fair value adjustments on acquired debt (£44.3 million), notably following the repayment of the Bristol Water plc index-linked bond due 2041, and VAT recovered on lease repayments (£21.5 million).

The Group's IFRS net debt at 31 March 2023 was £2,965.4 million (31 March 2022 £2,682.9 million), which is also referred to as sustainable net debt. This includes fair value adjustments on acquired debt of £124.0 million[2] which are released over the life of the related debt instruments. The Group's net debt position excluding these adjustments is £2,841.4 million.

Sustainable net debt

Pennon Group – summarised net debt flow (£m)	2022/23 flows
Net debt excluding fair value uplifts 1 April	**(2,514.3)**
Opening balance 1 April	**(2,682.9)**
Cash generated from operations	**313.7**
Corporation tax paid	**(1.4)**
Net interest paid	**(154.8)**
Capital investment	**(330.5)**
Repurchase of own shares	**(40.0)**
Ordinary dividends paid	**(101.6)**
Non-cash index-linked accretion	**(84.3)**
Other movements[3]	**116.4**
Closing balance 31 March	**(2,965.4)**
Net debt excluding fair value uplifts 31 March	**(2,841.4)[2]**

Agile and efficient financing

The Group has made several changes to its financing since the end of the last financial year to ensure we can efficiently support the needs of our business strategy and are agile to address the changes in the macro-economic environment.

Since 31 March 2022, the Group has secured and completed c.£825 million of new and renewed facilities, including:

- Our first syndicated £300 million private placement with an average maturity of 12 years.

1. 2021/22 water business comparator of 3.7% re-analysed to provide comparative performance under post-integration South West Water Limited group of companies' structure
2. Carrying value of fair value acquisition adjustments to debt as at 31 March 2023 - £36.4m Bournemouth Water, £87.6m Bristol Water.
3. Including fair value unwinds on settlement of Bristol Water 2041 bond, a reduction of debt associated with historically accreted leave interest and net VAT recoverable from lease repayments.

- £205 million of new term loans and leasing with an average maturity of 9 years.
- £25 million 20-year private placement.
- £295 million of new and renewed revolving credit facilities.

During 2022/23 all new and renewed facilities were raised under our Sustainable Financing Framework.

Our lease portfolio will continue to deliver long-term benefits as part of our diverse range of facilities as we look to further diversify our portfolio going forward, as a strand of our Sustainable Financing Framework. During the year, we continued our programme of repayment and restructuring of the portfolio to ensure its continued efficient and effective management with a further c.£167 million (including interest on leases) repaid during 2022/23.

The Group has taken steps during the year to re-balance the proportion of index-linked debt to align with previously maintained levels for the longer-term. In November 2022, we reduced our index-linked debt proportion by repaying the £40 million Bristol Water plc index-linked bond due 2041, generating an £18.4 million non-underlying gain.

The statutory transfer of the Bristol Water business to South West Water completed in February 2023, including outstanding debt being transferred on an unsecured basis.

Resulting from the changes above and drawing of new debt during the year, South West Water[1] gross debt at 31 March 2023 was £2,918 million (31 March 2022 £2,848 million). The debt has a maturity of up to 34 years with a weighted average maturity of c.15 years.

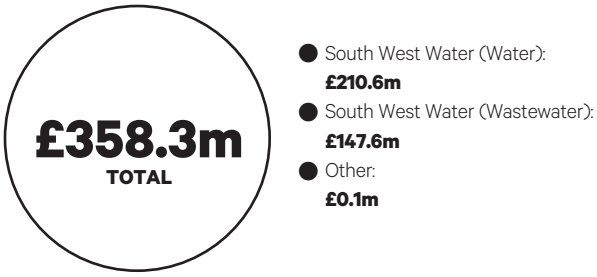
At 31 March 2023, South West Water[1] net debt to RCV^ ratio[2] stood at 60.8%, (31 March 2022 62.0%). This is broadly in line with Ofwat's notional structure of 60%.

South West Water's cost of finance, with an Effective interest rate^ in 2022/23 of 5.5% remains among the lowest in the industry, continuing to benefit from the diverse portfolio of debt.

Financing portfolio - strategic positioning

The Group has a strong liquidity and funding position with £420 million of cash and committed facilities as at 31 March 2023. This consists of cash and cash equivalents of £165 million (including £22 million of restricted funds representing deposits with lessors against lease obligations) and £255 million of undrawn facilities. £104 million of the cash holdings are held at the Pennon company level.

Major Categories of Capital Expenditure (£m)



Following the successful transfer of Bristol Water to South West Water, this has meant changes to the regulatory licence and we are targeting to obtain a strong investment-grade rating for South West Water for the start of the next regulatory period.

South West Water[1] net debt at 31 March 2023 is a mix of fixed / swapped (£1,854 million, 65%), floating (£609 million, 21%) and index-linked borrowings (£402 million, 14%), which reflects our diverse debt portfolio and compares to an industry average[3] of fixed / swapped 42%, floating 4% and index linked 54%. New debt raised during this regulatory period has been fixed to align to iBoxx indices in line with Ofwat's approach to allowed cost of debt. Where appropriate, derivatives are used to fix the rate on floating rate debt.

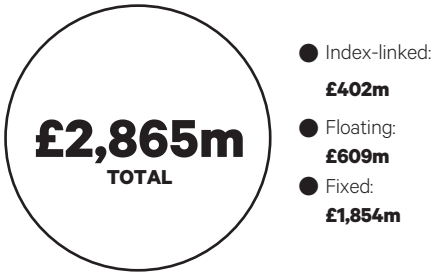
As we progress through the remainder of K7, we expect the mix of our debt portfolio to evolve and are strategically targeting index-linked debt to represent 20-25% of our portfolio in the long term. This will enable the Group to maintain its financing flexibility, whilst remaining within our treasury policy of at least 60% fixed rate debt.

As the Group continues to develop, and we see our funding requirements grow, we expect the Group to manage its portfolio with larger and more diverse debt instruments, taking advantage of the public ratings once established in 2025, in line with Ofwat's final PR24 methodology requirements.

Longham Lakes, Bournemouth

We will continue to maintain a diverse portfolio of debt to support flexibility and growth opportunities. We expect that our reinvestment of our outperformance in environmental enhancements will be financed through debt, resulting in increased net debt to RCV gearing in the short term. In the long-term this investment will provide returns though K8 revenues and a higher RCV. We now expect RCV to reach £5.2bn at the start of K8.

Water business Net Debt Structure (£m)



Internal borrowing

South West Water's funding is treated for regulatory purposes as ring-fenced. This means that funds raised by South West Water are not available for other areas of the Group.

Bristol Water was transferred to South West Water in February 2023 and all the debt is now managed on the South West Water standard covenant package as unsecured and unrated.

Pennon Water Services funding is predominantly provided by Pennon. Pennon will continue to use funds to support the Group's ongoing operations as appropriate.

Taxation strategy

Transparency remains a critical component of our approach, recognising that openness and honesty with our customers is essential. Optimising our tax position benefits them, for example by keeping water bills down, but we do not enter into artificial tax arrangements, use tax havens or take an aggressive stance in the interpretation of tax legislation. As a long-term business with a long-term approach to financial management, there have been no changes to the Group's overall tax strategy this year compared to last.

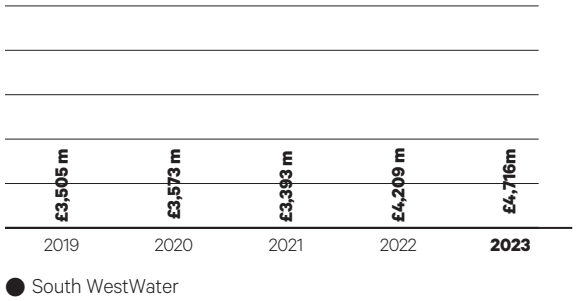
We continue to hold the Fair Tax Mark. Launched in 2014, the Fair Tax Foundation's purpose is to encourage and recognise businesses through their Fair Tax Mark accreditation scheme. This is an independent accreditation scheme for businesses paying their fair share of corporation tax and reporting on their tax practices transparently. Achieving the Mark demonstrates that we are paying the right amount of corporation tax in the right place at the right time and apply the gold standard of transparency.

Under our tax strategy we:

- At all times, consider the Group's corporate and social responsibilities in relation to its tax affairs.
- Operate appropriate tax risk governance processes to ensure that the policies are applied throughout the Group.
- Comply with our legal requirements, file all appropriate returns on time and make all tax payments by the due date.
- Consider all taxes as part of ongoing decisions.
- Do not enter into artificial tax arrangements nor take an aggressive stance in the interpretation of tax legislation.
- Do not undertake transactions that are outside the Group's low-risk appetite for tax or not in line with the Group's Code of Conduct.
- Engage with HMRC in a proactive and transparent way and discuss our interpretation of tax laws in real time, such interpretations following both the letter and spirit of the laws.
- Do not have any connections with tax havens unless it is necessary for the purposes of trading within those jurisdictions.
- As a long-term business with a long-term approach to financial management, there have been no changes to the tax strategy which is reviewed and reaffirmed on an annual basis.

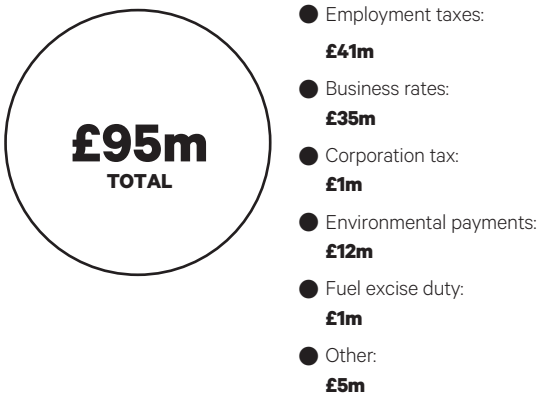
Further details are given in the Group's tax strategy report available on the Pennon Group website **www.pennon-group.co.uk**

Regulatory Capital Value (RCV) (£m)



1. Based on South West Water Limited's group of companies, including Bristol Water plc.
2. Based on South West Water[1] net debt and shadow RCV
3. UK water position as at 31 March 2022 as per published annual performance reports - weighted average

Tax contribution 2022/23 – borne/collected



The Group's total tax contribution (TTC) for 2022/23 amounted to £95 million (excluding £150 million of VAT receipts) (2021/22 £88 million reanalysed to excluded VAT receipts). TTC is a standardised measure of a group's total tax contribution, having been developed by PwC and the 100 Group (FTSE 100 Finance Directors). It is acknowledged as being a fair and comparable representation of total tax cost.

TTC looks at taxes borne, and taxes collected. Taxes borne includes all taxes which are a cost to the Group, such as landfill tax, business rates, corporation tax and employers' National Insurance contributions (NICs). Taxes collected and recovered highlights where the business is collecting tax on behalf of HMRC.

Employment taxes totalled £41 million (2021/22 £37 million) including employees' Pay As You Earn (PAYE) and total NICs. The total amount of £41 million includes PAYE of £4 million (2021/22 £4 million) on pension payments made by the Group pension scheme. A net amount of £30 million (2021/22 £27 million) was collected on behalf of the authorities for employee payroll taxes.

Business rates of £35 million (2021/22 £34 million) were paid to local authorities. This is a direct cost to the Group and reduces profit before tax.

UK Corporation Tax payments to HMRC in the year were £1 million (2021/22 £7 million) in relation to payments due for prior years. There were no payments due in respect of 2022/23 as the Group has generated tax losses in the year.

Payments to the Environment Agency and other regulatory bodies total £17 million (2021/22 £17 million). This reduces profit before tax.

Fuel excise duty of £1 million (2021/22 £1 million) related to transport costs. This reduces profit before tax.

VAT repayments of £150 million due (2021/22 £88 million) have been received to the Group from HMRC. VAT has no material impact on profit and is excluded from the TTC figure to avoid distortions in this.

Contingencies

Ofwat and the Environment Agency announced an industry-wide investigation into sewage treatment works on 18 November 2021. In June 2022, as part of its ongoing investigation, Ofwat announced enforcement action against South West Water Limited, alongside the five companies which received enforcement notices in March 2022.

On 23 May 2023 Ofwat announced an investigation into South West Water's 2021/22 operational performance data relating to leakage and per capita consumption. This operational performance data was reported in South West Water's Annual Performance Report 2021/22.

All company data is subject to extensive process checks, which include both internal and external assurance. All data disclosed in South West Water's Annual Performance Report is subject to checks and balances carried out by South West Water's external technical auditor.

The company continues to work openly and constructively with regulators to comply with the formal notices as part of these ongoing investigations by engaging and providing information as required.

Pensions

At 31 March 2022, the surplus on retirement obligations of £66.3 million comprised a surplus on the Group's principal pension scheme, Pennon Group Pension Scheme (PGPS), of £59.5 million and a surplus of £6.8 million in respect of Bristol Water's defined benefit pension obligations.

The overall surplus at 31 March 2023 has reduced to c.£29 million reflecting the following principal movements:

- £23 million net reduction in surplus from the movement in financial actuarial assumptions with significant reductions in liabilities, from the increasing discount rate, offset by the reduction in asset values, (reflecting market volatility and the greater level of hedging in the schemes).
- £16 million reduction in surplus with the change in other actuarial assumptions reflecting the impact of inflation on immediate term pension increases, and other changes in actuarial assumptions from the March 2022 triennial valuation.

The triennial valuation of PGPS as at 31 March 2022 has been agreed and no deficit recovery payments are required. The valuation recorded an actuarial technical provisions surplus of c.£8 million, representing c.101% funding. The valuation reflects the improvements in the funding of PGPS over recent years supported by the responsible payments made by the Group. The ongoing funding requirements for the Company to the scheme are limited to the continuing administration expenses.

As funding of PGPS has improved the investment portfolio has been de-risked through increasing the scheme's real gilts hedging position through Liability Driven Investments (LDIs), which are commonly used by UK pension schemes. Whilst LDIs remain a critical part of the hedging strategy, further risk management and monitoring strategies have been implemented to help protect against the potential for rapid movements in yields given what was seen in gilt markets last autumn.

Bristol Water's pension surplus relates to the Bristol Water Section of the Water Companies Pension Scheme (WCPS). The liabilities of the scheme are fully insured, securing the pension promises made to the benefit of members through a bulk annuity policy. Changes in actuarial assumptions have little impact on the surplus recognised as the change in liabilities is materially matched by the change in asset values through the bulk annuity policy. As a result the net surplus of c.£7 million remains largely unchanged. The surplus recognised is restricted by a tax deduction of 35% under UK tax legislation.

Dividends

The Group continues to strive to deliver on its commitments to customers, shareholders and stakeholders as our investments drive strong and sustainable results. Around two thirds of Pennon's shareholders are UK pension funds, savings, charities and individuals with almost half of the Group's employees, now including Bristol Water, also being shareholders. Following the second issuance of our unique WaterShare+ initiative, customers now make up more than four times the number of institutional shareholders.

Pennon's sector-leading 2020-2025 dividend policy of growth of CPIH +2% reflects the Board's ongoing confidence in the Group's strategy and is underpinned by continued RORE outperformance in South West Water.

The Board has recommended a final dividend of 29.77 pence per share for the year ended 31 March 2023. Together with the interim dividend of 12.96 pence per share paid on 5 April 2023 this gives a total dividend for the year of 42.73 pence. This represents an increase of 10.9% (March 2023 CPIH + 2%) on 2021/22. Pennon offers shareholders the opportunity to invest their dividend in a Dividend Reinvestment Plan (DRIP).

1. UK water position as at 31 March 2022 – weighted average

The proposed dividends totalling £111.7 million are covered 2.8 times by underlying EBITDA (2021/22 3.8 times). The reduction in EBITDA dividend cover^ was expected given the significant near-term pressures on earnings from elevated power pricing. Pennon Group plc has substantial retained earnings and a sustainable balance sheet to support its stated dividend policy. The strong fundamentals of its principal operating subsidiary, South West Water Limited, underpin this policy with its strong RORE and growing RCV. Dividends are charged against retained earnings in the year in which they are paid.

Investing for sustainable growth – renewable energy generation

In line with both our long-term sustainable growth strategy in UK environmental infrastructure and our desire to accelerate on our Net Zero target by 2030, we have allocated £160 million for investment in renewable energy generation. This strategy will also benefit the Group by reducing our exposure to future volatility in wholesale power markets, that we have experienced this year, and will provide commercial returns ahead of those earned from our regulatory water business.

In May 2023 Pennon Power Limited, a direct subsidiary to Pennon Group plc, acquired a c.40 GWh site in Dunfermline for an expected total acquisition and build cost of around £35 million. This is an attractive ready to build site, with consents in place, and is expected to commence generation in 2024. This site also has capacity for further investment of around £25 million for a 2-hour 60 MW battery storage facility that will support the UK's transition to renewable energy and earn further healthy returns.

In addition, we are in advanced discussions on a further four sites that could provide a further 150 GWh generation, potentially bringing our total generation to c.190 GWh from these projects. This amount equates to around 45% of our electricity usage and would be a big step forward towards our 2030 target of 50% self-generation.

Financial outlook

Looking to 2023/24, there are some signs of inflation stabilisation before it recedes to more normal levels, whilst the global economy continues to be volatile and reactive to a range of ongoing geopolitical dynamics.

We recognise the pressure that inflationary pricing increases pose to our customers, and customer bill affordability continues to remain a key consideration for us. Our broad range of affordability measures ensures we are able to support those in need of support, and we continue to focus on delivering improvements efficiently and effectively.

We expect overall revenues to increase with the combined impact of inflation on our 2023/24 tariffs (net of the year on year impact of regulatory adjustments and ODI penalties) and ongoing expected growth in our non-household retail business.

Whilst wholesale cost levels remain elevated, we anticipate, power costs to remain broadly flat year on year[1] compared to 2022/23 total power costs of c.£103 million (wholesale costs £67 million, non-commodity costs £36 million). We have recognised the pressure sustained high levels of inflation place on our colleagues and pay increases of c.5-7% have been agreed across the Group with a greater allocation towards lower income bands. In other areas the sustained elevated levels of inflation continue to place upward pressure on our input costs. Despite these upward cost pressures we are targeting to maintain total operating costs in South West Water at 2022/23 levels, whilst growth in the retail business outside our region will increase wholesale water costs.

We have reduced the level of volatility on our interest costs by reducing our exposure to index-linked debt with £300 million of RPI swaps to smooth the impact of inflation over the remaining years of K7. Whilst the changes we have made in our financing remain efficient the increased borrowing rates on variable debt and increased debt levels to support our capital investment profile are expected to result in an overall increase in net finance costs.

Overall, these impacts are expected to result in improvements in near-term earnings and, in the longer term, the elevated inflationary environment provides the Group with additional growth in long-term sustainable value, with revenues and RCV linked to November and March outturn inflation, respectively.

Paul Boote
Group Chief Financial Officer

31 May 2023

1. Based on current market pricing and current hedged position of c.75% for 2023/24

Roadford Reservoir in West Devon

Risk management and principal risks

Managing our risks

The Group operates within a complex and evolving risk landscape which includes changing Government policy, multiple regulatory frameworks and increasing customer and wider societal expectations.

The long-term success of the Group is dependent on the effective management of risks and opportunities and remains a key focus for the Pennon Board and Executive. To achieve this, Pennon operates mature risk management and internal control frameworks which are aligned to the Group's strategic priorities and are embedded into our processes, culture and ways of working. These frameworks form a key part of our governance structure ensuring that there is robust review, challenge and assurance over the management of both our current and emerging risks and opportunities.

Pennon risk management framework

The Group's risk management framework encompasses both a 'top-down' and 'bottom-up' approach. This:

- allows risks and opportunities to be cascaded and escalated effectively.
- enables a common understanding of the risks and opportunities and their potential impact on the achievement of the Group's strategic priorities.
- provides a multi-layered approach to the review and challenge of risk.

During the year, as part of the broader integration of Bristol Water and other organisational changes, the Group's risk management framework and associated governance and processes have been further enhanced and standardised across the Group. All members of the Pennon Executive attend the Pennon Executive Risk Committee meetings, reflecting the increasing interconnectedness and complexity of the principal risks facing the Group.

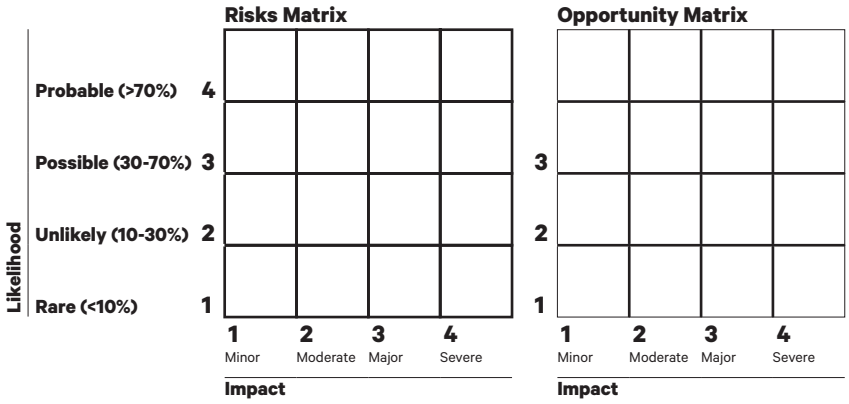
Our risk assessment methodology

A consistent methodology is applied in the assessment of the Group's risks (including climate-related risks) and opportunities, which considers both the likelihood of the risk occurring and the potential impact.

Impact is assessed across the following financial and non-financial categories: financial, safety, environmental, stakeholder and customer impact, reputation, sustainability, and quality. Over the past year the Group has enhanced the impact assessment criteria to better reflect environmental and sustainability considerations, including impacts to the Group's climate, carbon, and nature objectives.

Likelihood is defined as likelihood over the next five years under four categories (probable, possible, unlikely, or rare) with defined probability thresholds.

Risks are assessed on both a 'gross' (without the consideration of existing control measures) and 'net' (with consideration of existing control measures) basis. The impact and likelihood is multiplied and plotted on a 4x4 matrix to determine the overall Red, Amber, Green (RAG) risk rating which is used to prioritise risks and actions.



Key - Financial Impact

Minor	Moderate	Major	Severe
<2%	2% - 5%	5% - 7.5%	>7.5%
PAT	PAT	PAT	PAT

Governance of the risk management and internal control frameworks

The consideration and reporting of risk management and the key responsibilities and activities which encompass the Group's risk management framework are summarised below.

Principal and business-level risks are subject to regular review and challenge by individual functions, the Pennon Executive Risk Committee, the Pennon Executive and the Pennon Board.

The Group mitigates its risk exposure in line with the desired risk appetite and tolerance levels, through the operation of a robust internal control and assurance framework which is aligned to the 'three lines' model.

The Group Executive and the Pennon Board obtain assurance over the effectiveness of the internal control environment across all three lines of defence from a variety of internal and external assurance providers, including an independent Group Internal Audit function.

Oversight

Pennon Board

Key risk management responsibilities
- Sets the Group's strategic objectives.
- Establishes the Group's risk appetite.
- Determines the Group's principal risks.
- Ensures an effective internal control framework.

Key assurance activities
- Quarterly review of the Group's principal risks against the determined risk appetite.
- Quarterly review of the Group's emerging risk log.

Audit Committee

Key risk management responsibilities
- Reviews the effectiveness of the Group's risk management framework.
- Reviews the adequacy of the internal control framework.

Key assurance activities
- Performs quarterly deep-dive reviews on principal risks.
- Approves the Group Internal Audit Plan.
- Receives reports on the outcomes of key assurance activities.

First line

Individual subsidiaries / functions

Key risk management responsibilities
- Identifies and assesses subsidiary / functional-level risks.
- Implements and executes appropriate risk mitigation strategies, aligned with the agreed risk appetite.
- Monitors compliance with internal control framework.
- Review of subsidiary / functional principal risks on a quarterly basis by senior leadership teams.

Key assurance activities
- Functions provide assurance activities across key business processes including regulatory, legal, health & safety.
- Self-certification of compliance with the internal control framework.

Second line

Pennon Executive

Key risk management responsibilities
- Day-to-day management of the Group's principal and operational risks.
- Establishes the relevant Group-wide risk management processes and procedures.
- Maintains the internal control framework.

Key assurance activities
- Performs a thorough appraisal of the Group's principal and emerging risk profile quarterly.
- Monitors the Group's performance against operational and financial metrics.
- Establishes and reviews policies, procedures and delegated authorities

Pennon Executive Risk Committee

Key risk management responsibilities
- Reviews the Group's principal risks and mitigation strategies.
- Provides challenge to individual functions over the management of their business-level risks.
- Considers mitigation plans for High Impact Low Likelihood (HILL) risks.
- Receives functional and departmental updates on business level (bottom-up) risks.
- Performs horizon scanning on emerging risks and opportunities.

Key assurance activities
- Quarterly review of Group principal risks and key subsidiary / functional risks.
- Undertakes deep-dive reviews of specific risks.

Energy Risk Committee

Key risk management responsibilities
- Establishes the Group's approach to energy management and risk exposure in line with the desired risk appetite.

Key assurance activities
- Monitors adherence to agreed strategies and risk positions.

Operational Risk Management

Asset Management

Project Risk Management

Third line

Group Internal Audit

Key risk management responsibilities
- Provides independent, risk-based assurance on the effectiveness of the internal control framework.
- Coordination of independent assurance activities.

Key assurance activities
- Regular reporting to Audit Committee and Pennon Executive on the effectiveness of internal controls and the outcomes of key assurance activities.

Environmental, social and governance risk management

Our purpose and values recognise the broader societal role that the Group plays within the regions and communities it serves. Consequently environmental, social and governance (ESG) considerations are at the heart of the Group's activities and how we operate as a responsible business. The identification, assessment and management of ESG risks and opportunities are integrated into the Group's overall risk management framework and methodology. The delivery of ESG metrics and targets, and the associated risks and opportunities, are monitored thorough the ESG framework by the ESG Committee. Further detail is provided on page 126.

As the owner of a water and wastewater company, the Group acknowledges the fundamental impact that climate change has on the Group's strategy and priorities and is considered to be pervasive across the Group's principal risk profile. The assessment of the individual principal risks, as detailed within the table below, has included the consideration of both physical and transitional climate change impacts, where relevant, and the mitigating actions being taken.

Further detail on the specific physical and transitional climate change risks and opportunities relevant to the Group, along with mitigating actions being taken, are detailed further within TCFD on pages 74 to 95.

South West Water technical (non-financial) data

In addition to the risk management framework detailed above which applies across the Group, recognising the importance of the regulatory ODI framework, South West Water engages independent, third-party auditors to audit the accuracy of the technical (non-financial) data reported within the various annual performance reports and regulatory publications and submissions, including its performance commitments and environmental data. Furthermore, a third party provider, DNV, has also performed additional assurance work over selected sustainability measures.

Continuous improvements to risk management and internal control

The Group is committed to continuously improving its ability to identify and respond to current and emerging risks. Examples of risk management improvements during the year include:

- The creation of a Compliance function overseen by the Group Compliance Director, bringing together key second line compliance activities undertaken across the Group
- A Compliance Committee has been established enhancing the governance over key compliance aspects and returns
- Detailed analysis has been undertaken to inform the Group's capital investment to address long-term water resource and environmental improvement plans as part of the business planning process
- Testing of resilience and response plans has been undertaken covering various scenarios, including power outages and cyber security
- The successful launch of the 'Quality First' initiative as part of the continuous improvement of drinking water production.

Management of South West Water within the Group's risk management framework

Pennon manages its risks in such a way that South West Water, as a regulated company, is protected from risk elsewhere in the Group. The Group's principal risks and uncertainties include those Group-level risks that could materially impact on South West Water.

Pennon's risk management and internal control frameworks ensure that it does not take any action that would cause South West Water to breach its licence obligations. Further, the Group's governance and management structures mean that there is full understanding and consideration of South West Water's duties and obligations under its respective licences, as well as an appropriate level of information sharing and disclosure to give South West Water assurance that it is not exposed as a result of activities elsewhere within the Group.

Horizon scanning

Emerging risks and opportunities are considered to be factors and events which could have a future impact on the achievement of the Group's strategic priorities but lack the required clarity or certainty in order to adequately assess their impact. Horizon scanning of emerging risks and opportunities is embedded within the risk and opportunity review process performed by individual subsidiaries and functions. Emerging risks are reviewed by the Pennon Executive Risk Committee, Pennon Executive and Pennon Board as part of their regular assessment of the Group's risk profile. Notable emerging risks and opportunities are detailed within the table below:

Risk/opportunity

Micro-pollutants, plastics and micro-plastics

Comment	Risk category impact
The continued focus on the impact of micro-pollutants and micro- plastics could present both risks and opportunities arising from changes to water treatment processes.	• Operating performance. • Business systems and capital investment.

Time horizon

Medium-term

Risk/opportunity

Biodiversity

Comment	Risk category impact
Threats to the region's biodiversity, as a result of development, pollution and climate change, may require changes to how we interact with species and habitats in the areas where we operate.	• Operating performance.

Time horizon

Long-term

Risk/opportunity

Changes to the demographics within the South West

Comment	Risk category impact
Increases in population migration to the South West due to the longer-term impact of COVID-19 and climate change could place further demand on our resources and assets.	• Operating performance.

Time horizon

Long-term

Risk/opportunity

Artificial intelligence and machine learning

Comment	Risk category impact
There is a risk that automated intelligence and learning deployed within operational processes develops faster than Government regulations and standards.	• Operating performance.

Time horizon

Long-term

Risk/opportunity

PFAS and forever chemicals

Comment	Risk category impact
Changes in regulatory requirements or the introduction of statutory standards may require significant changes in operational processes in the water treatment process	• Operating performance. • Business systems and capital investment.

Time horizon

Long-term

Risk appetite

The UK Corporate Governance Code requires the Group to determine the risk appetite considered appropriate in achieving the Group's strategic priorities. Striking an appropriate balance between risk and reward is key to the success of the Group's strategy.

The Board has developed risk appetite statements for each risk category and for each principal risk. This allows the business to pursue value-enhancing opportunities, while maintaining an overall level of risk exposure that the Board considers to be appropriate. The Board's evaluation of the comprehensiveness of the Group's internal controls in mitigating its principal risks to an acceptable level is considered with due consideration of the relevant risk appetite. The risk appetite for each risk category is detailed below:

Risk category

Law, regulation and finance

Risk appetite statement

The Board is committed to complying fully with, and being seen to be complying with, all relevant laws, regulations and obligations and has no appetite for non-compliance in this area. This includes (but is not limited to) health and safety where the Board places the highest level of importance on the welfare of our employees, the public and those who work with or on behalf of Pennon. The Group also operates a prudent approach to our financing strategy to ensure our long-term financing commitments are met.

The Board acknowledges, however, that the Group operates in a complex environment influenced by Government and regulatory policy. Consequently, there is acceptance of increased inherent risk in these areas and the Group seeks to mitigate any potential downside and leverage opportunities that may arise from Government policy and regulatory change.

Risk category

Market and economic conditions

Risk appetite statement

The Board recognises that the Group's activities are exposed to changes in macroeconomic and external market conditions. The Group seeks to take well-judged and informed decisions to mitigate these risks where possible but accepts that a level of residual risk may remain beyond the Board's control.

Risk category

Operating performance

Risk appetite statement

The Board has no appetite for significant operational failure of our water and wastewater assets, and seeks to reduce both the likelihood and impact through long-term planning and careful management of our operational assets.

There is greater appetite for well-informed risk taking to develop further markets, subject to this not detrimentally impacting on the level of service expected of our regulators, customers and wider stakeholders.

Risk category

Business systems and capital investment

Risk appetite statement

The Board has a low risk appetite for risk associated with the delivery of capital investment within our regulated business plan. There is greater appetite for broader investment with decisions taken through weighting risks against the expected level of return on a case-by-case basis.

The Group seeks to minimise technology and security risk to the lowest possible level without detrimentally impacting on the Group's operations.

Principal risks and uncertainties

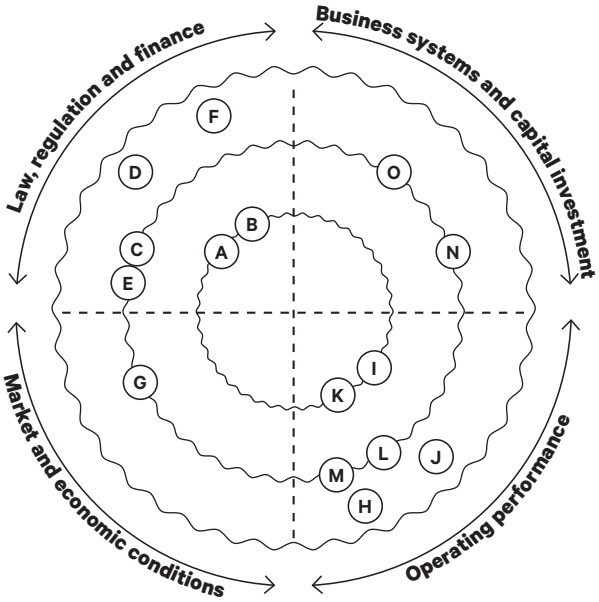
The Group's business model exposes the business to a variety of internal and external risks that are influenced by the potential impact of macro political, economic and environmental factors. Specifically, the macro level events have contributed to the high inflationary environment, and the consequential impact on power prices and interest rates both in the UK and globally has continued to directly and indirectly impact the Group during the year. While the ability of the Group to influence these macro-level risks is limited, they continue to be regularly monitored and the potential implications are considered as part of the ongoing risk assessment process. The Group performs a range of scenario planning and analysis exercises to understand the risk exposure of one, or a number, of these events occurring.

During the year the Board has carried out a detailed review of the of the current and emerging risks in the context of the Group's strategic objectives and priorities as well as the external environment within which it operates. This has resulted in the following changes to the Group's principal risks compared with those previously reported:

- The availability of sufficient water resources has been separated from the broader drinking water principal risk and is now included as a standalone Group principal risk.
- The Group's principal risks reflect the delivery of the Group's 2030 Net Zero commitment in mitigating the impact of climate change.
- The delivery of customer and environmental commitments have been combined to form a standalone principal risk.
- Non-recovery of customer debt has been removed as a principal risk reflecting the Group's robust debt management and customer collections processes. With ongoing cost-of-living challenges for our customers, this continues to be carefully monitored as an operational risk.
- The Bristol Water acquisition principal risk has been removed following clearance from the Competition and Markets Authority and merger of Bristol Water's licence into South West Water.
- Key risks associated with the delivery of regulatory outcomes and performance commitments are reflected within individual principal risks and has therefore been removed as a standalone principal risk.

These principal risks have been considered in preparing the viability statement on page 63.

Overview of Pennon's principal risk profiles



Category	Reference	Strategic priorities	Risk description	Net risk
Law. Regulation and finance	A	**1, 2, 3**	Changes in Government policy	↑
	B	**1, 2, 3**	Regulatory Frameworks	↑
	C	**1, 2, 3**	Non-compliance with laws and regulations	↑
	D	**1, 3**	Inability to secure sufficient finance and funding, within our debt covenants, to meet ongoing commitments	↑
	E	**2, 3**	Non-compliance or occurrence of an avoidable health and safety incident	↓
	F	**3**	Failure to pay all pension obligations as they fall due and increased costs to the Group should the defined benefit pension scheme deficit increase	↔
Market and economic conditions	G	**1, 2, 3**	Macroeconomic near-term risks impacting on inflation, interest rates and power prices	↓
Operating performance	H	**2, 3**	Failure to deliver the Group's 2030 Net Zero Commitment to respond to the impact of climate change	↔
	I	**2, 3**	Availability of sufficient water resources to meet current and future demand	↔
	J	**1, 2, 3**	Failure of operational water treatment assets and processes resulting in an inability to produce or supply clean drinking water	↑
	K	**1, 2, 3**	Failure of operational wastewater assets and processes resulting in an inability to remove and treat wastewater and potential environmental impacts, including pollutions	↔
	L	**2, 3**	Non-delivery of customer service and environmental commitments	↔
	M	**1, 2, 3**	Insufficient skills and resources to meet the current and future business needs and deliver the Group's strategic priorities	↑
Business systems and capital investment	N	**1, 2, 3**	Insufficient capacity and resilience of the supply chain to deliver the Group's operational and capital programmes	↑
	O	**3**	Inadequate technological security results in a breach of the Group's assets, systems and data	↑

Key – Strategic priorities					
1	Growth in environmental infrastructure	High	Increasing	T	Transitional climate change impact
2	Pioneering solutions	Medium	Stable	P	Physical climate change impact
3	Leadership in UK water	Low	Decreasing		

Law regulation and finance

Principal risk	Strategic impact	Net risk
A **Changes in Government policy** Strategic priorities **1, 2, 3** Climate Change Impact: **T**	**Strategic impact** Changes in Government policy and direction may fundamentally impact our ability to deliver the Group's strategic priorities, impacting shareholder value. **Mitigation** There has been continued focus on the performance of the water sector by Government, with its Plan for Water launched in March 2023 following on from its Storm Overflows Discharge Reduction Plan in August 2022. With a General Election due in 2024 this focus is expected to continue. South West Water has been given approval to accelerate c.£125 million of investment to meet these requirements alongside the delivery of its WaterFit strategy that is designed to go further than the Government's Plans. We actively engage and respond to policy consultations and the Group regularly engages with MPs and other political stakeholders, both directly and via Water UK, demonstrating the value from our operational performance, continued investment in our network and wider societal contribution. Horizon scanning of emerging changes in Government policy, including climate change-related policies, is regularly undertaken to monitor and assess the potential direct or indirect impact on the Group. **Appetite** We recognise that Government policy evolves which presents both risks and opportunities. The Group seeks to minimise the potential risks and maximise opportunities through regular engagement and robust scenario planning.	↑
Principal risk	**Strategic impact**	↑
B **Regulatory frameworks** Strategic priorities **1, 2, 3** Climate Change Impact: **T**	Changes to regulatory frameworks may impact on the deliverability and affordability of the Group's priorities, which can impact shareholder value. **Mitigation** Ofwat has published its final methodology for the next Price Review period and investment plans and priorities are well developed, overlaid by a robust governance and assurance framework. South West Water's business plan will be submitted in Autumn 2023. We are actively engaging with regulators through this process but there remains a risk sufficient funding is not provided through the regulatory mechanism to achieve the environmental and climate-related ambitions of the Group, or that the priorities of regions we serve are not recognised by regulators. Established processes exist for monitoring changes in the regulatory environment and responding to regulatory consultations, including via Water UK. **Appetite** We accept that regulatory frameworks evolve which creates both risks and opportunities. We seek to minimise the potential risks by targeting changes which are Net Present Value (NPV) neutral over the longer term to protect customer affordability and shareholder value.	

Our water leak detection dogs, Denzel and Kilo

Law regulation and finance

Principal risk	Strategic impact	Net risk
C **Non-compliance with laws and regulations** Strategic priorities **1, 2, 3** Climate Change Impact: **T, P**	The Group is required to comply with a range of laws and regulations across our businesses. Non-compliance with one or a number of these may result in financial penalties or a negative impact on our ability to operate effectively and reputational damage to the Group. **Mitigation** There remains an increased appetite amongst regulators for pursuing enforcement action for perceived non-compliance with, for example, an industry-wide investigations of wastewater treatment works permit compliance ongoing. The Government is also seeking to amend the maximum amount that water companies can be penalised for damaging the environment. The Group operates within robust and mature frameworks ensuring compliance with permit and other requirements of Ofwat, the Environment Agency and other relevant regulators. These frameworks are regularly reviewed to ensure the Group remains compliant with the increasingly complex legal and regulatory landscape. The Group also maintains a comprehensive internal framework to ensure compliance with corporate laws and regulations, reinforced through key policies endorsed by the Pennon Board and compliance training provided to staff. These frameworks have been further strengthened during the year through the establishment of an executive-led Compliance Committee and Ethics Management Committee, that maintains oversight of the Group's confidential whistleblowing processes, allowing concerns to be raised confidentially and appropriately investigated. **Appetite** The Group maintains the highest standards of compliance and has no appetite for legal or regulatory breaches.	↑
Principal risk	**Strategic impact**	↑
D **Inability to secure sufficient finance and funding, within our debt covenants, to meet ongoing commitments** Strategic priorities **1, 3**	Failure to maintain funding requirements could lead to additional financing costs and put our growth agenda at risk. Breach of covenants could result in the requirement to repay certain debt. **Mitigation** The Group has well-established treasury, funding and cash flow arrangements in place, underpinned by a Treasury Management Policy endorsed by the Board. The Group's financing commitments and cash flow, funding and covenant compliance are regularly reviewed by the Executive and the Board. Whilst the macro-economic environment has increased financing costs, the Group remains comfortably within debt covenant levels with sufficient headroom in place to meet ongoing commitments. The Group retains £420 million of cash and committed facilities as at 31 March 2023 in line with its established pre-funding approach. **Appetite** The Group operates a prudent approach to our financing strategy in order to ensure our funding requirements are fully met.	
Principal risk	**Strategic impact**	↓
E **Non-compliance or occurrence of an avoidable health and safety incident** Strategic priorities **1, 2, 3**	A significant health and safety event could result in financial penalties, significant legal costs and damage to the Group's reputation. **Mitigation** During the year the Group has continued to deliver and embed the 2025 HomeSafe strategy, which has included launching HomeSafe within the Bristol region. Health and safety training, communication and policy updates are provided to all staff and senior leaders regularly visit sites, reinforcing the Group's health and safety culture. Health and safety performance is monitored by the Executive and the respective Board and Executive Health and Safety Committees. There has also been continued investment for safety improvements, focused on operational sites and activities. This has resulted in the Group achieving its lowest ever number of LTIs during the year. **Appetite** The Group has no appetite for health and safety-related incidents and maintains the highest standards of compliance for our staff, contractors and other third parties.	

Key – Strategic priorities

1	Growth in environmental infrastructure	High	Increasing	T	Transitional climate change impact
2	Pioneering solutions	Medium	Stable	P	Physical climate change impact
3	Leadership in UK water	Low	Decreasing		

Law regulation and finance continued

Principal risk

F

Failure to pay all pension obligations as they fall due and increased costs to the Group should the defined benefit pension scheme deficit increase

Strategic priorities

3

Strategic impact

The Group could be called upon to increase funding to reduce the deficit, impacting our cost base.

Mitigation

The Group has in-house pensions expertise supplemented by external specialists, including professional advisors who manage the scheme's investment strategy.

In response to the fall in gilt yields in October 2022, the investment portfolio has been de-risked through increasing the scheme's real gilts hedging position through LDIs (Liability Driven Investments).

As at 31 March 2023 the Group's pension schemes remain in surplus, reflecting the improvements in the funding of PGPS in recent years, and no deficit recovery payments are required following the triennial valuation of PGPS as at 31 March 2022.

Appetite

The Group will ensure that all obligations are met in full but seeks to manage this without unnecessary costs to the Group.

Net risk

Market and economic conditions

Principal risk

G

Macro economic near-term risks impacting on inflation, interest rates and power prices

Strategic priorities

1, 2, 3

Climate Change Impact:

T, P

Strategic impact

Significant changes in inflation, interest rates and power prices could increase the Group's near-term cost base.

Mitigation

The macro-economic volatility experienced during the year has stabilised somewhat with UK power prices and inflation softening and expected to fall further over the next 12 months.

A significant proportion of the Group's power prices have been hedged in line with the agreed strategy set by the Group's Energy Risk Committee. Careful management of the debt portfolio has also enabled c.66% of the Group's net debt to be fixed or swapped.

The Group's in-house procurement function also drives value through competitive tendering of high value contracts.

Long-term protection from the increasing inflationary environment is also provided through regulatory mechanisms with inflation-linked revenues and RCV growth, along with regulatory true-ups.

Appetite

The Group seeks to mitigate the potential impact of macroeconomic events where possible including through inflation-linked revenues and RCV growth, recognising there remains a degree of near-term exposure beyond its control.

Operating performance

Principal risk

H

Failure to deliver the Group's 2030 Net Zero commitment to respond to the impact of climate change

Strategic priorities

2, 3

Climate Change Impact:

T

Strategic impact

Failure successfully to transition to Net Zero may result in an adverse environmental impact, increased costs and reputational damage.

Mitigation

The Group remains on track to deliver its commitments within the 2030 Net Zero strategy which is overseen by an executive led Net Zero Committee.

During the year we have continued to support carbon capture through peatland restoration, increased the deployment of electric vehicles and progressed towards our target of 50% energy self-generation through discussions with counterparties offering large-scale solar development opportunities.

The Group's capital allocation of £160 million has started to be deployed which will accelerate our journey to Net Zero.

Appetite

The Group is committed to achieving Net Zero whilst recognising that this needs to be balanced against the need to deliver other priorities for our customers and the environment.

Operating performance continued

Principal risk	Strategic impact	Net risk
I **Availability of sufficient water resources to meet current and future demand** Strategic priorities **2, 3** Climate Change Impact: **T, P**	An inability to ensure the necessary water resources exist to meet demand may lead to impacts for our customers, increased operational costs and reputational damage. **Mitigation** The drought of 2022 had a significant impact on river flows, groundwater levels and reservoir stocks in our regions. Climate change is expected to result in hotter, drier summers becoming more frequent and greater demand through increased population within the South West. During the year the Group has enacted its Drought Management Plan, alongside extensive engagement and collaboration with regulators and innovative initiatives – such as the Stop the Drop campaign – to minimise the impact of the dry weather on both customers and the environment. Additionally, there has been continued focus on leakage reduction and the launch of region-wide customer communication campaigns. Despite the action taken, storage levels remain below their historical levels heading into Summer 2023. Further action is being taken including exploring desalination in Cornwall as well as more water storage options and increasing the ability to move water around our network. **Appetite** The Group is committed to ensuring there are sufficient water resources through careful management of both supply and demand activities.	
Principal risk	**Strategic impact**	
J **Failure of operational water treatment assets and processes resulting in an inability to produce or supply clean drinking water** Strategic priorities **1, 2, 3** Climate Change Impact: **T, P**	An inability to produce or supply clean drinking water could result in financial penalties, regulatory enforcement and damage to the Group's reputation. **Mitigation** Our drinking water assets and processes have remained resilient despite challenging conditions during the drought and the freeze / thaw conditions that occurred in 2022. Where such events do occur, these are managed through established incident management procedures and utilisation of the Group's supply chain partners. Asset health is managed through a well-established programme of routine planned and preventative maintenance works with asset and network performance monitored by the 24/7 Control Centre. Additionally, our 'Quality First' initiative was also launched during the year and is a cultural and training programme reinforcing the continuous improvement approach adopted by our Drinking Water operational teams. **Appetite** The Group operates a low tolerance for significant operational failure of its water treatment assets or quality of water produced and seeks to mitigate these risks where possible.	

University of the 3rd Age on a tour of Launceston Sewage Treatment Works, Cornwall

Key – Strategic priorities

1	Growth in environmental infrastructure	High	Increasing	T	Transitional climate change impact
2	Pioneering solutions	Medium	Stable	P	Physical climate change impact
3	Leadership in UK water	Low	Decreasing		

Operating performance continued

Principal risk

K

Failure of operational wastewater assets and processes, resulting in an inability to remove and treat wastewater and potential environmental impacts including pollutions

Strategic priorities

1, 2, 3

Climate Change Impact:

T, P

Strategic impact

An inability to remove or treat wastewater could result in adverse environment impacts, financial penalties, regulatory enforcement and damage to the Group's reputation.

Mitigation

Minimising the impact of our activities on the environment remains a strategic priority for the Pennon Board and Executive.

Delivery of the Group's WaterFit strategy and Pollution Incident Reduction Plan continues as the Group drives for a step change in environmental performance, which includes enhanced processes, targeted capital investment and proactive asset maintenance.

These strategies have contributed to a further decrease in the number of pollution events and our best ever performance during 2022/23, 100% of our bathing waters met the high standards for water quality and a c.30% year-on-year reduction in the average number of storm overflow spills.

During the year WaterFit Live has been launched providing the public with information on where bathing waters may be affected by the operation of our overflows as well as information on future investment.

Despite this progress it is recognised there is more work to do to deliver a step change in our environmental performance and this will continue to remain an area of strategic focus in both the current and next regulatory period.

Appetite

The Group operates a low tolerance for significant operational failure of its wastewater processes and assets and maintains the highest level of environmental standards.

Net risk

Principal risk

L

Non-delivery of customer service and environmental commitments

Strategic priorities

2, 3

Climate Change Impact:

T, P

Strategic impact

Failure to deliver our customer and environmental commitments may result in reputational damage, and financial penalties impacting on shareholder value.

Mitigation

The Group continues to enhance and invest in its customer services teams, expanding the channels by which it can interact with and support household and business customers.

The Group offers a range of schemes and tariffs to support customers with affordability challenges and South West Water is BSI18477 accredited, a dedicated standard for identifying and responding to customer vulnerability.

The Group also has a number of initiatives which support the communities that we service.

It is recognised that further work is required to improve both South West Water and Bristol Water's regulatory customer service metrics. Pennon Water Services continues to maintain high customer satisfaction scores, including a rating of 4.8 out of 5 on Trustpilot.

The Group's environmental commitments are measured through 39 metrics with performance reported on the Group's website. The delivery of the WaterFit strategy, is key to this and progress remains on track. See page 25 for further details.

Appetite

The Group continually seeks to deliver high levels of customer service with performance in the upper quartile for the Water sector.

Operating performance continued

Principal risk	Strategic impact	Net risk
M **Insufficient skills and resources to meet the current and future business needs and deliver the Group's strategic priorities** Strategic priorities **1, 2, 3** Climate Change Impact: **T**	Failure to have a workforce of skilled and motivated individuals will detrimentally impact all of our strategic priorities. We need the right people in the right places to innovate, share best practice, deliver synergies and move the Group forward. **Mitigation** There remains high demand nationally for the skills and expertise utilised within the Group. The Group's People Strategy enables the Group to attract, retain and develop our employees as well as recognising the significant contribution that our people make. The Group's RISE employee engagement forum provides a platform for our people to provide feedback, raise their priorities and promote ideas. Additionally, we have continued to develop a diverse and inclusive talent pipeline and have updated long-term commitments, with enhanced recruitment targets for graduates and apprentices through to 2030 and continued prioritisation of our diversity and inclusion agenda. Furthermore, the acquisition of Bristol Water has enabled the best talent from across the business to come together. The Group's senior leadership has also been further strengthened during the year with a number of key Executive appointments, as described on pages 105 and 106. **Appetite** While turnover of employees does occur, we ensure the appropriate skills and experience are in place with succession plans providing adequate resilience.	↑

Business systems and capital investment

Principal risk	Strategic impact	
N **Insufficient capacity and resilience of the supply chain to deliver the Group's operational and capital programmes** Strategic priorities **1, 2, 3** Climate Change Impact: **T, P**	The inability of our supply chain to support in the delivery of our operational and capital programmes may result in increased costs and delays, detrimentally impacting our ability to achieve our change and growth agenda. **Mitigation** The Group engages with a range of partners to support in the delivery of operational and capital programmes. The demand for these skills and expertise continues to increase, particularly across the Water Industry to deliver programmes in the current regulatory period and to prepare for future investment programmes during 2025-30. We are underway with a full tender for Tier 1 contractors to support our current, accelerated investments and to be in place for the next regulatory period. We anticipate awarding more Tier 1 contractors than in our current framework to support elevated investment levels. Supplier events have been held to expand the number of partners we work with and to utilise the expertise that exists within the regions we serve. The Group also uses its in-house procurement expertise to help source and drive value within the purchasing process. The Group regularly monitors the financial health of key partners and we work in partnership with our supply chain to identify and manage potential issues and challenges. Where action is required there are established plans and alternative arrangements which provide mitigation and early intervention. **Appetite** The Board has a low appetite for risk associated with the delivery of key operational and capital programmes within our regulated business plan.	↑
Principal risk	**Strategic impact**	
O **Inadequate technological security results in a breach of the Group's assets, systems and data** Strategic priorities **3**	Failure of our technology security, due to inadequate internal processes or external cyber threats, could result in the business being unable to operate effectively and the corruption or loss of data. This could have a detrimental impact on our customers and result in financial penalties and reputational damage to the Group. **Mitigation** External threats are increasing in complexity and sophistication and continue to be carefully monitored by the Group's information security teams. The Group maintains a strong preventive and detective information security framework, aligned to guidance issued by the National Cyber Security Centre with regular awareness training provided to staff. South West Water continues to hold the ISO27001 accreditation. As part of the Group's planning, cyber response exercises have taken place during the year featuring members of the Executive. Broader disaster recovery plans are also in place for both corporate and operational technology and are subject to regular review. The Group's water businesses continue to progress actions as part of the roadmap to meet the requirements of the Network and Information Systems (NIS) Directive, with activities aligned to the priorities identified by the Drinking Water Inspectorate. **Appetite** The Group seeks to minimise technology and security risk to the lowest possible level without detrimentally impacting on the Group's operations.	↔

Viability statement

The Directors of Pennon Group plc are responsible for ensuring the long-term viability of the Group. The Directors need to ensure the resilience of the Company by identifying, managing, avoiding or mitigating risks which may impact viability.

The Board's consideration of the longer-term viability of the Group is an extension of the Group's strategic business planning, which is managed through regular long-term modelling and monitoring of key measures including gearing, debt covenant headroom and level of liquidity. The resilience of the business and these key viability measures are appropriately assessed by a number of mechanisms including a robust risk management assessment, sensitivity analysis and stress tests of financial performance.

The overall market context is a cornerstone of the viability assessment. The Group's main operating subsidiary of South West Water now accounts for the vast majority of the Group's earnings, being a long-term business characterised by multi-year investment programmes, with associated revenue streams with high levels of future visibility.

The viability assessment has been made with reference to the Group's current position and prospects, including consideration of the ongoing impacts of the Ukraine crisis, climate change, its longer-term strategy, the Board's risk appetite and the Group's principal risks and how these are managed, as detailed on pages 52 to 62 of the risk report.

Period of assessment

The Board regularly considers the appropriate period for the viability assessment to be performed in line with the UK Corporate Governance Code. The Board considers the appropriate period to assess the Group's viability remains unchanged at five years, which recognises both the longer-term visibility in the regulatory environment of the South West Water business and the corporate activity, including acquisitions and other non-regulated investments undertaken by Pennon.

Risks

The Board considers the preventative and risk management actions in place and the potential impact of the principal risks (as detailed on pages 52 to 62) against our ability to deliver the business plan. This assessment has considered the potential impact of these and other risks arising on the business model, future performance, solvency and liquidity over the period in question. The Group has a strong liquidity and funding position with £420 million of cash and committed facilities as at 31 March 2023 and net assets of £1,119.3 million. The Group has a mixture of fixed, floating and index-linked debt financing with a weighted average maturity of 13 years. In making their assessment, the Directors reviewed the principal risks and considered which risks might threaten the Group's viability. Over the course of the year, the Board, either directly or through the activities of the Audit Committee, has considered a deep-dive review of the following principal risks to enable a thorough assessment of the impact of these risks on ongoing viability.

- Cyber security.
- Non-collection of debt.
- Insufficient finance and funding.
- PR24.
- Power outage.

Stress testing

The Group's business plan has been stress-tested. Whilst the Group's risk management processes seek to mitigate the impact of principal risks as set out on pages 52 to 62, individual sensitivities (shown in the table below) have been identified. These sensitivities, which are ascribed a value with reference to risk weighting, factoring in the likelihood of occurrence and financial impact, were applied to the baseline financial forecast which uses the Group's annual budget for FY 2023/24 and longer-term strategic business plan through to March 2028.

The impact of climate risks have been assessed in detail as set out in the Task Force on Climate-related Financial Disclosures (TCFD) section on pages 74 to 87. The Group's strategic business plan includes the expected investment identified at this stage to meet climate-change adaptation. The stress-testing scenarios applied during the viability assessment period do not include specific reference to climate-change related risks alone as climate change has been considered as part of the Principal risks identified. Beyond the period of assessment, additional impacts from climate change are considered in more detail within the TCFD section along with mitigating actions.

Principal risk	Viability sensitivities tested
A: Changes in Government policy	Changes in Government policy affecting the water industry, such as additional environmental legislation may impact operational performance or investment requirements. The estimated average adverse impact on the Group's cash flows from a range of potential policy changes has been applied as a sensitivity.
B: Regulatory reform	Potential changes in PR24 price review may impact allowed regulatory returns in South West Water. The estimated average adverse impact on the Group's cash flows from a range of potential policy changes has been applied as a sensitivity.
C: Non-compliance with laws and regulations	The estimated impact of financial penalties and reputational damage from failure to comply with laws and regulations has been modelled as a sensitivity.
D: Inability to secure sufficient finance and funding to meet ongoing commitments	The impact of reduced availability of financing resulting in increased costs has been modelled as a sensitivity.
E: Non-compliance or occurrence of an avoidable health and safety event	The financial impact and cash outflows related to a major health and safety event has been applied as a sensitivity.
F: Failure to pay all pension obligations as they fall due and increased costs for the Group should the defined benefit pension scheme deficit increase	The financial impact on the Group's gearing from additional funding being required to support the Group's defined benefit pension schemes has been applied as an adverse scenario.

Principal risk	Viability sensitivities tested
G: Macroeconomic risks impacting on inflation, interest rates and power prices	The adverse impact of higher operating and finance costs from increasing power prices and general inflation increases over and above increases assumed in base financial plans, including the impact on Totex underperformance on regulatory returns and impact on debt financing costs have been applied as a sensitivity, as well as a reduction in the collection of customer debt from adverse economic conditions.
H: Failure to deliver the Group's 2030 Net Zero commitments in response to the impact of climate change	The adverse impact of the failure to transition towards Net Zero in a timely manner could lead to increased costs; these have been applied as a sensitivity.
I: Availability of sufficient water resources to meet current and future demand	The cost of sourcing water from outside the South West Water catchment area to ensure availability of supply has been included as an adverse scenario.
J: Failure of operational water treatment assets and processes resulting in an inability to produce and supply clean drinking water	The adverse impact from non-delivery of regulatory performance targets which result in ODI penalties, other financial penalties and required additional investment reducing Group revenues and cash inflows have been applied as a sensitivity to the base plan.
K: Failure of operational wastewater assets and processes resulting in an inability to remove and treat wastewater and potential adverse environmental impacts, including pollutions	
L: Non-delivery of customer service and environmental commitments	
M: Insufficient skills and resources to meet the current and future business needs and deliver the Group's strategic priorities	
N: Insufficient capacity and resilience of the supply chain to deliver the Group's operational and capital programmes	
O: Inadequate technological security results in a breach of the Group's assets, systems and data	The adverse financial impacts of a cyber attack resulting in operational disruption, potential loss of data, potential detrimental impacts on customers with potential for financial penalties have been included in the sensitivity analysis.
A combined stress-testing scenario has been performed to assess the overall impact of these individual scenarios impacting the Group collectively. The combined weighted impact of the risks occurring is c.£120 million: this value is considered equivalent to an extreme one-off event that could occur within a year, though the probability of such an event happening is deemed unlikely.	

Stress-testing evaluation and mitigations

Through this testing, it has been determined that none of the individual principal risks would in isolation, or in aggregate, compromise the Group's viability over the five-year period. The assessment has been considered by reviewing the impact on the solvency position as well as debt and interest covenants. The financial impacts of the risks were probability weighted to obtain a value that was used in the stress testing. While mitigations were not required in any of the above individual or combined scenarios to ensure that the Group was viable, additional mitigations could be deployed to reduce gearing and increase covenant headroom. These include:

- Reduction in discretionary operational expenditure
- Deferral of capital expenditure and/or cancellation of non-essential capital expenditure
- Reduction in the amount of dividend payable
- Raising additional funding.

The Group has confidence in its ability to raise additional funding if required should it be required to ensure the Group maintains solvency.

In addition, a reverse-engineered scenario that could possibly compromise the Group's viability over the five-year assessment period has been modelled. This scenario builds on the factors above and additionally assumes all the Group's principal risks incurring in any given year across the viability period, with no probability weightings attached. The Board considered the likelihood of this scenario on the Group's viability over the five-year viability period as remote, concluding the Group could remain viable. Mitigations, as noted above, could also be deployed over the period if deemed necessary.

In making its assessment of the Group's viability, the Directors have taken account of the Group's strong capital solvency position, the Group's latest assessments of forward power and other commodity prices, latest inflation forecasts, its ability to raise new finance and a key potential mitigating action of restricting any non-contractual payments. In assessing the prospects of the Group, the Directors note that, as the Group operates in a regulated industry which potentially can be subject to non-market influences, such assessment is subject to uncertainty, the level of which depends on the proximity of the time horizon. Accordingly, the future outcomes cannot be guaranteed or predicted with certainty. As set out in the Audit Committee's report on pages 120 to 125, the Directors reviewed and discussed the process undertaken by management, and also reviewed the results of the stress testing performed.

Viability assessment conclusion

The Board has assessed the Group's financial viability and confirms that it has a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over a five-year period, the period considered to be appropriate by the Board in connection with the UK Corporate Governance Code.

Our integrated approach to ESG

Our approach to ESG ensures everything we do supports our commitment to provide environmental stewardship and to support our customers and local communities. As a responsible employer, we remain focused on employee development alongside a robust health, safety and wellbeing programme. Our activities are underpinned by a strong governance framework that upholds our core values within the organisation and throughout our supply chain.

ESG Capitals

Creating value through our ESG approach

Everything we do links to a capital in some way – the development of our capitals framework is integral to better decision making for the future.

Our Natural Capital – Environment

- Freshwater
- Land (including soils)
- Species
- Ecological communities
- Coasts
- Atmosphere
- Waste

Our Social & Human Capital – Social

- Colleagues
- Customers
- Communities

Our Manufactured, Intellectual & Financial Capital – Governance

- Supply chain
- Responsible business
- Stakeholders and partnerships
- Finance

Our ESG capitals progress

We are on track with our plans to develop appropriate measures, benchmarking our approach and identifying tools and methodologies to help us value these metrics in line with our materiality assessment, keeping close alignment with our Net Zero and Green Recovery ambitions.

External benchmarking

Our ESG strategy and capitals framework has driven positive change in the business as we continue to embed sustainability in everything we do.

During the year, we continued to show strong performance across external ESG ratings, demonstrating our commitment and management of risk across the ESG agenda.

Latest external assessment scores

13.8
ESG Risk
(Previous rating: 16.5)

80
ESG Rating
(Previous rating: 78)

AA
MSCI ESG Indexes
(Previous rating: AA)

B
CDP Climate Change
(Previous rating: B)

C
CDP Water security
(Previous rating: B)

S&P Global Corporate Sustainability Assessment (CSA)
60/100
(Previous rating: 59/100)

3.9/5
(Previous rating: 3.5/5)

B
ISS corporate rating
(Previous rating: B)

A
GRESB Infrastructure Public Disclosure
(Previous rating: B)

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ESG performance and targets

Materiality assessment

We undertook a detailed materiality assessment with our stakeholders in 2021/22 to inform our strategy and ESG targets to 2025. Findings were published in our 2022 Annual Report. Further stakeholder engagement took place in December 2022 to inform our 2050 Strategic Direction report https://www.southwestwater.co.uk/about-us/documents/business-plan-2020-2025/. This feedback alongside assessment of business and external risks has been used to reappraise our material issues which broadly confirmed we are focused on the right issues. However importance of certain issues has evolved, a summary of the high priority issues is given below.

UN Sustainable Development Goals (SDGs)

We actively engage with the UN SDGs to inform our approach and better understand our impact. We have mapped which of the UN SDGs our ESG targets most directly support. Our primary contribution is to SDG 6: Clean water and sanitation. Read more on our ESG targets on page 87 and 88 and to read more on our contribution towards the SDGs, visit our website www.pennon-group.co.uk/sustainability

Highest Importance to all Stakeholders	What it means to all stakeholders
Net Zero	Taking action to mitigate our own emissions
Freshwater stewardship	Taking care of precious water resources
Water quality – river and coastal	Taking action to deliver a step change in both river and coastal water quality
Climate resilience	Our preparedness for climate change
Drinking water quality	The provision of clean, safe drinking water
Amenity and recreation	Access to high standard bathing water across our region's coasts and inland waters
Trust and transparency	Being open and transparent in a time of increased water sector scrutiny

Key: ● Achieved ◕ Not Achieved

Material issue and associated target	Annual performance against target	2022/23 target	2025 target	SDG
Net Zero				
% energy usage from renewable generation	◕	7%	13%	
Reducing greenhouse gas emissions	●	65%	70%	
Freshwater stewardship				
Reduce water use within our operational sites	●	5Ml	10Ml	
Biodiversity				
Trees planting (cumulative)	●	180,000	250,000	

Material issue and associated target	Annual performance against target	2022/23 target	2025 target	SDG
Customer and community engagement				
Increase our community investment by 10% each year	●	10%	30%	
Diversity and skills				
% Female representation	●	31%	33%	
Increase REACH recruitment (excluding Bristol Water)	●	5%	10%	
Achieve 5% club status	●	Gold Accreditation	Gold Accreditation	
Health, safety and wellbeing				
Number of LTIs across the group	◕	22	11	
Great Place to Work accreditation	●	Maintain	Maintain	

Measure/issue and associated target	Annual performance against target	2022/23 Target	2025 target	SDG
Trust and transparency				
ESG Rating (Sustainalytics)	●	>75	80	
Fair Tax Mark accreditation	●	Maintain	Maintain	
% of active institutional investors met or offered to meet	●	68%	75%	
Sustainable finance				
New funding raised through Sustainable Financing Framework %	●	60%	75%	
Supply chain				
Supplier payment days (average)	●	40 days (Group)	30 days (Group)	
% of key and strategic suppliers that have established an ESG policy or equivalent	●	50%	100%	

Sustainability reporting

Streamlined energy and carbon report (SECR)

Pennon Group plc GHG emissions

	2022/23		2021/22	
	market-based	**location-based**	market-based	location-based
Scope 1 GHG emissions by source (tCO_2e)[1]				
Direct emissions from burning of fossil fuels (tCO_2e)	**8,003**	**8,003**	4,962	4,962
Process and fugitive emissions (tCO_2e)	**15,389**	**15,389**	14,388	14,388
Transport: Company owned or leased vehicles(tCO_2e)	**5,381**	**5,381**	5,052	5,052
Total Scope 1 GHG emissions (tCO_2e)	**28,773**	**28,773**	24,403	24,403
Scope 2 GHG emissions (tCO_2e)	**31,321**	**77,217**	80,279	80,847
Total gross Scope 1 & 2 GHG emissions (tCO_2e)	**60,094**	**105,990**	104,682	105,249
Scope 3 GHG emissions[2] (tCO_2e)	**230,737**	**230,737**	292,698	292,698
Total gross Scope 1, 2 & 3 GHG emissions (tCO_2e)	**290,831**	**336,727**	397,380	397,947
GHG emissions removals through purchases of Renewable Energy Guarantees of Origin (tCO_2e)	**Included in scope 2 above**	**–**	Included in Scope 2 above	–
GHG emissions saved by exporting self-generated electricity (tCO_2e)	**0**	**0**	(1,428)	(1,494)
Total annual net GHG emissions (tCO_2e)	**290,831**	**336,727**	395,952	396,454
Energy consumption used to calculate Scope 1 and 2 GHG emissions (MWh) (see Energy usage section) [4]	**461,716**	**461,716**	426,429	426,429
GHG emissions intensity measure: (tCO_2e) (gross Scope 1+2/£100,000 revenue)[3]	**7.3**	**12.9**	13.2	13.3
Biogenic GHG emissions outside of Scopes (tCO_2e)	**3,148**	**3,148**	2,521	2,521

Notes:

Group total Scope 1 (28,773 tCO_2e) and Scope 2 market-based (31,321 tCO_2e) and Scope 2 location-based (77,217 tCO_2e) GHG emissions. These figures have been independently assured by DNV.

Scope 1 (direct GHG emissions): GHG emissions activities owned or controlled by our organisation that release emissions straight into the atmosphere. For Pennon, primary Scope 1 GHG emission sources during 2022/23 include GHG emissions from stationary plant, fugitive emissions from air conditioning plant and wastewater treatment and transport related GHG emissions from our own vehicles and fleet Scope 2 (indirect GHG emissions) GHG emissions released into the atmosphere associated with our consumption of imported electricity. Scope 3 (other GHG indirect emissions) GHG emissions that are a consequence of our actions, which occur at sources which we do not own or control.

1. GHG emission figures are expressed in tonnes of carbon dioxide equivalents (tCO_2e) whereby emissions of carbon dioxide (CO_2), methane (CH_4), nitrous oxide (N_2O), the fluorinated gases (HFC, PFC, SF6) are shown in terms of the equivalent emissions from CO_2. A breakdown of emissions by GHG is available in our ESG databook available on our website.
2. Estimated GHG emissions for relevant Scope 3 categories calculated in 2022/23 are provided in our ESG Databook available on our website www.pennon-group.co.uk/reportandpresentations.
3. Based on relevant Group revenue for 2022/23.
4. Renewable Energy Guarantees of Origin (REGOs) have been allocated for electricity consumption to March 2023. REGOs for April 2022 to March 2023 are to be allocated in October 2023.

Fernworthy Reservoir, Devon

Operational Pennon Group plc GHG emissions by business

	South West Water	Bristol Water	Group Total*
Scope 1 GHG emissions	23,317	5,310	28,773
Scope 2 GHG emissions (market based)	48	31,273	31,321
Total gross scope 1 & scope 2 GHG emissions (tCO_2e)	23,364	36,583	60,094
Operational intensity measure ($kgCO_2e$/Ml) – water	59.72	358.51	n/a
Operational intensity measure ($kgCO_2e$/Ml) – wastewater	128.45	n/a	n/a

Note:

The water business figure provided here includes the impact of emissions from our two hydroelectric power stations. This does not form part of our annual reporting to the water regulator Ofwat since these sites are outside of the Ofwat regulated contract.

For 'Water' measure Ml = measured water into supply. For 'Wastewater' measure Ml = full measured flow treatment.

*Group total includes 146 tCO_2e from Pennon Water Services and Group shared services.

Change in GHG emissions

Operational Scope 2 market-based GHG emissions for the Group decreased by 65.7% from 2021/22 as a result of South West Water's purchase of REGO backed electricity. Our generation of renewable electricity also contributed to reducing our Scope 2 location-based emissions.

The revenue-based intensity metric has reduced for the Group both with and without Bristol Water and now stands at 12.9 tCO_2e/£100,000 turnover. This shows that emissions have decreased relative to the revenue earned.

Scope 3 GHG emissions

Scope 3 categories were evaluated for relevant categories in line with the reporting guidance. The assessment, carried out by carbon consultants EcoAct on behalf of Pennon, is based on 2022/23 activity data for the Group.

The estimated Scope 3 GHG emissions for 2022/23 for the Group are 230,737 tCO_2e compared to the equivalent figure in 2021/22 of 284,147 tCO_2e. Bristol Water's Scope 3 activities have been calculated and reported within the Group figures for the first time. The change in reported emissions is due to better interrogation of the spend data used to drive Category 1 purchased goods and services calculation. This analysis showed that some financial spend lines were wholly down to financial transactions with zero emissions associated and therefore these activities were excluded from 2022/23 calculations.

A breakdown of our estimated Scope 3 GHG emissions is provided in our ESG Databook, published on our website (www.pennon-group.co.uk/sustainability).

GHG Reporting Methodology

Our approach follows the UK Government's Environmental Reporting Guidelines, including Streamlined Energy and Carbon Reporting guidance (2019) and the Greenhouse Gas Protocol Corporate Standard including the Scope 3 Calculation Guidance (collectively referred to here as the reporting guidelines). In calculating our emissions, we have used the 2022 UK Government conversion factors for GHG reporting and considered the Department for Environment, Food & Rural Affairs' (Defra) 2009 GHG reporting guidance.

Organisational boundary and scopes

The GHG emissions listed here cover 100% of the Group's companies, each of which uses the financial control approach to report GHG emissions. We report our Scope 1, 2 and 3 GHG emissions where relevant. A breakdown of Scope 3 GHG emissions categories is provided in our supplementary ESG Databook online at www.pennon-group.co.uk/reportsandpresentations.

Market and location-based methodology

We report both market-based and location-based Scope 2 GHG emissions. Where our supply is backed by Renewable Energy Guarantees of Origin (REGOs), this qualifies as zero carbon market-based emissions. Where supply is not REGO backed, in accordance with the reporting guidelines, we have used our electricity suppliers' specific published Fuel Mix Disclosure emissions factors to report our Scope 2 market-based emissions. Where Fuel Mix Disclosure emissions factors are not available, we have used the residual grid mix emissions factor.

Self-generated renewable energy export

In accordance with the reporting guidelines, we may report an emissions reduction in our reported net CO_2e figure for any renewable electricity we have generated and exported to the national grid or a third party.

External assurance statement

Group Scope 1 and 2 GHG emissions and energy use, together with selected Scope 3 GHG emissions, have been independently assured by DNV. The assumptions, methods and procedures that are followed in the development of the reported data have been tested and the data audited for accuracy and consistency. Assurance statements can be found at www.pennon-group.co.uk/sustainability.

Offshore Emissions

All of Pennon Group's energy usage is within the UK and Pennon Group had no offshore GHG emissions or energy usage in the reporting period.

Energy usage

Including self-supplied energy, the Group used 485,823 MWh of energy in 2022/23, compared to 448,914 MWh in 2021/22. A breakdown of Group energy usage and associated data assessment methodologies is shown below. Further details and previous years' data are provided in our ESG Databook.

Energy usage

	2022/23[1] (MWh)	2021/22 Group (MWh)	Methodology
Imported grid electricity#	399,301	378,880	Metered data except some NHHM supply which is estimated by electricity supplier (see note[2])
Imported private wire electricity (renewable)	4,819	4,874	Metered data
Self-supplied renewable electricity	12,079	11,859	Metered data
Self-supplied heat	7,141	5,780	Estimated that 60% of heat generated by sewage gas CHP is beneficially used, the rest (40%) is released to atmosphere
Natural gas#	23,471	17,787	Metered data – from billing (some element of estimates)
Liquid fuels (for stationary applications)#	14,904	6,798	Estimated based on fuel use/spend data. Reported totals calculated based on raw data provided by the supplier
Energy used by fleet transport#	24,107	22,963	Estimated based on fuel use/spend and mileage data (see note[2])
Total energy usage	485,823	448,914	
Intensity measure: MWh/£100,000 revenue[3]	58.97	56.66	

Energy usage data notes:

1. Total energy usage (MWh) (485,823 MWh) by has been independently assured by DNV.
2. Hire car fuel usage and grey fleet (use of private vehicles on company business) are included in these SECR volumes – as per SECR guidance.
3. Based on relevant Group revenue for 2022/23.

Energy consumption used to calculate Scope 1 and 2 GHG emissions.

Energy efficiency action taken

A key pillar of our Net Zero plan is Sustainable Living, which targets energy and carbon reduction through changes to operational practices, and increasing energy efficiency. Some of our planned energy efficiency projects during the early part of 2022/23 were disrupted by essential drought measures as some of the most energy intensive rotating assets were and are critical to ensuring water supply. Equally challenging was the impact and delay observed in the international supply chain including lack of raw materials, especially steel.

In spite of these headwinds, some major refurbishments were conducted during the year with notable energy efficacy projects completed in the year including major pump refurbishments at Littlehempston, Restormel, and Roadford. The clean water pumping program has reduced energy consumption by around 990 MWh since October, this will increase as analysis from other sites are completed.

We've continued our meter replacement programme which continues to help identify areas for further efficiency improvements and alter us to aging assets. Permanent efficiency monitoring equipment has been installed across all 64 sites in the clean water pumping program. Building on this programme's success similar projects are being proposed for waste pumping and aeration. Across our offices, we've implemented a number of smaller energy efficiency projects including LED lighting at our Exewater workshop with an aim to expand our office energy efficiency projects over the coming year as part of our Net Zero plan.

South West Water retained its ISO 50001 energy management system accreditation. We are looking to expand the certification to cover Bristol Water sites as part of our integration plans.

The River Dart, part of our river bathing water quality pilot, Devon

SASB Pennon 2022/23 Disclosure

For the second year, we have aligned our non-financial disclosures to the Sustainability Accounting Standards Board (SASB) reporting framework. SASB provides a set of industry specific standards (Water Utilities and Services industry), which each contain topics which are material to our investors. These topics contain a number of metrics we disclose against. SASB metrics now include the full Group including Bristol Water for the first time however some metrics related to regulated figures which are currently reported separately within the South West Water and Bristol Water Annual Performance Reports (APR) respectively. The latest APR's were published in July 2023.

Metric	Code	Pennon Disclosure
Energy Management		
(1) Total energy consumed (2) percentage grid electricity (3) percentage renewable	IF-WU-130a.1	Pennon Annual Report, SECR, Energy Usage, page 69
Drinking Water Quality		
Number of: (1) acute health-based (2) non-acute health-based (3) non-health-based drinking water violations	IF-WU-250a.1	**Pennon Annual Report** Clean, safe and reliable water, (CRI Score), page 17 Taste, smell and colour contacts, page 17
Discussion of strategies to manage drinking water contaminants of emerging concern	IF-WU-250a.2	For more information about our specific strategies such as the Upstream Thinking Project, please refer to: Upstream Thinking – available at: https://www.southwestwater.co.uk/environment/working-in-the-environment/upstream-thinking/the-project/ For more information about Bristol Water's catchment sensitive farming partnership to improve water quality and enhance habitats see: https://www.bristolwater.co.uk/performancecommitments
Distribution Network Efficiency		
Water main replacement rate	IF-WU-140a.1	Mains Repairs, (Number of repairs per 1,00km), page 17
Volume of non-revenue real water losses	IF-WU-140a.2	Leakage (3 yr average), page 17
Effluent Quality Management		
Number of incidents of non-compliance associated with water effluent quality permits, standards, and regulations	IF-WU-140a.2	South West Water EPA Data Report, Section 4. Discharge Permit Compliance metric – produced by the EA, available from gov.uk

Burrator Reservoir, Devon

Metric	Code	Pennon & Bristol Water Disclosure
Effluent Quality Management continued		
Discussion of strategies to manage effluents of emerging concern	IF-WU-140a.2	To access data that South West Water contribute to the Chemical Investigation Programme (CIP), please refer to: *CIP data portal* – available at: https://ukwir.org/sign-up-and-access-the-chemical-investigations-programme-data-access-portal To see the findings from the last CIP2 report, please refer to: CIP2 report – available at: https://ukwir.org/the-chemicals-investigation-programme-phase-2,-2015-2020
End-Use Efficiency		
Percentage of water utility revenues from rate structures that are designed to promote conservation and revenue resilience	IF-WU-420a.1	Omitted based on lack of applicability – Pennon do not offer different rate structures
Customer water savings from efficiency measures	IF-WU-420.a	Pennon Annual Report, Water Saving Community Fund, page 29
Network Resiliency & Impacts of Climate Change		
Wastewater treatment capacity located in 100-year flood zones	IF-WU-450a.1	This year we are publishing our first Drainage and Wastewater Management Plans (DWMP), in accordance with new government regulations. Within this plan we have outlined which of our assets are within flood zones 3 (FZ3). This plan will be accessible from May 2023, via the South West Water webpage.
1) Number and (2) volume of sanitary sewer overflows (SSO), (3) percentage of volume recovered	IF-WU-450a.2	Please refer to: EDM Return – available at: www.southwestwater.co.uk/search/?category=0&searchTerm=EDM
(1) Number of unplanned service disruptions, and (2) customers affected, each by duration category	IF-WU-450a.3	Pennon Annual Report, Operational KPI, page 17
Description of efforts to identify and manage risks and opportunities related to the impact of climate change on distribution and wastewater infrastructure	IF-WU-450a.4	**South West Water** WRMP, Section 5. Forecasting our supply requirements, chapter 4. Impacts of climate change on water supply. Please refer to: South West Water Draft Water Resource Management Plan (WRMP) 2024 - available at: https://www.southwestwater.co.uk/environment/water-resources/water-resources-management-plan/ Climate change Adaptation Report, 2021. Appendix A: Detailed risk management matrix - available at: https://www.southwestwater.co.uk/siteassets/document-repository/environment/climate-change-adaption-2021.pdf **Bristol Water** Bristol Water's Draft Water Resource Management Plan (WRMP) 2024, Chapter 9. Climate Change - available at: https://www.bristolwater.co.uk/about-us/our-plans/water-resources/
Water Affordability & Access		
Average retail water rate for: (1) residential (2) commercial (3) industrial customers	IF-WU-240a.1	South West Water average retail water rates for business customers is available at: https://www.source4b.co.uk/SourceForBusiness/media/Documents/22-23-Charges-Scheme.pdf The average retail water rate for residential customers is available at: https://www.southwestwater.co.uk/your-account/bills/our-charges Bristol Water household charges, available at: https://7850638.fs1.hubspotusercontent-na1.net/hubfs/7850638/Bristol%20Water%20Charges%20scheme%2022-23.pdf Non-household and wholesale charges, available at: https://f.hubspotusercontent30.net/hubfs/7850638/Assurance%20statement%2022-23.pdf
Typical monthly water bill for residential customers to 10 Ccf (1,000 cubic feet) of water delivered per month	IF-WU-240a.2	South West Water charges document, available at: https://www.southwestwater.co.uk/bills/our-charges/ Bristol Water household charges available at: https://www.bristolwater.co.uk/our-blogs/charges-2021-22

Metric	Code	Pennon & Bristol Water Disclosure
Water Affordability & Access		
Number of residential customer water disconnections for non-payment, percentage reconnected within 30 days	IF-WU-240a.3	Omitted based on lack of applicability – Pennon do not disconnect customers for non-payment
Discussion of impact of external factors on customer affordability of water, including the economic conditions of the service territory	IF-WU-240a.4	South West Water's addressing affordability and vulnerability Document- available at: www.southwestwater.co.uk/siteassets/document-repository/business-plan-2020-2025/addressing-affordability-and-vulnerability.pdf
Water Supply Resilience		
Total water sourced from regions with High or Extremely High Baseline Water Stress, percentage purchased from a third party	IF-WU-440a.1	South West Water and Bournemouth Water Drought Plan (2022)- available at: https://www.southwestwater.co.uk/siteassets/document-repository/environment/sww-bw-final-drought-plan-september-2022.pdf For further information of classifications, please refer to the EA's Water Stressed Areas Classification report available at: https://www.gov.uk/government/publications/water-stressed-areas-2021-classification Under the EA classification Bristol Water do not source water from regions with high or extremely high-water stress
Volume of recycled water delivered to customers	IF-WU-440a.2	Omitted based on lack of applicability – We do not deliver recycled water to customers
Discussion of strategies to manage risks associated with the quality and availability of water resources	IF-WU-440a.3	**South West Water** Draft WRMP 2024, chapter 1 section 9.5.9 Drinking Water Safety Plans, and chapter 10 modelling & scenario analysis. Please refer to: South West Water Draft Water Resource Management Plan (WRMP) 2024 - available here: https://www.southwestwater.co.uk/environment/water-resources/water-resources-management-plan/ **Bristol Water** Draft WRMP 2024, section 5. Water Supply and section 8. Sustainable Abstraction. Please refer to: Bristol Water's Draft Water Resource Management Plan (WRMP) 2024 - available here: https://www.bristolwater.co.uk/about-us/our-plans/water-resources/
Activity Metric		
Total water sourced, percentage by source type	IF-WU-000.B	**South West Water and Bristol Water APR** Additional regulatory information section - Water resources asset and volumes data table ESG Databook, section 1.5 Water
Total water delivered to: (1) residential (2) commercial (3) industrial (4) all other customers	IF-WU-000.C	**South West Water and Bristol Water APR** Additional regulatory information – Water network plus, Treated water distribution – assets and operations table
Average volume of wastewater treated per day, by: (1) sanitary sewer (2) stormwater (3) combined sewer	IF-WU-000.D	**South West Water and Bristol Water APR** Additional regulatory information -Wastewater network plus, Wastewater network+ – Sewer and volume data able and Sewage treatment works data table
Length of: (1) water mains (2) sewer pipe	IF-WU-000.E	**South West Water APR** Additional Regulatory Information –Water Network Plus section, Water Network+ table – mains, communication pipes and other data Wastewater network plus, Wastewater network+ table –sewer and volume data

Taskforce on Nature-related Financial Disclosures (TNFD) 2023 – our approach

The aim of TNFD is to support a shift in global financial flows toward 'nature-positive' outcomes. We welcome the development of TNFD as an important mechanism for further embedding environmental leadership across the business. Our voluntary engagement with the TNFD framework is strengthening our long-term risk management and aligns to our strategic ambition to create green investment opportunities.

Our interpretation of TNFD

We recognise this is the decade of action for nature restoration and we are adapting to the national policy landscape which is developing at pace to set new standards and frameworks for businesses to better prioritise, manage and disclose nature-related risk and opportunities.

Stakeholders rightly tell us that they expect environmental leadership from us as a priority, which we intend to deliver with increased transparency around our management of green and blue spaces, our environment, and our natural resources.

What we are doing

Across the business, there is already a wide variety of nature-related activity facilitating the TNFD which we are in the processes of assessing to inform future financial planning. We are continuing to align processes and plans for nature-related risk management whilst using TNFD to inform our decision making as we aspire to meet best practice and maximise 'win-win' opportunities. For example, we have made significant investment into nature-based solutions through our climate change adaptation plan to tackle simultaneously a range of emerging risks such as pollution, climate change and biodiversity loss.

Baseline natural capital assessments undertaken in 2019 provide good indication of our 'business footprint' which informs how we map our interface with nature as well as better understand our upstream, direct and downstream activities dependent on natural resource management. Furthermore, in the past year internal teams began working together to understand how we can incorporate existing tools and platforms into the (LEAP) methodology for TNFD.

Key considerations

Going forward, our intention is to incorporate nature-climate related risks and opportunities into strategic decision making. There are key interdependencies to address between TNFD and Taskforce for Climate related Financial Disclosure (TCFD), which we have implemented since 2019. Importantly, we need to consider potential negative trade-offs between nature and climate for future financial planning. For example, if water quality is best improved using end-of-pipe solutions vs. grey structures with more embodied carbon.

Furthermore, individuals and businesses will depend on nature in river catchments we interface with, but we are not the sole actor impacting on them and therefore developing collaborative approaches to nature-related risk and opportunity management is very important e.g., engagement in regional planning groups for the WRMP to deliver collaborative catchment management approaches such as Upstream Thinking.

Pennon TNFD summary

Governance
We have developed our governance framework for Pennon's ESG Committee to include oversight of the company's nature-related risks and opportunities. These were identified through our ESG materiality assessment undertaken in 2020-21 in line with the 'risk appetite and identification' stage of our existing risk management cycle.
Our approach to following best practice and how we comply with legal and regulatory requirements is outlined in our Biodiversity and Environmental policies.
Strategy
Our plans set out how we strive to maintain compliance, meet regulatory requirements, drive performance using targets, adopt best practice and invest in nature-based solutions (NBS).
Our policies are underpinned by a series of environmental strategies and plans that interlink up to 2050.
Risk & Impact Management
Through our longer-term planning processes we measure a range of nature-related risks such as flood risk, biosecurity risk prevention and habitat restoration.
Metrics & Targets
Our long-term targets align with government expectations for bathing water quality improvement, delivering Biodiversity Net Gain and achieving favourable conditions for SSSI sites.
We measure Group performance on nature-related metrics against our ESG targets and communicate the environmental impact of our operations using South West Water's Environmental Dashboard.

Next Steps

Initially we have drawn together our interpretation of the TNFD guidance and LEAP process (Locate, Evaluate, Assess, Prepare) and are starting to gain oversight on how we map our interfaces with nature across our operations, activities, and supply chain. From this, the way we identify, assess, and prioritise nature-related risks and opportunities (transition and physical risks) will inform our nature-related risk registers.

We are using previous work and relevant risk assessments in this area and considering the additional actions required to manage our nature-related risks to deliver on our nature-positive objectives.

The delivery of our business plans including Green Recovery, WaterFit and Net Zero Plan to 2030 will define our contribution to a nature positive economy. Looking to the future of ESG reporting, the Group is now looking to further embed TNFD recommendations for nature-related risk and opportunity management into business decision making in preparation for PR24 and beyond.

Task Force on Climate-related Financial Disclosures (TCFD)

We are driven by our strategic focus of leading UK environmental infrastructure, delivering for the benefit of our customers, communities, and the environment.

We are committed to meeting the challenges arising as a result of climate change and the transition to Net Zero. Our TCFD disclosure sets out the key climate-related risks and opportunities being addressed by the Group. Our regulated water business is the main focus of our TCFD disclosures with the majority of our assets, revenues, and expenditures related to this area of our business.

TCFD recommendations

Created by the Financial Stability Board (FSB), the TCFD published its recommendations in June 2017. This is our fourth year of TCFD reporting and the below shows our progress and compliance to the recommendations including the updated TCFD guidance (2021 Annex).

In alignment with the FCA listing rule 9.8.6R(8) we have taken into account available knowledge and guidance concerning the listing rule and climate-related risks to develop our compliant TCFD disclosure. Each year our disclosures have been enhanced as knowledge and guidance improves. Pennon has addressed the 11 recommended disclosures and has considered the latest best practice guidance from the TCFD.

As part of our ongoing TCFD programme, we have enhanced our assessment of physical risks, transition risks, and climate-related opportunities. In 2022 we expanded upon our focus on physical risks, which was the focus of our 2021 TCFD disclosure and South West Water's Climate Adaptation Report in 2021.

The year of 2022 provided record-breaking weather events, including extreme high temperatures, prolonged dry conditions, and consecutive red weather warnings for storms and high winds. These events have provided us with significant insight into our resilience to these kinds of events (which we could see more frequently in the future) which are factored into our update of physical risk assessment and our review of adaptive strategies.

Since our 2022 TCFD disclosure, South West Water have published our draft Water Resources Management Plan (dWRMP24) and Drainage & Wastewater Management Plan (DWMP), and are currently developing its business plan for PR24, which involved developing best-value plans and strategies to ensure the resilience of our assets and operations, supporting our communities and the environment. Therefore, our TCFD disclosure this year reflects updated current and future actions to mitigate risks and realise opportunities. The updates to our risk assessments also consider new climate-related evidence and recent publications from the IPCC and CCC, further to recent publications from Ofwat (South West Water's economic regulator) on scenario analysis, adaptive planning, PR24 methodology, and updates in regulation and legislation, the latter of which gives us greater confidence in our transition risk impact reporting in the short term.

We have also provided further details on impacts under each horizon and distinguished primary financial impacts to our business between impacts of the unmitigated risk and impacts from mitigating the risk to emphasise the investment required to build adaptive capacity (or alternatively, the costs of not taking action).

The Group is focused on delivering for our stakeholders including our customers and shareholders. As a result, we are continuing to embed climate change resilience and sustainability into decision making within our business, as well as managing the near-term inflationary pressures including power prices. We will also continue to manage change to our investments to explore new technology, materials, and nature-based solutions, within the current global constraints on capacity and supply chains to deliver both affordability and fairness for our customers.

As a Group, we maintain consistent and strong reporting with the CDP presenting our efforts to combat climate change and our GHG emissions since 2013. Our GHG emissions performance continues to improve, reported through our CDP Climate Change submission in which we received a B in 2022. You can read our GHG emissions performance on page 67.

Solar panels at De Lank Water Treatment Works, Cornwall

Governance

The organisation's governance around climate-related risks and opportunities

2022/23 progress	2024 and beyond
• We have further developed our governance framework, including increased recognition of the role that each Board Committee and several executive committees play in managing climate-related risk and opportunities • We have enhanced how carbon impacts are considered in our capital planning by incorporating carbon values into investment appraisal.	• Whilst climate change is already considered as part of the decision-making process across the business, we will continue to further embed the TCFD considerations into the governance and management of climate risks across our business in 2023/24 • We will continue to further embed the assessment and identification of climate-related risks within our investment appraisal processes.

Strategy

The actual and potential impacts of climate-related risks and opportunities on the organisation's business, strategy, and financial planning

2022/23 progress	2024 and beyond
• We have reviewed and enhanced our assessments of physical and transitional climate risks and opportunities. We have re-assessed the materiality of key risks with stakeholders across the Group and enhanced the actions we are taking to manage the most pressing risks. • We have considered climate change in South West Water's strategic planning for Water Resources (dWRMP24) and Drainage & Wastewater (DWMP), and we are embedding climate resilience and Net Zero into the PR24 business plan as part of PR24.	• We will continue to integrate our climate risks within our existing risk management systems and risk registers across the Group. Risk owners will continue to drive and monitor action to manage risks and pursue opportunities. • We will continue to review our policies and strategic decision-making across the Group in order to enhance considerations of climate risks and opportunities. • South West Water will publish it's final WRMP and our draft business plan for PR24.

Risk Management

The processes used by the organisation to identify, assess, and manage climate-related risks and opportunities

2022/23 progress	2024 and beyond
• We have enhanced our risk management methodology to improve consideration of impacts related to carbon, sustainability, nature, and the Group's ESG goals. • We have reviewed our principal risks and enhanced our recognition of how climate change and Net Zero impact and influence our principal risks.	• We will continue to review and update our management of climate change and our decision-making frameworks to ensure climate-related risks are clearly identified and assessed through the investment processes and operational decision-making.

Metrics and Targets

The metrics and targets used to assess and manage the relevant climate-related risks and opportunities

2022/23 progress	2024 and beyond
• We have enhanced our metrics linked to key climate risks and opportunities, and our investments in climate action. We are tracking progress against our ESG targets and our Net Zero commitments and renewable energy generation. • We are undertaking analysis to quantify key risks, such as major assets at risk of coastal flooding.	• We are continuing to explore options to develop quantitative metrics for our key climate risks and opportunities, and exploring our ability to report on our capital expenditure related to climate action.

Climate-related Governance

Disclose the organisation's governance around climate-related risks and opportunities.

Recommended disclosures	Board oversight
a. Describe the Board's oversight of climate-related risks and opportunities. b. Describe management's role in assessing and managing climate-related risks and opportunities.	The Group has a strong governance structure in place to oversee the effective operation of our business and to manage all risks - including climate-related risks and opportunities. Overall ownership and responsibility for risks, opportunities, and mitigation actions is held by the Pennon Group Board and CEO. Various Board Committees and executive sub-committees play a key role in overseeing climate-related risks within their domain. The Group recognises that climate change and the transition to Net Zero impacts and influences several of the Group's principal risks (see our Principal Risks report on page 52. Principal risks are reviewed as part of our audit governance processes. During the regulatory period, climate change planning is assessed to ensure the business remains resilient to changes to its capital programme.

Pennon Group and South West Water Board

The Group and South West Water Boards provide oversight to the management of the climate-related risks and opportunities. The Board has overall responsibility for the Group's risk management policies and processes, and all principal risks are reviewed by the Board on a regular basis. The Board considers climate-related risks and opportunities throughout its duties - including when considering the Group's strategy and objectives, monitoring business and operational performance, business planning and annual budget setting, reviewing major capital expenditures and existing investments, and in considering acquisitions/divestitures. We are continuing to enhance the awareness and capacity of our Board and senior executives relating to climate risks and opportunities. For more information see our Corporate Governance report pages 98 to 161.

Board Committees

All Board Committees play a role in managing our climate-related risks and opportunities, and matters are escalated to the Board as appropriate. Board Committees report their actions and decisions to the Board, ensuring robust governance - including for matters influenced by climate change and the transition to Net Zero. The responsibility for climate-related risks and opportunities is cascaded through the business in order to meet our targets and objectives.

Audit Committee

Attendance: Meets 4 times annually. Attended by the Chair and other Non-Executive Directors.

Role relating to climate risks and opportunities: The Committee monitors the Group's financial reporting, including how the impacts of climate risks are accounted for in financial statements. The Committee also reviews key risks and opportunities (including climate-related risks), and challenges and tests the Group's internal control processes including risk management and internal audit. Further information on page 120.

ESG Committee

Attendance: Meets 4 times annually. Attended by the Pennon Board, CEO, CFO and other Group Executives.

Role relating to climate risks and opportunities: Provides the platform for discussion of the Group's ESG agenda and related climate risks and opportunities, as well as setting and reviewing key metrics relating to our '6 capitals' assessments, and reviewing performance against ESG targets and goals. The Sustainable Financing reporting and monitoring is reported to the Committee for onward submission to the Board. Further information on page 126.

Nomination Committee

Attendance: Meets 4 times annually. Attended by the Chair and other Non-Executive Directors.

Role relating to climate risks and opportunities: Considers competency related to climate risks and opportunities when reviewing the structure, size, and composition of the Board and senior executives In the Group. Further information on page 128.

Remuneration Committee

Attendance: Meets 4 times annually. Attended by the Chair and other Non-Executive Directors.

Role relating to climate risks and opportunities: Considers the Group's objectives and responsibilities, and advises the Board on the framework of executive remuneration for the Group and for the wider workforce, including mechanisms to incentivise achievement of the Group's objectives related to climate change, Net Zero, and sustainability goals. Further information on page 134.

Health and Safety Committee

Attendance: Meets 3 times annually. Attended by the Chair, CEO, CFO, and other Non-Executive Directors.

Role relating to climate risks and opportunities: Supports the Executive Board on matters of risk across all areas of health & safety, resilience, and process safety - including areas impacted by climate-related risks, particularly related to extreme weather events. Also reviews the effectiveness of the Group's procedures for H&S reporting and performance. Further information on page 132.

PR24 Committee

Attendance: Meets during the Board cycle as we progress the plan. Attended by the Chair, other Non-Executive Directors, CEO, CFO and other Group executives.

Role relating to climate risks and opportunities: Considers climate change and Net Zero as part of business planning and the Group's PR24 strategy.

Peatland restoration on Bodmin Moor, Cornwall carried out by the South West Peatland Partnership team

Pennon Executive Committee[1]

Attendance: CEO, CFO, COO, GCCS, CPO, CCDO, Director of Regulation Strategy and Asset Management, Chief Engineering Director, Director of Drought and Resilience

Role relating to climate risks and opportunities: The Committee monitors, approves and reviews business objectives and plans, and provides challenge and feedback to investment decisions. Throughout these processes climate-related risks and opportunities are considered and actions to manage risks are embedded in business planning and Investment decision-making. There are several executive committees who report to PEx, and below are some of the key committees which consider climate-related risks and opportunities within their remit:

- The monthly business review meeting - oversees and informs Board Committees on operational performance and risks across the Group, including the impacts of climate-related risks to operations and the actions being taken to manage operational risks. Other committees report to OPEx, and key committees with a specific remit related to climate risks and opportunities include: PR24 Executive Committee, Compliance Committee, and Drought & Resilience Programme Steering Committee
- Energy Risk Committee - focused on managing the Group's energy risk exposure and reviewing renewable energy opportunities
- Executive Risk Committee - reviews and approves items relating to principal risks before they are presented to Committees at Board level - including risks and opportunities relating to and influenced by climate change
- IPC Procurement Committee - considers climate-related risks and opportunities when reviewing and approving investment planning and major procurement items
- ESG Executive Committee - reviews and approves items relating to ESG before they are presented to the ESG Committee at Board level - including items which relate to or are influenced by climate change
- Net Zero Executive Committee - monitors, reviews, and provides support for the implementation of the Net Zero Strategy, including considering risks and opportunities relevant to delivery of the strategy

Management's role

Executive managers play a key role in identifying, assessing, and managing climate-related risks and opportunities, and Executive managers sit on relevant Executive committees. The responsibility for climate-related risks is clearly owned, managed, and assessed by a number the Group's management teams across our business including our management responsible for water resources, wastewater, regulation, procurement, and finance. Risk is identified and categorised in different parts of our business prior to being formally passed onto senior management responsible for those business functions. Each business function and department maintains a risk register, and management escalates risks to the Executive Committees as appropriate.

The Executive Directors' remuneration policy is set to incentivise the achievement of key performance objectives. In 2021/22, the element previously based on personal objectives was changed and now relates to ESG objectives and performance including targets relating to our carbon reduction goals, the working environment for our employees, and diversity.

Strategy

Disclose the actual and potential impacts of climate-related risks and opportunities on the organisation's businesses, strategy, and financial planning where such information is material.

Recommended disclosures

a. Describe the climate-related risks and opportunities the organisation has identified over the short, medium, and long term.
b. Describe the impact of climate-related risks and opportunities on the organisation's businesses, strategy, and financial planning.
c. Describe the resilience of the organisation's strategy, taking into consideration different climate-related scenarios, including a 2°C or lower scenario.

Our most material physical and transitional climate-related risks and opportunities are presented on the following pages. These have been identified by considering the climate scenarios described on page 90. The risks have been assessed using the Pennon 4x4 risk assessment matrix which puts the highest risks in the red category under the RAG rating. Further information on our risk assessment methodology can be found on page 52. We have identified impacts over short (0-10 years), medium (10-30 years) and long term (30-100 years) horizons (the rationale behind these time horizons is presented on page 90).

Due to the nature of the business, the opportunities are not only assessed on financial merits, with some opportunities not increasing revenues but are opportunities to save costs and/or carbon, which supports our ability to provide the best outcomes for our customers and stakeholders.

We then present our findings from scenario analysis, exploring the potential range of impacts and our strategic responses under plausible contrasting climate scenarios (see page 91).

1. CBO = Chair of the Board, CEO = Chief Executive Officer, CFO = Chief Financial Officer, GCCS = General Counsel & Company Secretary, COO = Chief Operating Officer, CPO = Chief People Officer, CCDO = Chief Customer and Digital Officer

Key – Strategic priorities

Risk			Opportunity		
High	Medium	Low	Increasing	Stable	Decreasing

Physical Risks

	Key impacts identified on our operations and customers[1]
Key physical climate risks Increasing frequency and intensity of droughts - risks to water supply, wastewater networks, and services. **Relevant time horizon** Short, medium and long term, with increasing likelihood and magnitude of risk over each horizon **Risk score in 2025 including current actions** **Risk score in 2050 without further action**	• Increased daily and peak demand for garden watering, crop irrigation, and tourism during drought events exceeds capacity to redistribute water. • Sustained drought can lead to supply shortfalls with a heightened risk for recovering water storage if there are consecutive drought years. • Drought events lead to loss of supply and de-pressurisation of pipelines, greater incidence of pipe failure and contamination. • More extreme wetting and drying cycles cause soil movement, more pipe movement/ subsidence and bursts/ increased leakage. • Lower river flows as a result of drought events reduce yields. Could lead to reductions in our future abstraction allowances and increased need to release more water to rivers/the environment (see also 'climate-related regulation in the Water sector' transition risk). • Lower groundwater levels reduce borehole yields. Intake, borehole pump and reservoir draw-off levels may not match reduced levels. • Saline intrusion due to lowering groundwater compounded by sea level rise (see 'Rising sea levels' risk). • Decreased intake raw water quality (see 'Increasing average temperatures and heatwaves' risk). • Impacts on wastewater networks due to low flows from surface water.
Key physical climate risks Increasing average temperatures and heatwaves - risks to water quality and water treatment **Relevant time horizon** Short, medium and long term, with increasing likelihood and magnitude of risk over each horizon **Risk score in 2025 including current actions** **Risk score in 2050 without further action**	• Decreased water quality (odour, discolouration, dissolved organics, Cryptosporidium) requiring additional resources and cost to remove pathogens from drinking water or ensure water quality meets regulatory standards at WTWs. • Increased microbe propagation and survivability affecting treatment processes. • Higher septicity levels in received wastewater. • Algal blooms, triggered by catchment runoff, are exacerbated by higher temperatures. • Higher peak demand for water compounded by reduced runoff yields due to higher temperatures increasing evaporation (see 'Increasing frequency and intensity of droughts' risk). • Decreased water quality during heatwaves compounded by overheating of equipment/assets. • Cascading impacts to interdependent networks (e.g. power supply) from overheating, leading to service disruption. • Increased prevalence of invasive non-native species (INNS).
Key physical climate risks Increasing frequency of heavy rainfall and floods - risks to assets & services, water quality, and the environment **Relevant time horizon** Short, medium and long term, with increasing likelihood and magnitude of risk over each horizon **Risk score in 2025 including current actions** **Risk score in 2050 without further action**	• Flooding of assets and treatment works, loss of access to assets, and greater sediment levels in raw water which disrupt services and potentially impact the environment. • Cascading impacts to interdependent networks (e.g. power supply) from flooding, leading to service disruption. • Increased groundwater leading to increased infiltration into assets. • Increased volumes of storm water exceed pump capacity leading to service failures. • Exceedance of storm tank design and asset flooding/damage with interruption to service. • Increased frequency and duration of storm overflows, with potential impacts to water bodies - including potential closure of beaches. • Increased river flows and risk of bank erosion exposing wastewater pipes increasing the risk of collapse. • Catchment erosion in moorland or peatland areas, with nutrients leaching that increase algal growth in waterbodies and reservoirs. • Dilution of, and rapid variations in, influent flows – longer retention of water in storm tanks leads to increased septicity and operational problems. • Increased flood incidence impacts water quality for some boreholes, may result in temporary inaccessibility or contamination. Increased turbidity of water sources.

1. Key impacts are taken as the top-scoring risks from South West Water's Adaptation Report 2021 under the relevant climate driver, considering the 2025 and 2050 time horizons.

Examples of our actions to mitigate risks and realise opportunities	Primary financial and reputational impacts to our business

Current actions:
• Collaborative water resource management planning – West Country Water Resources and Water Resources South East.
• Drought planning including more extreme events. Stochastic and multi-year drought analysis to test how water supply systems perform in extreme prolonged droughts.
• Prioritisation of support for vulnerable customers during droughts.
• Demand management and water efficiency, including Per Capita Consumption (PCC) reductions and leakage reduction strategy.
• Investigation of regional water transfers.
• Potential Abstraction Incentive Mechanism (AIM) schemes.
• Enhancements to distribution system to remove bottlenecks/ support us to meet peak demand.
• Desalination scheme in development for 2023 to enhance our drought management.
Planned or future actions:
• Finalise draft Water Resources Management Plan 2024[1] including:
  • demand management options i.e. increased metering, leakage reduction.
  • schemes to increase water supply (e.g. Cheddar2 SRO, Mendip SRO, enhancing interconnectivity of water resource zones) with new sources, storage.
  • water treatment improvements and wastewater reuse
• Potential for additional desalination schemes.
	Impacts from mitigating the risk:
	We could incur increased expenditure (Opex and Capex) to increase capacity for water supply infrastructure, and to manage drought conditions and water demand. Some of these costs could be recoverable through the regulatory system. Increased energy and material use could impact our operational and embodied carbon.
	Impacts of the unmitigated risk:
	Service disruptions could negatively impact our reputation and reduce ODI rewards/ increase ODI penalties (affecting our revenue).
	We could face additional expenditure (Opex and Capex) to recover from service disruptions, reduce leakage, and manage water demand.
	Some of our assets could deteriorate and face impairment due to physical impacts.

Current actions: • Upstream Thinking catchment management tackling raw water quality to increase resource availability in 80% of our drinking water catchments. • Granular activated carbon at certain Water Treatment Works (WTWs). • Robust health and safety practices and management. • Farm water efficiency and resilience project – 1,000 pond nature-based solutions. • Biodiversity management and INNS programmes. • Installation of cooling systems for equipment/assets. **Planned or future actions:** • Upgrade to granular activated carbon treatment at further WTWs.	**Impacts from mitigating the risk:** We could incur increased expenditure (Capex and Opex) for water and wastewater treatment and odour management, and to increase capacity for water supply infrastructure. Some of these costs could be recoverable through the regulatory system. Increased energy and material use could impact our operational and embodied carbon. **Impacts of the unmitigated risk:** Service disruptions and lower-quality service provision could negatively impact our reputation and reduce ODI rewards/increase ODI penalties (affecting our revenue). We could incur increased expenditure (Capex and Opex) to recover our services or use alternative water supplies. Some of our assets could deteriorate and face impairment due to physical impacts.
Current actions: • Drainage & Wastewater Management Plan (DWMP). • Asset flood risk assessments undertaken every five years. • Contingency planning in flood risk hotspots e.g. River Otter, including prioritisation of support for vulnerable customers. • Sites have temporary deployable flood protection. • Investment in PR19 to improve flood defences at four WTWs up to 1-in-1,000-year events. • Catchment management through Upstream and Downstream Thinking. • Continued investment in our WaterFit Plans - reducing storm overflow releases and improving river and coastal water quality, creating and restoring habitat, and looking to inspire local champions to improve water quality through schools and communities. • New Mayflower WTW in Plymouth increases local flood resilience. • Partnership flood schemes e.g. Countess Wear Wastewater Treatment Works (WWTW)(Exeter). **Planned or future actions:** • Further sewer separation schemes in areas at risk. • Surface water drainage plans and investment in key areas. • Expand our Upstream Thinking initiative. • Real-time monitoring and control (e.g. at all CSOs). • Continue to improve incident management.	**Impacts from mitigating the risk:** We could incur additional expenditure (Opex and Capex) to improve operational resilience and flood defences, and to enhance our Upstream and Downstream Thinking programmes. Some of these costs could be recoverable through the regulatory system. Increased energy and material use could impact our operational and embodied carbon. **Impacts of the unmitigated risk:** Service disruptions and combined storm overflows could negatively impact our reputation and reduce ODI rewards/increase ODI penalties (affecting our revenue). We could incur additional expenditure (Opex and Capex) to recover our services and repair damaged assets. Some of our assets could deteriorate and face impairment due to physical impacts.

1. South West Water draft WRMP24 chapter 11 recommended plan v2.1 (southwestwater.co.uk)

Key – Strategic priorities					
Risk			Opportunity		
High	Medium	Low	Increasing	Stable	Decreasing

	Key impacts identified on our operations and customers[1]
Key physical climate risks Rising sea levels and coastal erosion - risks to assets and services **Relevant time horizon** Short, medium and long term, with increasing likelihood and magnitude of risk over each horizon **Risk score in 2025 including current actions** **Risk score in 2050 without further action**	• Direct asset damage from flooding, storm damage and/or coastal erosion. • Cascading impacts to interdependent networks (e.g. power supply) due to damage from coastal flooding, storm damage and/or coastal erosion. • Rising sea levels increase the extent of the saline intrusion zone. Tidal limits move upstream, causing increased salinity at river intakes. This can cause accelerated asset deterioration and reduced process performance efficacy. • Increased health and safety implications e.g. hydrogen sulphide gas from wastewater treatment works. • Saltwater intrusion of groundwater sources causing source to become unusable (compounded by lowering groundwater levels – see our 'Increasing average temperatures and heatwaves' risk). • Coastal estuarine storm overflow discharges become tide-locked hindering free discharge • Increased environmental ambition by other stakeholders to replace lost coastal habitat and manage coastal erosion, impacting our assets and services (in some cases requiring us to carry out actions which may not be funded through the regulatory system).
Key physical climate risks Increasing frequency of extreme weather events and storms - risks to assets and services **Relevant time horizon** Short, medium and long term, with increasing likelihood and magnitude of risk over each horizon **Risk score in 2025 including current actions** **Risk score in 2050 without further action**	• Power supply failure due to high winds, heavy rainfall/flooding, lightning at key network and treatment sites and resultant cascading impacts to interdependent networks, including water supply delivery and wastewater management. • Cold snaps and freeze/thaw events leading to pipe bursts/ increased leakage. • Reduced ability for our services and assets to recover under consecutive storms.

Transition Risks

Type as defined by TCFD
Policy, Regulation and Legal Risks
Relevant time horizon of risk
Short and medium term
Potential for this risk to decrease over time as regulation evolves to remove contradictions and misalignment, and as leadership on climate action becomes commonplace across Government and the economy.
Current Risk Rating
	Risk of challenges balancing trade-offs in regulation in the Water sector between agendas of Net Zero, climate resilience, environmental enhancement, and other objectives, posing the risk of increasing costs and carbon: Potential undesired climate outcomes due to trade-offs in regulatory priorities. Challenges with balancing objectives to improve environmental outcomes while reducing carbon emissions at the same time as rapid changes in climate-related policies and regulations are occurring in the Water sector.
	A holistic and balanced approach to delivering our goals for Net Zero, providing a resilient water supply and protecting and enhancing the environment, could be at risk if one agenda imposes more stringent regulation, thus presenting a misalignment in the pace with which preferably holistic actions can be delivered relative to actions that benefit a single more stringent agenda. In some cases, new/enhanced policies and regulations pose a risk due to increasing costs to Pennon or increasing Pennon's carbon footprint, in other cases the absence of policies and regulation pose a risk due to potential that costs incurred by Pennon may not be recovered through the regulatory system.
	Some examples include:
	• more stringent environmental regulation being imposed in response to the climate adaptation and nature positive agenda, including the pace with which requirements are being imposed:
	  • reduced abstraction allowances and increased compensation flows into our rivers being imposed (see our 'drought' physical risk)
	  • increased environmental ambition by other stakeholders to replace lost coastal habitat and manage coastal erosion (see our 'rising sea levels' physical risk).
	• changes to carbon accounting methodologies and scope boundaries, including changes to location-based GHG accounting methodology instead of market-based accounting (e.g. disincentivising power purchase agreements (PPAs) for renewable energy).
	• enhanced requirements which increase Pennon's energy and carbon footprint e.g. phosphorus removal, UV disinfection, reducing combined sewer overflows in cases where the scale and pace required disadvantages nature-based solutions.
	• regulation in contradiction to achieve overall Net Zero goals, and regulatory system providing limited incentives for wider Net Zero action outside of the regulated water business.

Examples of our actions to mitigate risks and realise opportunities	Primary financial and reputational impacts to our business
Current actions: • Asset flood risk assessments undertaken every five years. • Prioritisation of support for vulnerable customers. • Improved flood resilience of all assets in the coastal floodplain. • Partnership flood schemes e.g. Countess Wear WWTW (Exeter). • Protection of sites from saline intrusion/incursion (Otter Basin). • Continuing work with stakeholders involved in managing coastal erosion. **Planned or future actions:** • Protection of further sites from saline intrusion/incursion. • Desalination programme.	**Impacts from mitigating the risk:** We could incur additional expenditure (Opex and Capex) for protecting our sites and assets from coastal flooding and saline intrusion. Some of these costs could be recoverable through the regulatory system. Increased energy and material use could impact our operational and embodied carbon. **Impacts of the unmitigated risk:** Service disruptions could negatively impact our reputation and reduce ODI rewards/increase ODI penalties (affecting our revenue). We could face additional expenditure (Opex and Capex) for using alternative water supply if sites/sources become unusable. Some of our assets could deteriorate and face impairment due to physical impacts.
Current actions: • Cold weather plan, including prioritisation of support for vulnerable customers. • Investment in centralised control room and alternative water supply teams. • Duplication of strategic water mains network. • Backup power at plants to manage risks of energy supply interruption. • Recovery plans for 100 WWTWs. • Working with other stakeholders (e.g. energy providers) to enhance resilience. **Planned or future actions:** • Extend real-time monitoring and control. • Extend recovery plans at more WWTWs. • Further investment in generating renewable energy and back-up power.	**Impacts from mitigating the risk** We could incur additional expenditure (Opex and Capex) for maintenance and upgrades to assets to enhance resilience to storms. Some of these costs could be recoverable through the regulatory system. Increased energy and material use could impact our operational and embodied carbon. **Impacts of the unmitigated risk** Service disruptions could negatively impact our reputation and reduce ODI rewards/increase ODI penalties (affecting our revenue). We could face additional expenditure (Opex and Capex) to restore services and repair assets. Some of our assets could deteriorate and face impairment due to physical impacts.
Balancing trade-offs from actions to address different agendas in policy and regulation: **Current actions:** • Horizon scanning to identify emerging/changing regulation. • Stakeholder engagement/public relations management. • Net Zero programme. • Engaging with regulators to explain the climate change impacts of new regulation. • Working with others in the sector to clarify carbon accounting approaches. • Adaptive planning approach within dWRMP24, including high, moderate, and low environmental ambition. • Considering options which Pennon can take outside of the regulatory framework (e.g. offsite investment in renewable energy). **Future actions:** • Pursuing opportunities for nature-based solutions where these are acceptable under the regulation. • Investment in innovation/ research and development, and investment in enhancements to resilience to key climate risks. • Considering applying an internal carbon price to consider full costs and benefits of decisions. • Public value assessments in decision-making (balancing trade-offs of different agendas, and contradictions in the regulatory framework). • Seeking opportunities for additional funding, making the investment case based on core water company activities. • Future climate adaptation planning and transition planning.	**Impacts from mitigating the risk:** We could incur increased expenditure (Capex and Opex) due to changes to regulation, for example costs related to installation and operation of new process equipment to meet enhance regulations. Some of these costs could be recoverable through the regulatory system. Increased energy and material use to meet increased regulatory requirements has potential to increase our carbon footprint through operational and embodied carbon. **Impacts of the unmitigated risk:** If we fail to balance regulatory requirements, we could face reduced ODI rewards/ increased ODI penalties (affecting our revenue). Public perception of how we balance trade-offs could result in negative impacts on our reputation (see our 'Negative public and stakeholder' reputation risk). Some of our assets could incur obsolescence and impairment If they are driving high carbon emissions or poor environmental outcomes.

Key – Strategic priorities

Risk			Opportunity		
High	Medium	Low	Increasing	Stable	Decreasing

Transition Risks continued

	Potential risks and opportunities
Type as defined by TCFD Policy, Regulation and Legal Risks **Relevant time horizon of risk** **Short and medium term** In the short term the risk is more focused on funding to achieve Net Zero, over the medium and long term the risk will increasingly focus on funding to enable adaptation to climate change. **Current Risk Rating**	**Regulatory funding risk for achieving Pennon's goals for operational Net Zero by 2030 and adapting to climate change :** Risk that the investment required to transition to operational Net Zero by 2030, and investment to proactively adapt to climate change in the time period targeted by Pennon, is not allowed under the regulatory framework.
Type as defined by TCFD Technology Risks **Relevant time horizon of risk** **Short and medium term** In the short term the risk is primarily driven by limited supply and readiness of technology and resources (due to past underinvestment in skills development across the UK and beyond), over the medium term the risk will be increasingly driven by high demand for technology and resources. **Current Risk Rating**	**Capacity and readiness of technology and resources to achieve Net Zero before other sectors and the wider UK:** Risks that skills, technology, resources, and infrastructure are not ready and available to enable Pennon's transition to Net Zero operational carbon by 2030, resulting in delays and in some cases resulting in Pennon paying high costs to access resources. Some examples include: • availability and capacity of Pennon's workforce and supply chain to procure and design low-carbon solutions (which Is compounded by wider risks, such as geopolitical events and macro-economic conditions such as high inflation). • availability and capacity of technology and infrastructure, particularly in the Great South West of England, to enable development of Pennon's renewable energy projects and other Net Zero programme activities. • high demand for resources and technologies from others causing delays and increasing costs for Pennon (e.g. demand for expertise, batteries, electric vehicles). • unsuccessful investment in new technologies/approaches, or technology which is then superseded, including risks around recovering costs through the regulatory system. • Innovation required to reduce process emissions is of larger scale than originally understood, amplifying the risk of potential unsuccessful R&D Investments, and the risk of taking investment decisions which in future turn out to be suboptimal / high-regret.

Examples of our actions to mitigate risks and realise opportunities	Primary financial and reputational impacts to our business
Managing regulatory funding risk: **Current actions:** • Business planning/ making case for investment. • Engagement with regulators and customers and stakeholders. • Public campaigns/awareness of investment need for climate action including TCFD programme. • Exploring options to ensure a return on investment for some climate-related actions. • Demonstrating/communicating that Net Zero 2030 for the water sector is a helpful milestone on the way to Government's goal for Net Zero 2050. • Exploring options which Pennon can take outside of the regulated water businesses (e.g. offsite investment in renewable energy, enhancing revenue through water transfers and water resource schemes for other companies). **Future actions:** • Explore options for third-party funding or partnerships for climate action. • Potential for Pennon to review climate change objectives if they are not supported by regulators and Government	**Impacts from mitigating the risk:** We could incur increased expenditure (Capex and Opex) to take actions outside of the regulated water business, and to enhance engagement with regulators and stakeholders. There is potential for us to increase our revenue through some actions. See our 'Products and Services' climate opportunity. **Impacts of the unmitigated risk:** If we cannot proactively invest in carbon reduction and climate resilience we could face reduced ODI rewards/ increased ODI penalties (affecting our revenue). Increased costs to our customers in the long-term would negatively impact our reputation (see our 'Negative public and stakeholder' and 'Customer affordability' reputation risks). Some of our assets could deteriorate and face impairment due to physical impacts from climate change. We may be limited in our ability to reduce our carbon emissions.
Managing capacity constraints in Pennon: **Current actions:** • Continual enhancement of capacity within Pennon (e.g. training, recruiting key skills). • Collaboration with supply chain partners (e.g. consultants, technology providers, contractors). • Collaboration with stakeholders (e.g. academia, environmental groups in the Great South West). • Collaboration with other water companies and across the sector to develop standard approaches and enhance capacity. **Future actions:** • Prioritising actions/solutions which are low-regret/ flexible e.g. nature-based solutions • Piloting options/technology before scaling. **Managing supply chain and infrastructure limitations:** **Current actions:** • Horizon scanning to identify emerging limitations and risks. • Engagement with key suppliers and partners and enhancing collaboration with partners and stakeholders. • Engaging with infrastructure providers, regulators, and Government to encourage investment to enable network capacity. • Enhancing capacity within Pennon to reduce reliance on suppliers. • Purchasing renewable electricity. **Future actions:** • Procurement strategies for key technologies/expertise. • Enhancing supply chain resilience (e.g. diversification of suppliers). • Exploring options which are less reliant on network capacity (e.g. onsite battery storage). **Managing costs to transition:** **Current actions:** • Seek to fund investment through the regulatory process (business planning and price reviews). • Investment in innovation to reduce costs of low-carbon technology. **Future actions:** • Increasing efficiency to reduce costs (see our 'resource efficiency' transition opportunity). • Recovering some costs from retired assets (e.g. selling used equipment) • Explore partnership opportunities (e.g. PPAs). **Managing research and development investment:** **Current action:** • R&D programme with gated investment (e.g. piloting before scaling up). • Horizon scanning to identify emerging technology and risks. • Procurement strategies to reduce costs (e.g. competitive tendering, joint ventures). • Learning from others in the water sector in UK and international. • Engagement with regulators and community to test acceptability of strategies and schemes. **Future action:** • Prioritising solutions that are low-regret, particularly nature-based solutions through piloting technology before scaling.	**Impacts from mitigating the risk:** We could incur increased expenditure (Opex) to build capacity across our company and supply chain, and increased costs to access skills and technology to meet our targeted timeline. Some of these costs could be recoverable through the regulatory system. **Impacts of the unmitigated risk:** We could incur increased expenditure (Capex and Opex) due to delays with implementing solutions to reduce operational carbon emissions, and due to high demand for resources. Unsuccessful investment in new technologies could also result in increased expenditure. We could incur penalties and/or negative impacts to our reputation if delays in technology and resources mean we do not meet our targets and/or Net Zero programme (see our 'Negative public and stakeholder reputation' risk). We may be limited in our ability to reduce our carbon emissions.

Key – Strategic priorities

Risk			Opportunity		
High	Medium	Low	Increasing	Stable	Decreasing

	Potential risks and opportunities
Type as defined by TCFD Market Risks **Relevant time horizon of risk** **Short and medium term** In the short term the risk is primarily driven by limited supply of renewable energy and low-carbon materials (due to past under investment in infrastructure and materials across the UK and beyond), over the medium term the risk will be increasingly driven by high demand for renewable energy and low-carbon materials. **Current Risk Rating**	**Increased costs of energy and materials due to the transition to Net Zero, impacts of climate change, and wider factors:** Increases in costs of energy sources and input materials - influenced by the Net Zero transition and/or impacts of climate change and compounded by geopolitical events and macro-economic conditions (e.g. such as high inflation). Some examples include: • Record high price for electricity, particularly 100% renewable electricity/REGOs, which may remain in high demand/ limited supply. • Price of liquid fuels and gas increasing due to transition to Net Zero and geopolitical events. • Price of chemicals and construction materials (e.g. cement, steel) increasing as energy prices increase and in some cases as carbon reduction measures increase across supply chains (adding costs to production of materials In the short/medium term). • Price of some technologies for generating renewable electricity has increased due to high demand/limited supply.
Type as defined by TCFD Reputational Risks **Relevant time horizon of risk** **Short and medium term** In the short term customers and stakeholders are primarily concerned about impacts on water quality and aquatic environments. Over time it is likely that customers and stakeholders will have higher concern for carbon emissions and other sustainability objectives. **Current Risk Rating**	**Negative public and stakeholder relations due to Pennon failing to be a seen as a leader in environmental sustainability:** Negative perception from the public/stakeholders/regulators, possibly linked to a major climate-related incident/event/failure. Some examples include: • Public concern about climate-induced pollution events and sewer overflows (e.g. after storms linked to climate change). • Customers and stakeholders concerned about the environmental impact of abstraction and wastewater discharge in response to the climate adaptation agenda. • Asymmetry of information which customers notice, for example less focus on our action to reduce carbon and more focus on activities which may be seen as high energy, such as desalination (even though desalination would be powered by renewable energy). Greater media coverage of negative impacts more than positive actions compounds this risk. • Shifts in stakeholder/customer expectations related to carbon and climate which are difficult for Water companies to manage. • Stakeholder and customer dissatisfaction if Pennon fails to meet Net Zero commitments.
Type as defined by TCFD Reputational Risks **Relevant time horizon of risk** **Short and medium term** The need for additional investment to meet the Net Zero and climate adaptation challenges will likely continue to impact across the medium term, particularly if global climate action is slow and the physical impacts are greater. **Current Risk Rating**	**Customer affordability and fairness concerns for achieving Net Zero and adapting to climate change:** Affordability for customers and questions around fairness become very challenging, even with Government contribution to water and wastewater bills (this is compounded by cost-of-living pressures). This risk includes: • Large investment needs related to climate change, which could result in dissatisfaction from customers and stakeholders. • Questions relating to fairness for paying for climate adaptation, for example high costs/Impacts being imposed on residents in Cornwall and Devon due to greater exposure to coastal change, whereas other water companies may not have as high costs/impacts. • Multiple agendas and misalignment from different Government departments and regulators requiring increased investment from water companies.

Examples of our actions to mitigate risks and realise opportunities	Primary financial and reputational impacts to our business
Managing cost of energy: **Current actions:** • Generation of renewable energy by Pennon, including exploring additional options and power purchase agreements (PPAs). • Increasing efficiency to reduce energy demand (e.g. enhance energy efficiency, reduce leakage - see our 'resource efficiency' opportunity). • Electricity price hedging. **Future actions:** • Fuel switching (e.g. eliminating fossil fuels for alternatives, at lower cost where possible). • Changing operational practices to reduce energy use/ energy expenditure (e.g. taking advantage of off-peak electricity pricing). • Exploring options which require less energy (e.g. nature-based solutions). • Action taken by Government and wider actors to increase energy security and supply of low -carbon energy. **Managing cost of input materials:** **Current actions:** • procurement strategies to reduce cost (e.g. competitive pricing). **Future actions:** • Increasing efficiency to reduce material use and light-weighting/reducing material consumption. • Enhancing supply chain resilience (e.g. diversifying suppliers to reduce cost). • Investing in innovation to use different chemicals and materials.	**Impacts from mitigating the risk:** We could incur increased expenditure (Capex and Opex) due to investment in generating renewable energy or using alternative/low-carbon materials. Some of these costs could be recoverable through the regulatory system, and in some cases there will be a return on investment (see our 'energy source' and 'markets' climate opportunities). **Impacts of the unmitigated risk:** We could incur increased expenditure (Capex and Opex) due to increased cost of energy/REGOs and materials. We may be limited in our ability to reduce our carbon emissions.
Managing public and stakeholder relations: **Current actions:** • Risk management practices. • Investment to reduce key risks, including our WaterFit programme. • Net Zero programme. • Environmental programmes (e.g. Water Industry National Environment Programme – WINEP). • Customer and stakeholder engagement/public relations. • Community outreach and educational programmes. • Engagement and pilots to test and build customer acceptability for schemes. • ESG and sustainability initiatives. • '6 capitals' considered in decision making. **Future actions:** • Consider applying an internal carbon price to consider full costs and benefits of decisions. • Consider new ways to enhance engagement with customers and communities and increase engagement and raise profile of positive actions (e.g. tree planting).	**Impacts from mitigating the risk:** We could potentially incur increased expenditure (Opex) to manage stakeholder relations and public perception to mitigate reputational impacts. **Impacts of the unmitigated risk:** Public perception of our environmental actions and performance could result in negative impacts on our reputation (see also our 'Challenges balancing trade-offs' policy transition risk).
Managing customer affordability: **Current actions:** • Secured Government contribution to customers' bills. • Customer and stakeholder engagement/public relations (including engaging with regulators and Government about sharing costs etc.), including community outreach and educational programmes to help explain need for investment in climate action. • Seeking return on investment for actions taken to manage climate change. • Arrangements with/requirements on suppliers to cover some costs (e.g. building and vehicle leases). • Procurement strategies to reduce costs (e.g. competitive tendering, joint ventures etc.) • Support programmes and social tariffs for customers struggling to pay bills. • Phased investment in climate adaptation and Net Zero over time to reduce pressures on bills. • Exploring actions to reduce costs across the business. • Becoming more efficient to reduce costs and impacts on customer bills. • Exploring innovative tariffs to ensure fair bills. **Future actions:** • Innovation programme seeking to reduce costs. • Recovering some costs from retired assets (e.g. selling off). • Seeking third-party sources for investment (e.g. climate action grants/funds, partnership funding). • Considering flexibility in climate commitments to reduce cost pressures on customers.	**Impacts from mitigating the risk:** We could potentially incur increased expenditure (Opex) to manage public perception of our investments to mitigate reputational impacts (e.g. raising profile of our opportunities). **Impacts of the unmitigated risk:** Public perception of our investments and expenditure could result in negative impacts on our reputation if our decisions and investments do not align with customer priorities (see also our 'Challenges balancing trade-offs' policy transition risk). We could incur penalties if we failed to support customers in need / vulnerable customers suffering from high bills.

Key – Strategic priorities					
Risk			Opportunity		
High	Medium	Low	Increasing	Stable	Decreasing

Potential risks and opportunities

Climate-related opportunities

Type as defined by TCFD
Resilience

Relevant time horizon of risk
Short, medium, and long term
Enhancing resilience to climate change and extreme weather events is of high relevance today, with increasing likelihood and magnitude of risk over each horizon.

Current opportunity rating

Enhancing resilience across Pennon's operations, asset base, and supply chain to avoid costs and enhance value: Opportunity to invest in enhancing resilience across Pennon's business and supply chain, in some cases saving costs (e.g. avoided damage to assets, avoided losses in revenue, avoided penalties on ODIs and GSS) and enhancing company reputation and value. Some examples include:

- Enhancing Pennon's resilience by investing in climate change adaptation e.g. investing in drought and flood prevention measures to avoid customer disruption/ penalties/ compensation payments and avoid asset damage.
- Enhancing supply chain resilience by investing in buffers/storage for critical resources, diversifying suppliers, replacing suppliers who have high climate risks, thereby reducing potential risks and costs associated with supply chain disruption and delays.

Type as defined by TCFD
Energy Source

Relevant time horizon of risk
Short and medium term
This opportunity is of high relevance to meet our 2030 Net Zero target, with continued relevance Into the medium and long term due to Increasing market risks to energy pricing and resilience of energy supply as physical risks increase In magnitude and likelihood over each horizon.

Current opportunity rating

Reducing carbon and enhancing energy resilience and revenue by using and generating renewable energy: Opportunities to lower carbon emissions by using renewable energy and opportunities to invest in renewable energy generation which can lower our carbon emissions, enhance our energy resilience (e.g. less reliance on energy suppliers), and enhance our revenue through sale of renewable energy.
Some examples include:

- South West Water's commitment to purchase 100% renewable electricity from 2022 onwards.
- Generating renewable energy on Pennon's sites and through partnerships (e.g. PPAs) such as through generating energy from wastewater and sludge, and generating electricity through solar and wind.
- Deploying our £160m capital allocation to renewables.
- Switching fuels to lower-carbon sources, such as switching diesel to renewable electricity and HVO as a transition fuel.

Type as defined by TCFD
Markets

Relevant time horizon of risk
Short and medium term
In the short term the opportunity is more focused on financing to achieve Net Zero and current physical risks; over the medium and long term the opportunity will increasingly focus on environmental targets and climate change resilience to long term challenges.

Current opportunity rating

Generating value and reducing our financing costs through sustainable financing: Opportunity to reduce our cost of finance (and avoid cost increases) through access to sustainable financing and generation of green financial assets. Our Sustainable Finance Framework is part of our strategy for taking action on climate change, and our approach is evolving as policy and markets change and information becomes available. We are exploring the implications for our business, including regulatory developments such as the EU Taxonomy/UK Green Taxonomy.

Examples of our actions to mitigate risks and realise opportunities	Primary financial and reputational impacts to our business
Enhancing Pennon's resilience: **Current actions:** • Investment in diversifying water sources, including desalination and repurposing ex quarries and mines • Pursuing new reservoir capacity through regulatory frameworks. • Company resilience planning. • Climate risk assessments and climate adaptation planning. • Engaging stakeholders and regulators and customers. • Investments in response and recovery to operational disruption. • Generation of renewable energy by Pennon, including exploring additional options and power purchase agreements (PPAs) (see our 'market' transition risk). **Future actions:** • Actions to adapt to climate change (e.g. enhancing drought resilience) and to mitigate climate risks. **Enhancing supply chain resilience:** **Current actions:** • Enhancing capacity within Pennon to reduce reliance on suppliers (e.g. generating renewable energy - see our 'energy source' opportunity). • Existing storage and buffers for resources (e.g. chemical storage, parts storage). • Existing diversity in suppliers. **Future actions:** • Actions to enhance supply chain resilience (e.g. diversifying suppliers/ location of suppliers) - see also our actions for managing supply chain under our 'technology' risks. • Procurement strategies (e.g. requirements on suppliers to meet ESG criteria/ low climate risks). • Investments in response and recovery to supply chain disruption.	Potential to reduce and avoid costs (Opex) and enhance our reputation by preventing disruptions to our services. We could also incur reduced penalties/ increased rewards for performance on ODIs (e.g. supply interruptions, leakage, and water quality), therefore increasing our revenue. However, this requires significant investment (Opex and Capex), including strengthening our infrastructure and enhancing our adaptive capacity. Some of these costs could be recoverable through the regulatory system. We will need to manage the carbon footprint associated with schemes related to climate resilience.
Using renewable energy: **Current actions:** • Procurement strategy for renewable energy to minimise the impact of increasing costs of energy. • Supply contract for 100% renewable energy by 2023 for South West Water (currently excludes newly integrated Bristol Water operations). • Generation of renewable energy by Pennon, Including exploring additional options and power purchase agreements (PPAs). • Net Zero programme. • Prioritising investment to deliver highest carbon reduction. • Seeking return on investment (ROI) where possible. • Investment in generating renewable energy. **Future actions:** • Trialling low-carbon fuels. • Innovation programme (e.g. exploring options to generate and recover energy from sewers). • Engagement with potential partners for PPAs. • Establishing the commercial and legal arrangements to co-fund renewable energy investments.	We could incur increased expenditure (Capex and Opex) due to investment in generating renewable energy, however this has potential to reduce our carbon footprint. Some of these costs could be recoverable through the regulatory system). Investment in renewables could reduce expenditure (Opex) in the long term if electricity prices continue to rise (see our 'market' transition risk and 'market' opportunity). We could enhance our revenue through selling renewable energy. We will need to manage the carbon footprint associated with generating renewable energy.
Sustainable finance: **Current actions:** • Sustainable financing framework. • TCFD and TNFD programme. • Investigating requirements to access sustainable finance markets. • Procurement and finance strategies. • ESG initiatives. **Future actions:** • Establishing commercial and legal arrangements for buying and selling green financial assets/credits. • Future disclosure/ESG initiatives (e.g. EU/UK taxonomy, Taskforce on Nature-related Financial Disclosures, ISSB, Transition Plans/TPT). • Exploring opportunities to attract third-party funding.	Through sustainable financing, we have potential to reduce our expenditure by avoiding cost increases related to financing/ cost of capital. We also have potential to enhance our reputation and mitigate reputational risks (see our 'reputation' transition risks).

Key – Strategic priorities					
Risk			Opportunity		
High	Medium	Low	Increasing	Stable	Decreasing

Climate-related opportunities continued

	Potential risks and opportunities
Type as defined by TCFD Resource Efficiency **Relevant time horizon of risk** **Short and medium term** In the short and medium term, investment in resource efficiency Is central to many of our options and decisions In our business plan and WRMP's best value plan. This will enhance our resilience, our ability to meet our environmental and our Net Zero targets and enhance our revenue over the medium and long term. **Current opportunity rating**	**Saving water, energy, materials, and carbon by enhancing efficiency, using low-carbon and nature-based solutions, and reducing emissions across Pennon's supply chain:** Opportunities to invest in enhancing efficiency and reduce wastage of water, energy, and materials, opportunities to use low-carbon construction, approaches, and nature-based solutions, and opportunity to work with suppliers to reduce their carbon footprints and enhance their sustainability. Some examples include: • Pennon's leakage reduction programme, water efficiency programme, smart metering, rainwater harvesting, grey water, incentivising customers to use less hot and cold water. • Enhancing efficiency of process equipment (reducing energy use and chemical use), energy-saving measures for buildings and transport. • Substituting construction materials for low-carbon alternatives, local sourcing of materials, enhancing efficiency of material use in construction. • Using technology to avoid high-carbon interventions, such as using Real Time Control in sewers to increase operational capacity instead of constructing bigger sewers (see also our 'technology' risk). • Constructing wetlands for wastewater treatment and sustainable drainage systems (SuDS) to reduce capital and operational carbon. • Removing carbon from the atmosphere through investing in marine carbon opportunities, restoring peatlands, tree planting, and soil and grassland activities. • Working with suppliers to reduce their carbon footprints and enhance their sustainability, and opportunity to access new suppliers with high ESG credentials.

Examples of our actions to mitigate risks and realise opportunities	Primary financial and reputational impacts to our business
Enhancing water efficiency: **Current action:** • Demand management and water efficiency programme (within Pennon's own operations and across customer networks), including Per Capita Consumption (PCC) reductions and leakage reduction strategy. • Smart metering. • Customer education/outreach. • Communications around carbon. • Farm water efficiency and resilience project – 1,000 pond nature-based solutions. **Future actions:** • Rainwater harvesting, • Incentivising customers to use less water. • Considering applying an internal carbon value to consider full costs and benefits of decisions. • Extend real-time monitoring and control. **Enhancing process, building, and transport efficiency:** **Current actions:** • Actions to enhance process efficiency. • Energy efficiency programme for Pennon's buildings. • Requirements in leases for efficient buildings. • Changes to operational practices to reduce need for travel (e.g. remote monitoring and control). • Procurement/leasing of efficient vehicles. **Future actions:** • Investments in innovation to enhance efficiency. • Changes to operational practices to enhance efficiency (e.g. real time monitoring and control). • Partnerships with suppliers/ outsourcing specific operations. • Employee carpooling. • Light-weighting vehicles. • Considering applying an internal carbon value to consider full costs and benefits of decisions. **Using low-carbon solutions:** **Current actions:** • Implementing capital carbon accounting. **Future actions:** • Net Zero programme (embodied carbon initiatives), • Engagement with supply chain. • Procurement strategies (e.g. requirements on suppliers). • Innovation programme (e.g. exploring alternative materials and approaches). • Collaborations with supply chain (e.g. optioneering to reduce embodied carbon). • Learning from other companies in UK and internationally. • Considering applying an internal carbon value to consider full costs and benefits of decisions. **Using nature-based solutions:** **Current actions:** • Embedding natural capital into decision making. • Investing in innovation and piloting. **Future actions:** • Establishing partnerships with stakeholders (e.g. landowners; see our Upstream Thinking catchment management programme). • Collaborations with supply chain (e.g. optioneering considering nature-based solutions). • Learning from other companies in UK and internationally, • Considering applying an internal carbon value to consider full costs and benefits of decisions. **Reducing supply chain carbon:** **Current actions:** • Engaging with suppliers. **Future actions:** • Procurement strategies (e.g. requirements on suppliers to meet ESG criteria/ low climate risks, reduce emissions), • Learning from other companies in UK and internationally, • Diversifying supply chain to lower emissions/risks, • Sourcing locally where possible. • Life cycle assessment requirements for suppliers.	Potential to reduce our carbon footprint and our Opex in some cases where there are cost savings from resource efficiency. However this requires significant investment (Opex and Capex), including additional monitoring, metering, and capital projects. Some of these costs could be recoverable through the regulatory system. We will need to manage the carbon footprint associated with actions to realise resource efficiency opportunities.

Short-, medium- and long-term horizons

In determining our strategy, we have processes in place for identifying, assessing, and responding to climate-related risks and opportunities. In shaping the strategy, we consider short-, medium-, and long-term horizons.

Short-term – 1 to 10 years
Over this horizon we define key targets (operational, financial, sustainability) and we consider changing regulatory frameworks and emerging Government policies. We develop business plans every 5 years, defining our actions and investments over this period. Operational risks are planned and budgeted for over this time frame and planning begins during this period for the next regulatory period. Our operational Net Zero 2030 commitment falls within this time horizon, as well as the price review in 2029 (PR29). Transition risks and opportunities are likely to have the largest impacts to our business across this period, with physical risks projected to increase over time.
Medium-term – 10 to 30 years
Water and wastewater treatment assets have a typical life of up to 30 years and will therefore be reviewed relative over this horizon. Our WRMP and DWMP strategic plans consider requirements across this period. Major projects and operational plans will be renewed and managed over this time frame to ensure projects meet the correct regulatory period plans. Our 2045 total Net Zero target falls within this horizon, as well as the UK's 2050 Net Zero target, which will continue to present emerging policy and market changes. Transition risks and physical risks will both impact our business across this period to varying levels depending on global GHG emissions and the Net Zero pathway taken by the UK and globally.
Long-term – 30 to 100 years
Typically for longer-term strategic direction, risk, and resilience planning. Investment requirements for our long-life assets are considered such as mains pipes and reservoirs. Over this time period the planet is currently projected to warm by over 3°C, however there is much uncertainty related to the effectiveness of global climate change mitigation. Physical climate risks are likely to have the largest impacts to our business over this time horizon.

Climate scenario analysis

Scenarios

In alignment with the TCFD guidance, we have assessed the risks and opportunities associated with climate change and the transition to a Net Zero climate-resilient economy. We have used plausible contrasting scenarios to explore the potential range of impacts in the future and in turn the possible range in our strategic responses required to mitigate risks and build adaptive capacity in an uncertain future. Our physical risk scenarios are informed by the IPCC's Representative Concentration Pathways (RCPs) from the IPCC's 5th assessment (2014), including a high and a low emissions scenario, which are also used as the basis for planning by Ofwat as part of our PR24 methodology. Our transition scenarios are informed by high and low levels of socio-economic drivers surrounding policy ambition, the speed at which policy is implemented, and the pace of technological advancement, which map onto 'fast' and 'slow' transition scenarios. We have selected these contrasting scenarios as they span a range of possible futures, and present different challenges and opportunities for our business. We will continue to re-visit our scenario analysis in future, including considering the merit in selecting additional scenarios.

Our scenarios can be defined as follows:

Physical risk scenarios

RCP2.6[1]: Lower Physical Impacts

An approximate 2°C warming scenario by the year 2100 – corresponding to a low emissions 'optimistic' scenario.

RCP8.5[1]: High Physical Impacts

An approximate 4°C warming scenario by the year 2100 – corresponding to a high emissions 'business-as-usual' scenario, which is appropriate to use when considering high risks.

Transition risk scenarios

1.5 degree scenario: Fast Transition

A scenario which sees the UK as a global leader with strong policies and actions to mitigate climate, aligned with the Paris Agreement.

Policy ambition
1.5°C

Government policy
Immediate and smooth

Technology change
Fast change

'Current policies' scenario: Slow Transition

A scenario which sees the UK make incremental progress to mitigate climate change, but assumes no major policy changes and results in missing the aims of the Paris Agreement.

Policy ambition
3°C+

Government policy
None – current policies

Technology change
Slow change

Key assumptions

For our scenario analysis, the following assumptions for all scenarios were made:

- Scenarios focus on the UK policy and regulatory context and are semi-independent of global action and temperature pathways.
- It is assumed that the current high energy prices remain high throughout this decade.
- The Government's ambition around environmental protection and conservation remains high, regardless of the pace of transition.
- No significant change to Pennon Group's business activities.
- Population in our region increases by 0.4 million by 2050, overall water demand remains unchanged from today (due to leakage reduction and water efficiency measures), and overall volume of wastewater treated remains unchanged from today (due to actions taken to reduce surface water flows to sewers).

1. The IPCC's Representative Concentration Pathways from the IPCC's 5th assessment (2014)

Physical risks

Approach taken

The Group undertook qualitative scenario analysis in 2021 considering the financial implications of physical climate risks for South West Water under two climate scenarios based on the IPCC's Representative Concentration Pathway (RCP) scenarios. Potential material financial impacts were considered over the 10-year horizon to 2030, aligning with the Group's regulatory financial viability testing. Material impacts on our business and strategy were considered over the time horizon to 2050 – aligning with a medium-term view of climate change impacts before uncertainty increases beyond 2050. We have extended our analysis to cover Bristol Water (acquired June 2021) within this disclosure.

Impacts

This section discusses impacts under each physical risks scenario of RCP2.6 and RCP8.5.

- **Climate resilience will require increased expenditure and investment.** The most significant financial impacts for the Group are on our expenditures (Opex and Capex), to mitigate against future climate risks by increasing capacity for water supply infrastructure; managing drought conditions and water demand; improving water and wastewater treatment and odour management; improving operational resilience to flooding, saline intrusion and storms; and enhancing our Upstream and Downstream Thinking programmes. These financial impacts would be significantly greater under the higher emissions scenario over the long-term horizon as they will require higher levels of adaptive capacity, although adaptive planning will seek to minimise this impact by identifying low-regret options under both high and low emissions scenarios to inform investment decisions. These costs could be recoverable through the regulatory system.
- **Investments in our natural capital will be central to climate adaptation.** Within the water industry, healthy and functioning ecosystems are critical for resilient operations. Therefore, the risks to Pennon's infrastructure are affected by risks to the natural environment. Accordingly, increased expenditures (Opex and Capex) include heavy investment in our natural capital schemes, catchment management, partnerships, and research and development in this area, as well as implementing our comprehensive Biodiversity Strategy and Environment Plan 2050.
- **Climate impacts will affect our ability to meet performance commitments and objectives.** The Group could also be impacted financially by Outcome Delivery Incentive (ODIs) penalties and rewards due to potential failure to achieve performance commitments as part of the regulatory framework, further resulting in negative impacts to our reputation. This impact is more likely under the higher emissions scenario over the long-term horizon due to higher projected magnitude of climate impacts and frequency of extreme weather events.
- **Investment required is high, but the cost of inaction is much higher.** The risk assessment clearly shows long-term significant risks if the impacts of climate change are not mitigated. South West Water operates over £6 billion of water assets and over £7 billion wastewater assets all of which will be affected by climate change in some way. The unmitigated risk would result in additional expenditure (Opex and Capex) to recover from service interruptions and repair or replace deteriorated assets. The unmitigated risk would result in more frequent and greater ODI penalties. Although some of this will be at our Company's expense, wider flood protection investments will be required by others to protect wide-ranging coastal assets.
- **Impacts are worse with every bit of additional warming.** We would experience these impacts for extreme events over all time horizons, however these impacts would increase over each horizon as extreme weather events increase in frequency and magnitude and are compounded by higher average temperatures and drier summer conditions. This trend is more pronounced for the higher emissions scenario, particularly over the long-term horizon, where temperature increases are projected to accelerate.

Our strategic response

Our strategy for managing physical climate risks and financial impacts is underpinned by the following principles in order to maintain and improve our Company's performance to the year 2050:

Adapt to climate change

Enhance resilience

Innovate

Become more efficient

Collaborate

Balance investment

This will require significant action and investment by our Company, as well as action by our supply chain partners and wider actors (e.g. Government agencies, local authorities, and major land owners in SW England).

Longer-term investment, as outlined in our strategic plans, will be needed to manage future risks to acceptable/tolerable levels. The long-term risk is significant and will require additional investment to mitigate their effect. To achieve this, regulatory and Government support within their policy frameworks will be needed.

The combined characteristics of low population density, high coastline to land area ratio and tourism-based seasonal flux on water demand, present a unique set of challenges. Through the years, by innovating, investing, and adapting, we have achieved industry-leading results in many areas of the business. The extensive programme of environmental improvement with Upstream and Downstream Thinking catchment management has resulted in some of the finest bathing waters in Europe. This has been instrumental for us to tackle these challenges and meet the expectations of our customers. Having seen record visitors to our region following the COVID-19 pandemic, it is expected further investment will be required to continue building on the progress made by Pennon Group to protect the environment and our bathing waters.

Our strategic responses within our draft WRMP24 and DWMP23 for delivering reliable, efficient, and high-quality drinking water and wastewater services is driven by best-value adaptive planning, as per Ofwat's final methodology for PR24. This means that, using the same physical scenarios analysed here (RCP2.6 and RCP8.5), our draft WRMP24 has developed adaptive investment programmes which: 1) fulfil immediate and most probable future needs; 2) respond to external pressures in the future with alternative investment options that are triggered under specific conditions; 3) identify low- and least-regret investments that enable future options or return benefits under the broadest range of potential futures. Subsequently, our strategies for mitigating climate risks and building adaptive capacity are similar under the high and low emissions scenario in the short and medium term, however, additional options will be required under the RCP8.5 scenario, or options may need to be implemented earlier than the RCP2.6 scenario over the long term. As part of our adaptive planning approach, we have pre-defined trigger points and decision points to implement strategies of the appropriate pathway sufficiently early, so that we can have a pro-active and more resilient response to climate change - including more opportunity to implement nature-based solutions - rather than more costly reactive approaches which may have higher operational and embodied carbon.

Compared to today, overall our revenue is unlikely to be impacted significantly as we operate in a regulated environment funded through Price Reviews. However, there is a higher risk of reduced regulatory rewards and increased penalties (ODIs) due to climate change. Our operating costs are likely to increase compared to today, and additional capital investment will be required. The value of our assets and our cost

of capital would remain relatively unchanged compared to today if we continue to enhance our resilience.

Transition risks

Approach taken

The Group undertook qualitative scenario analysis in 2022 considering the financial implications of transition climate risks and opportunities for South West Water (including Bristol Water) under the two transition scenarios described earlier. The assessment considered impacts to the year 2030; this time horizon was selected as it aligns with our operational Net Zero target and there is much uncertainty beyond this time with regards to changes to policy, technology, markets, and public opinion.

Impacts - UK Slow Transition scenario

This scenario provides a challenging context for meeting our 2030 operational Net Zero target. In this scenario we have identified the following main impacts for our business:

- **The cost to our business of achieving our 2030 Net Zero target rises, and there is less ability to recover costs through the regulatory pricing system.** This is compounded by the readiness and higher costs for access to low-carbon technologies and related skills (due to the UK's underinvestment in this scenario), and increased costs related to both our own renewable energy generation, and the purchasing of green electricity from external suppliers (where demand is likely to outstrip supply).
- **Meeting our 2030 target requires greater use of carbon offsets.** The enabling environment for decarbonisation is weaker and costs are higher, which leads to slower progress in emissions reductions across our business. As a result, the residual emissions that need to be offset rise, which adds to our costs.
- **Environmental targets require additional energy use.** New guidance on targets for both nutrients and storm overflows will require a significant increase in energy use and associated capital and operational carbon. While nature-based solutions will form part of the solution, there will be significant reliance on engineered solutions due to potential inflexibility in regulation and deadlines to improve outcomes. The increased energy and carbon use compounds impacts above.
- **Reputational risks are significant and require careful management.** Some of our customers and stakeholders may have differing priorities and preferences for actions to meet our 2030 target, for example regarding the increased use of carbon offsets. Some may be highly sensitive to affordability, and increasingly scrutinise our investment choices.
- **Opportunities are lower than the Fast Transition scenario.** Opportunities for our business remain, however, they are in general more limited, and with lower return than in the Fast Transition scenario. Increasing efficiency of energy and resource use, and pursuing low-carbon energy alternatives are the primary opportunities and can help to offset some of the additional energy and carbon costs. There is also an opportunity to clearly identify and communicate the synergies between environmental objectives and the transition to a Net Zero business in order to increase support from customers, stakeholders, and regulators.

Compared to today, overall our revenue is unlikely to be impacted significantly in this scenario, but also our non-water revenue is less able to grow. Our costs to achieve operational Net Zero may increase relative to our current plans, however, early investment in decarbonising the business to meet the 2030 target remains more cost-effective in the long term (post 2030), and reduces the risk to our Company and our customers from measures such as carbon pricing, as well safeguarding our reputation on environment and climate change. The value of our assets and our cost of capital would remain relatively unchanged compared to today.

Impacts - UK Fast Transition Scenario

This scenario is more favourable to our business and to the UK's Net Zero goals, as it creates a more supportive enabling environment to achieve our 2030 operational Net Zero target, however this may present challenges balancing trade-offs between the agendas of Net Zero, climate resilience, environmental protection, customer affordability, and other objectives. In this scenario we have identified the following main impacts for our business:

- **Cost to our business of achieving our 2030 Net Zero target is lower than the Slow Transition scenario.** There is much greater regulatory support in order to support the step change in investment required, with an increase in costs which can be recovered through customers' bills. The maturity of technology and associated business models progresses rapidly, and helps to drive down costs across many areas, including in renewables, resource efficiency, and demand-side measures. Greater R&D programmes with gated investment and piloting will minimise technology investment risks compared to the Slow Transition scenario, where strategies could be more reactive than proactive.
- **Access to the skills and resources needed is costly.** There is very high demand for low-carbon technologies, skills, and expertise across the economy in this scenario, which significantly outpaces supply (partly due to the UK's past underinvestment and the time required to develop supply chains). This adds to our costs associated with decarbonisation, and risks delaying key projects.
- **Environmental targets require additional energy use.** This impact is the same as the Slow Transition scenario, however the regulatory environment may be more favourable for nature-based solutions (NBS) which can also sequester carbon, as there may be more stringent carbon management requirements, and carbon markets would also be stronger and provide more incentives for NBS.
- **Enhanced support to low-income customers may be needed.** Fairness in the distribution of the costs of the UK's transition to Net Zero is a key concern among stakeholders. Increased support to some customers may be required, and our investments will need to be carefully planned and phased to ensure they are efficient and avoid sudden price impacts.
- **Opportunities are higher than the Slow Transition scenario.** The more favourable enabling environment means that our opportunities are enhanced in this scenario, and they are easier to realise. There are particular opportunities to further invest and innovate on energy and resource efficiency, and to attract further investment through sustainable finance opportunities.

Compared to today, overall our revenue is unlikely to be impacted significantly in this scenario, but our non-water revenue has greater potential to grow. Our costs to achieve Net Zero may remain largely unchanged compared to today. The value of our assets may increase as we decarbonise and enhance our natural capital, and our cost of capital may decrease compared to today.

Our Strategic Response

Although there are important differences in the impacts between the different transition scenarios, there are a number of common elements which will require us to implement a common strategic response. The relative importance of each, and specific elements within the response, will vary across the two scenarios, but we have identified six key focus areas which will enhance resilience to transition risks, and better position the Group to take advantage of opportunities:

- **Investing in efficiency.** Under both scenarios there are major carbon savings that can be achieved by increasing efficiency, both in energy use (for example more efficient pumping), reducing water losses, and through the use of smart technology to enable more efficient water supply and transmission systems. Some of these opportunities will also reduce costs. We are currently investing in programmes to further reduce energy use and carbon across our operations. This will allow us to more rapidly progress to operational Net Zero and reduce the cost of the transition.
- **Enhancing our energy resilience.** We will continue to invest in generating our own renewable energy to reduce our exposure to energy prices and to enhance our options for energy supply, which is favourable under both scenarios.
- **Enhancing our access to Green Economy resources.** Across both scenarios there will be a shortage of skills and resources across key areas of the Green Economy that we will need to support our transition. To manage this we will diversify our supply chain of low-

carbon suppliers, and invest in a programme of internal capacity-building to ensure access to the skills needed. We will also work with partners across the industry and engage with peers, regulators, and Government to enable rapid investment in the skills and capacity needed to support Net Zero.

- **Engage and influence environmental targets and trade-offs.** New ambitious targets on nutrients and storm overflows will require increased energy use and new infrastructure, and subsequently higher operational and capital carbon. There is a trade-off between action to meet these targets and action on decarbonisation, with implications for the balance between nature-based, and engineering solutions. We will engage in ongoing consultations on environmental targets and strategies for meeting them, and seek clear guidance on managing different trade-offs. We will advocate for policies which enable flexibility and time to scale up nature-based solutions so we can maximise co-benefits for our customers and the environment.
- **Enhance our stakeholder and customer engagement.** There are significant reputational risks associated with both scenarios, although the balance of concerns will vary. We will develop plans for enhanced programmes of engagement and communication with our customers and stakeholders, in particular focusing on explaining the costs and benefits of the investments we are making, potential trade-offs and synergies between Net Zero and other environmental targets, and affordability.
- **Pursue opportunities to deliver more value for customers and shareholders.** We will continue to pursue opportunities to reduce costs and enhance sustainability. This includes reducing our financing costs through our sustainable finance framework, investing in our environmental programme which includes restoring ecosystems to capture carbon, and working with partners and suppliers to enhance our resilience and reduce emissions across our supply chain. We will also continue to explore opportunities to enhance our revenue through water resource options, selling renewable energy, and markets for bioresources and natural capital.

Statement of resilience

There are clear impacts on our business under different climate scenarios, in particular:

- higher costs in the short term to meet our operational Net Zero target by 2030 under the Slow Transition scenario.
- higher costs in the short, medium, and long term under the RCP8.5 Higher Physical Impacts scenario.

Several of the strategic responses outlined above are already included in our strategic plans and business plan, and we have confidence that our Company has a range of strategic options to manage the impacts, can take advantage of opportunities, and remain resilient under the different climate scenarios considered. Further analysis, including quantitative analysis is planned going forward to enhance Pennon's confidence related to resilience.

There will be the requirement to invest more to improve our resilience to climate change and deliver Net Zero. Assets are likely to require additional protection, and planning for new assets will require a greater level of embedded climate resilience. Significant action and investment will be required by our Company, as well as action by our supply chain partners and wider actors (e.g. Government, local authorities, major landowners/users, other providers of infrastructure and services).

Risk Management

Disclose how the organisation identifies, assesses, and manages climate-related risks.

Recommended disclosures

- **Describe the organisation's processes for identifying and assessing climate-related risks.**
- **Describe the organisation's processes for managing climate-related risks.**
- **Describe how processes for identifying, assessing, and managing climate-related risks are integrated into the organisation's overall risk management.**

The Group's risk management framework is explained in detail on pages 52 to 62, including the methodology for assessing risks.

The Group is continuing to integrate climate-related risk management within the Group's overall risk management process, and climate-related risks and opportunities are assessed using the same methodology as other business risks. In the past few years we have undertaken specific work to identify and assess climate-related risks and opportunities, and we are moving towards this risk identification and assessment being integrated within business subsidiaries/functions. We have the processes in place to enable this integration, and a key area we are continuing to work on is raising awareness and competency so that the key people across our subsidiaries/business functions can effectively identify climate-related risks, like they do with other risks (in many cases, climate risks are an amplifier or additional driver to risks we have already identified, rather than presenting novel risks). This year and last year we convened workshops with senior management from across business functions to re-visit and re-assess climate-related risks and actions, and management will take forward the responsibility to integrate climate-risks into risk registers owned by each business subsidiary/function.

Furthering our progress, the Group has identified several principal risks which are impacted or influenced by physical and transitional climate risks and opportunities, and as such we are increasingly cognisant that climate risk management is integral to the performance and resilience of our business and strategy. The link between climate-related risks and opportunities on our principal risks is summarised in the table over the page.

We recognise the evolving landscape of climate-related risk which is reflected in the changing regulatory frameworks, customer expectations and Government policies that are inherent to our operating context. This is particularly true for climate and Net Zero where new policies and technologies are rapidly emerging, and markets are rapidly changing.

For the climate-related risks that have been identified, a desired 'target' net risk level is documented within the Group's risk framework. This target risk level or tolerance level reflects the acceptable level of risk by the Group and also stands as a target and equitable measure for alleviatory measures to approach the risk going forward. Climate-related risks are approached with a minimal level of appetite, and this is subject to Board approval where all appetite levels are established. The appropriate action then follows from the level of difference between the net risk and the desired risk appetite. Actions to manage risks cover four response types:

- Tolerate: where decisions are taken to tolerate a risk, subject to ongoing monitoring. An example is climate-related risks where uncertainty is high and therefore we might decide to monitor risks until such time as it may be necessary to take further action.
- Treat: where actions are taken to manage and reduce risks, such as implementing operational measures in our drought plan or capital investments to enhance our resilience to droughts.
- Transfer: used where possible to transfer risks to other organisations - such as through insurance or through contracting out responsibilities. We recognise it is not possible to fully transfer risks, rather this approach helps to reduce our exposure. For example, reducing our exposure to the impacts of flooding through flood insurance.
- Terminate: where decisions are taken to stop activities so that we are not exposed to particular risks. For example, we may decide not to undertake a capital project if risks cannot be effectively mitigated - for example due to high costs for energy, materials, and specialist resources related to Net Zero or climate adaptation.

Actions to mitigate risks are allocated to action owners and progress is monitored through the risk review process.

Climate-related risks impact and influence our principal risks

		Physical Risks	Transition Risks
Our Principal Risks	**Law, Regulation and Finance**		
	Changes in Government policy		•
	Regulatory frameworks		•
	Non-compliance with laws and regulations	•	•
	Inability to secure sufficient finance and funding, within our debt covenants, to meet ongoing commitments		
	Non-compliance or occurrence of an avoidable health and safety incident		
	Failure to pay all pension obligations as they fall due and increased costs to the Group should the defined benefit pension scheme deficit increase		
	Market and Economic conditions		
	Macro-economic near-term risks impacting on inflation, interest rates and power prices		•
	Operational performance		
	Failure to deliver the Group's 2023 Net Zero commitment in response to the impact of climate change		•
	Availability of sufficient water resources to meet current and future demand	•	•
	Failure of operational water treatment assets and processes resulting in an inability to produce or supply clean drinking water	•	•
	Failure of operational wastewater assets and processes resulting in an inability to remove and treat wastewater and potential environmental impacts, including pollutions	•	•
	Non-delivery of customer service and environmental commitments	•	•
	Insufficient skills and resources to meet the current and future business needs and deliver the Group's strategic priorities		•
	Business Systems and Capital		
	Insufficient capacity and resilience of the supply chain to deliver the Group's operational and capital programme	•	•
	Inadequate technological security results in a breach of the Group's assets, systems, and data		
We recognise how climate-related risks are impacting our principal risks and/or how our response to these risks needs to consider climate resilience and Net Zero			

Metrics and targets

Disclose the metrics and targets used to assess and manage relevant climate-related risks and opportunities where such information is material.

Recommended disclosures

- **Disclose the metrics used by the organisation to assess climate-related risks and opportunities in line with its strategy and risk management process.**
- **Disclose Scope 1, Scope 2, and, if appropriate, Scope 3 greenhouse gas (GHG) emissions, and the related risks.**
- **Describe the targets used by the organisation to manage climate-related risks and opportunities and performance against targets.**

We are continuing to enhance the metrics we use to quantify key climate risks and to monitor progress towards managing risks and achieving our targeted objectives. We have adopted the TCFD guidance relating to metrics and targets, and our progress is shown in the table below.

We continue to disclose comprehensive data relating to our GHG emissions and energy consumption (SECR report on pages 67). We report on all Scope 3 categories which are relevant and material to our business (ESG databook). SASB reporting can be found on pages 70 to 72.

The Group is committed to improving its sustainability and climate change related disclosures and will continue to enhance this over the coming years.

	Description of the metric	Metric for FY22/23[1]	Trend[2]	Related Targets
GHG emissions	Scope 1, 2, and 3 GHG emissions (in tCO_2e).	290,831	V	Operational Net Zero by 2030 (SWW & BRW), Total Net Zero by 2045 (SWW). Commitment to set Science-Based targets (SBT) for near-term and long-term emissions. Reduce operational emissions by 70% by 2025 (Scope 2 market-based) (tCO_2e).
	GHG Reduction from the baseline year 2021 (Scope 2 market-based) (tCO_2e).	65.7%	V	
	Carbon intensity of our water services in tonnes of CO_2e per megalitre of water supplied to customers.	180.9 SWW 179.1 BRW	V	
	Carbon intensity of our business in tonnes of CO_2e per £100k of our revenue based on Scope 1 and 2 GHG emissions.	7.3	V	
Transition risks Selected metrics for some material risks	Risk of increased energy costs: Proportion of our operational expenditure on electricity (%).	c.28%	V	Purchase 100% renewable electricity by 2022 (SWW). Generate up to 50% of the energy we use through our own renewable energy generation by 2030. (SWW).
	Transition risks in our supply chain: proportion of our key and strategic suppliers who have evidenced they are working towards a Net Zero target.	21% SWW	V	100% of our key and strategic suppliers will have established an ESG policy or equivalent by 2025. (SWW). We are considering setting a target to encourage our suppliers to play their part in delivering Net Zero.
	Risk of customer affordability in achieving Net Zero and adapting to climate change: our customer affordability measure.	96.9% SWW 100% BRW	V	Zero water poverty by 2025 (SWW & BRW).

	Description of the metric	Metric for FY22/23[1]	Trend[2]	Related Targets
Physical risks Selected metrics for some material risks[6]	Proportion (%) of customers currently at risk of severe restrictions in a 1-in-200-year drought.	0	=	Our 2050 target is to achieve 0% of customers at risk of severe restrictions in a 1-in-500-year drought, aligning with Government planning guidance.
	Costs related to managing the current drought and ensuring resilient water supply (£).	c.£19m		
	Proportion (%) of customers at risk of sewer flooding in 2050 in a 1-in-50-year storm.	9.83	V	Our long-term target is to reduce this to zero, assuming funding is provided to achieve this through the regulatory system.
	Number of major sites/assets at high risk of coastal flooding and erosion.	In progress[3]	=	Our long-term target is to achieve 0 of our key sites/assets at high risk, assuming funding is provided to achieve this through the regulatory system
	Annual average number of storm overflow spills from each storm overflow (number per year).	28	V	Reduce spills to an average of 20 per year from each storm overflow by 2025. Zero harm to rivers and seas by 2030.
Climate-related opportunities Selected metric for a material opportunity	Enhancing our energy resilience and reducing our carbon emissions with renewable energy: Amount of renewable energy we've generated in 2022 (kWh).	31,084.05	V	Generate more renewable energy every year to 2030.
	Proportion of our energy use which came from energy we generated ourselves (%)[4]	6.89%	V	Generate up to 50% of the energy we use through our own renewable energy generation by 2030.
	Enhancing our resource efficiency to reduce GHG emissions and save water: • leakage reduction from the baseline 2019/20 year.	9.1% SWW 9.3% BRW	V V	Reduce leakage by 50% by 2050 (from 2019/20 baseline year).
	Per capita consumption (PCC) in litres per day per person.	In Progress	V	6% reduction in per capita consumption by 2024-25 (SWW) based on 2019/20 baseline year.
	Reducing our financing costs through sustainable finance: proportion of new finance under our sustainable finance framework during the year.	100%	V	>75% of new finance to be through sustainable financing framework.
Capital deployment Selected metrics for material capital investments	Investment (£) earmarked for our renewable energy generation capital plans to 2030.	£160m	=	accelerate our generation of up to 50% of the electricity we use through our own renewable energy generation by 2030.
	Additional investment (£) in enhancing resilience and environmental performance announced within the year 2022 on top of our ongoing business plan investment.	£120m	V	
Remuneration	Portion of the majority of our management and employees' incentive schemes linked to ESG outcomes, including climate change.	20%	=	
Internal carbon value	Value of carbon used in business cases and investment planning for PR24 (£/tCO_2e)[5]	£252/tCO_2e Sensitivity testing: Low: £126/tCO_2e High: £378/tCO_2e	=	

1. Some metrics relate only to South West Water (SWW) or Bristol Water (BW). In future we will be aiming to report combined metrics for the water businesses.
2. Indicates the trend from the baseline year.
3. We are currently undertaking analysis to investigate and quantify this risk.
4. Does not include energy used in transport.
5. Investment includes repurposing ex-quarries and mines, introducing desalination units to enhance water capacity, and WaterFit and Green Recovery initiatives.

In our Climate Adaptation Report provided to DEFRA in 2021 it shows intolerable levels of physical climate risks if left unmitigated. In addition, at least 17 of the top 20 physical climate risks (>60 risks identified) would exceed this threshold by 2080 without further adaptation. This signals the need for further investment in climate resilience in future planning rounds.

Our Net Zero carbon commitments will provide a step change to how we run our business and look to manage the risks of climate change, an update on our progress during the last year is found on pages 42 and 43. The metrics and targets associated with this help to show the investment in the area and the planned future investment to meet this goal.

All projects being put forward to the planning committee have a focus on both their carbon impacts and the ESG impacts which are used to manage the decision-making process.

Read more: Net Zero and Streamlined Energy and Carbon Report (SECR) – pages 42 and 67.

Non-financial and sustainability information statement

		Read more	Related policies
Climate and environment	Our ambition is to become Net Zero by 2030. To achieve this, our Net Zero strategy is built around three key pillars - Sustainable Living, Championing renewables, Reversing Carbon Emissions. To deliver on our carbon ambition, and reduce our climate-related risks, we continue to innovate and look for ways to decarbonise our operations, working with partners and supply chain.	• Approach to ESG – page 65. • Our Task Force on Climate-related Financial Disclosures – pages 74 to 95. • Net Zero – page 42 and 43.	• Biodiversity policy. • Water management policy • Environmental policy.
People	Our people are at the heart of our Group. We continue to foster a culture built on our purpose and one that reflects our values, trusted, responsible, collaborative, progressive. We operate a safety-first mindset to working across the business with our HomeSafe health and safety approach which is embedded in the day to day working culture of our business. We encourage continuous learning and development, providing opportunities for all employees. We are building a diverse and inclusive workforce.	• People section – pages 31 to 39.	• Health, safety and security policy. • Code of Conduct. • Workplace policy. • Diversity, respect and inclusion policy. • Board diversity policy.
Social matters	We work closely with our customers, communities and partners on the things that matter most to them and have regular engagement with them. Supporting our customers is a priority. Not only providing safe, clean drinking water, but supporting them financially when it matters most. We aim to keep our bills low and supported c.110,000 customers with their bills during 2022/23. Our approach to community relations and investment enables strong and clear governance, making positive community investments which create value, and benefits both the community and the business. Our Neighbourhood Fund is about supporting our local community. We're funding projects that support the wellbeing of people, the environment and communities in the South West. In 2022/23 we gave £100,000 to 79 community groups in the South West. Community groups can apply for up to £2,000 in funding. Through our corporate sponsorship and donations work we continue to fund a number of local charities, initiatives and events. We committed £136,242 plus VAT in 2022/23. This funding contributes to marine education initiatives with organisations like the Wildlife Trusts, through to funding events and awareness raising with charities such as the RNLI and Surf Life Saving GB. We also work with local community charities such as Devon and Cornwall Food Action.	• Our customers – page 28 to 30. • S172 – page 112.	• Community relations and investment policy.
Human rights	We are committed to having open and fair dialogue with all our stakeholders on human rights issues. We have a zero-tolerance approach to modern slavery. Our policies help prevent and address any human rights impacts on our business activities and relationships. We ensure all of our partners and suppliers comply with our policies, which include our Code of Conduct and Anti-Modern Slavery and Human Rights Policy etc. Our Modern Slavery Statement identifies the activities we conduct annually and our Suppliers Code of Conduct further aligns our supply chain to the standards we expect of ourselves and others.	• Modern Slavery Statement - foot of homepage at www.pennon-group.co.uk.	• Anti-Modern Slavery and Human Rights.
Anti-corruption	One of our guiding principles is to act fairly and responsibly in everything that we do. We are committed to promoting and maintain the highest level of ethical standards in relation to how we do business. We have a zero-tolerance approach to bribery and corruption and have effective systems in place to counter them. Anyone that works with or for the Group must comply with our anti-corruption policy and are encouraged to report any breaches.	• Code of Conduct – page 118. • Anti-bribery and corruption – page 118.	• Whistleblowing Policy. • Anti-Facilitation of Tax Evasion • Conflicts of Interest. • Anti-Money Laundering Policy. • Gifts and Hospitality Policy. • Anti-Bribery and Corruption policy. • Regulatory and Compliance.

The following information and the sections referenced, represent our non-financial information statement which is required by section 414CA and 414CB of the Companies Act 2006. The table below outlines our policies under the sections defined under the non-financial and sustainability information statement, as well as where further information in this report can be found. A full list of the Group's policies can be found online at https://www.pennon-group.co.uk/about-us/policies

Due diligence processes	Policy outcomes	Principal risks	Non-financial KPIs
• Governance framework in place led by the Board and its Committees. • External assurance. • External ESG benchmarking.	• Minimising our impact on the environment. • Meeting our regulatory commitments. • Net Zero 2030 ambition.	• Failure to deliver the Group's 2030 Net Zero commitment in response to the impact of climate change. • Availability of sufficient water resources to meet current and future demand. • Failure of operational water treatment assets and processes resulting in an inability to produce and supply clean drinking water. • Failure of operational wastewater assets and processes resulting in an inability to remove and treat wastewater and potential environmental impacts including pollutions. • Insufficient capacity and resilience of the supply chain to deliver the Group's operational and capital programmes.	• % energy usage from renewable energy generation. • % reduction in GHG emissions (Scope 2 market-based emissions only) • Tree planting.
• Annual all colleague Great Place to Work survey. • Health & Safety Steering Group overseeing targets, performance monitoring and interventions. • Employee representative groups, including RISE and Trade Unions relations. • Change the Race Ratio.	• Reduced workplace. accidents and improved employee wellness. • Board diversity target achievements. • Sustainability target. • Code of Conduct compliance.	• Insufficient skills and resources to meet the current and future business needs and deliver the Group's strategic priorities. • Non-compliance or occurrence of an avoidable health and safety incident.	• LTI number. • GPTW accreditation. • % REACH recruitment. • % female employees. • 5% Club achievement.
• Community engagement plan in place led by Regulatory team.	• Having a positive impact on our local communities through our business activities and investments. • Foster an environment that encourages employee engagement with communities and provides opportunities for volunteering and establishing community partnerships.	• Non-delivery of customer service and environmental commitments.	• £ community investment. • C-MeX. • % priority services register – customer satisfaction.
• Modern Slavery Statement www.pennon-group.co.uk	• An open dialogue with our stakeholders on human rights issues.	• Non-compliance with laws and regulations.	• % Supplier engagement with our Sustainable Procurement Framework.
• New Ethics Management Committee. • Speak Up helpline. • Gifts and Hospitality and Conflicts of Interest procedures. • Group-wide Bribery and Corruption mandatory training. • Supplier due diligence process.	• Seeking to prevent detect and report financial crime, including instances of bribery and corruption. • Maintaining and ethical approach to business and adhering to our code of conduct.	• Non-compliance with laws and regulations. • Inadequate technological security results in a breach of the Group's assets, systems and data.	• Number of cases reported through Speak Up. • % of suppliers who support our Code. of Conduct

Approval of the Strategic Report

Our strategic report on pages 1 to 97 has been reviewed and approved by the Board.

Andrew Garard
Group General Counsel and Company Secretary
31 May 2023

Governance at a glance

Highlights

Board changes

Welcoming two Independent Non-Executive Directors – Dorothy Burwell and Loraine Woodhouse

In December 2022, Dorothy Burwell and Loraine Woodhouse were appointed to the Board as Independent Non-Executive Directors. They both bring a wealth of experience from their roles in other companies.

Read more on their biographies on pages 102 to 104.

Welcoming our new Group General Counsel and Company Secretary – Andrew Garard

On 30 November 2022, Simon Pugsley stepped down as Group General Counsel and Company Secretary. On 1 December 2022, Andrew Garard joined the Group as Group General Counsel and Company Secretary.

Read more on Andrew's experience in his biography on page 104.

Governance updates

Establishment of a Pennon Ethics Management Committee

As part of our commitment to monitoring and improving purpose and culture, during the year we formed a Pennon Ethics Management Committee to assist the Pennon Executive and the main Board in overseeing our culture and commitment to ethical business and integrity, as well as our aspiration to be a great place to work and the best employer in the Great South West.

The Group's core membership is made up of our Group Chief People Officer, Group General Counsel and Company Secretary, People & Culture Director and Head of Legal Compliance.

Their role is to:

- Oversee the Group's ethics and compliance programme including the Code of Conduct.
- Identify general and specific ethics risks and facilitate an organisation and framework for the effective governance and assurance of ethics and compliance (including all associated policies, procedures and controls).
- Oversight of issues logged via the Speak Up line ensuring a consistent and transparent approach.
- Horizon and Group-wide scanning of potential ethics and compliance issues facing the Group.
- Review the Group's progress in living our values and delivering on our purpose.

Key focus areas for the Board in 2022/23

- Supporting customers on low income.
- Drought management and resilience programme including WaterFit.
- Strategic direction 2050.
- Integration of Bristol Water into the Group.
- Culture.
- Environmental performance.
- Operational performance.
- Storm overflows.
- Energy costs.
- WaterShare+.

Board meetings and attendance

There were six scheduled Board meetings during the year.

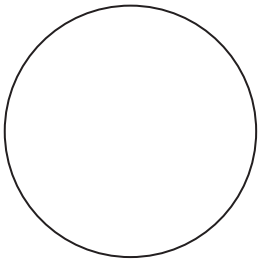
2022	**May** Board and Committee meetings
	July Board and Committee meetings
	September Board and committee meetings plus strategy day
	November Board and Committee meetings
2023	**January** Board meeting
	March Board and Committee meetings

Meeting attendance during the year and Board skills matrix

Position	Chair	Non-Executive Directors						Executive Directors	
Member	Gill Rider	Neil Cooper	Iain Evans	Claire Ighodaro	Jon Butterworth	Dorothy Burwell[1]	Loraine Woodhouse[1]	Susan Davy	Paul Boote
Attendance	**6/6**	**6/6**	**6/6**	**6/6**	**6/6**	**2/2**	**2/2**	**6/6**	**6/6**
Skills									
Independence	✓	✓	✓	✓	✓	✓	✓		
Water sector	✓	✓	✓	✓	✓	✓	✓	✓	✓
Regulation	✓	✓	✓	✓	✓	✓	✓	✓	✓
Finance and Accounting		✓	✓	✓		✓	✓	✓	✓
Strategy	✓	✓	✓	✓	✓	✓	✓	✓	✓
Transformation	✓	✓	✓	✓	✓	✓	✓	✓	✓
Health, safety and wellbeing	✓		✓		✓	✓		✓	
ESG including climate change			✓		✓	✓		✓	✓
Data, technology and digital				✓	✓			✓	
People	✓			✓		✓	✓	✓	✓
Governance	✓	✓	✓	✓	✓	✓	✓	✓	✓
Remuneration	✓			✓			✓		

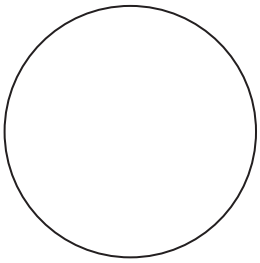
1. Were appointed 1st December 2022.

Board gender diversity as at 31 March 2023



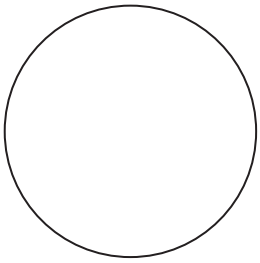
- Male: **44%**
- Female: **56%**

Board ethnic diversity at 31 March 2023



- Of ethnic minority: **22%**
- White: **78%**

Board tenure as at 31 March 2023



- 0 - 3 years: **3 Directors**
  Paul Boote, Dorothy Burwell, Loraine Woodhouse
- 3 - 5 years: **3 Directors**
  Jon Butterworth, Iain Evans, Claire Ighodaro
- 5+ years: **3 Directors**
  Neil Cooper, Susan Davy, Gill Rider

In numbers

14th

Ranking overall in FTSE 250 Women's Leaders Review, 1st in the utility sector.

1 in 14

number of households in the South West Water region now shareholders following the second issuance of WaterShare+ in 2023.

Chair's introduction to governance

Gill Rider
Chair

"Engaging with all our stakeholders has never been more vital."

Dear Shareholder

I am very pleased to introduce, on behalf of the Board, the Pennon Group Corporate Governance Report for 2023. We provide detail around our governance practices and processes, and how we apply the principles of best practice in corporate governance. It also covers our key focus areas and achievements during 2022/23 and explains how the Board continues to support the Group's strategy. The Board reaffirms its commitment to maintaining the effective corporate governance and integrity that enable us to deliver our sustainable strategy for the long-term benefit of all our stakeholders.

Review of the year

Our well-established governance arrangements and processes enabled the Board and its Committees to operate effectively and efficiently throughout the year. As well as physical Board meetings we also held several ad-hoc virtual meetings, enabling us to communicate more frequently and to give management our advice and support more often.

Strong governance remains central to the successful management of the Group, providing the framework we collectively need to deliver our strategy, effectively fulfil our purpose, create value for all our stakeholders and continuously develop of our sustainable business. We continue to operate to the highest standards of corporate governance. Our Board composition is substantially ahead of the diversity targets suggested by the Parker Review and the FTSE Women Leaders Review. And our ESG targets, which include our commitment to achieving Net Zero by 2030, remain well ahead of many companies in the FTSE 250.

Throughout 2022/23 we focused on achieving our strategic priorities while ensuring a robust response to the drought conditions that affected the environment as well as many of our customers and communities. Management kept us well-informed on progress against the Group's strategy and about the measures taken to mitigate the impact of the year's historically low levels of rainfall.

The table on page 111 will help you to navigate our reporting and evaluate our performance against the Principles of the UK Corporate Governance Code 2018 (the UK Code). As we explain below, we also have processes and procedures in place to safeguard the independence of decision-making by the Boards of South West Water and, prior to its integration with South West Water, Bristol Water.

Promoting diversity

Diversity and inclusion (D&I) continues to be a top priority for the Board and the Group,. As a whole it is encouraging to see our CEO recognised for her work in this area. Our gender and ethnic diversity representation on the Board exceeds the Hampton-Alexander and Parker targets. Our commitment to diversity is also reflected right across the business; our widespread commitment and focused drive to recruit talent from all backgrounds has the heartfelt support of our strong and diverse leadership team.

Engaging with our stakeholders

Engaging with all our stakeholders has never been more essential, particularly in view of the national and global issues we are facing. All companies in the water sector face much scrutiny around their environmental impacts, so it is vital that we listen to and respond to our stakeholders' views. We make sure to carefully consider all decisions and their likely impacts on our stakeholders. And we ensure through our stakeholder engagement programme that everyone has the opportunity to provide feedback to the Board.

We continue to foster an open and transparent feedback culture within the business. All colleagues have the opportunity to share feedback with the Executive team and Board in several ways, including the Big Chat initiative, our Great Place to Work survey and our new Employee Forum RISE.

You can read more on how we engage with our stakeholders in our Section 172(1) statement on page 112.

Culture

As a Board we pay particular attention our Group's culture, ensuring it is fully aligned with our shared purpose, values, and strategy. We continue to monitor these essential properties and receive regular reports from management on the work being done to ensure continuous improvement.

Role of the Board and its effectiveness

It is my view that the Board continues to be highly effective with a deep understanding of the opportunities available to us and the threats facing the business. The results of this year's Board and Committee performance evaluations support this view; see page 117 for further detail. We keep all identified threats to the future success of the business under constant review. Please see our risk report on pages 52 to 62 for a description of the risks we identify and review.

Board independence – Pennon, South West Water and Bristol Water

In accordance with Ofwat's principles on board leadership, transparency and governance, the Group maintains separate Boards for Pennon and South West Water including Bristol Water following licence consolidation.

Our system of governance remains appropriate and effective, while continuing to support the delivery of our strategy.

Our Board and Committee framework also allows us to remain efficient in our decision-making processes. The South West Water Board convenes on the same day as each Pennon Board meeting and considers all key relevant issues. This arrangement allows full operational oversight and governance by the Boards over the Group's water interests, while the Pennon Board continues to focus on strategic forward-looking matters for the Group as a whole.

Changes to the Board

We are delighted to welcome two new Non-Executive Directors, Loraine Woodhouse and Dorothy Burwell to the Board. Both Dorothy and Loraine bring a wealth of experience and I look forward to working with them to promote the success of the Group. You can find more details on our new appointees on page 104.

In December 2022, we also welcomed Andrew Garard as Group General Counsel and Company Secretary to continue supporting the Board, succeeding Simon Pugsley. I'd like to thank Simon for his continued support of the Board and his valuable contribution to Pennon Group during his 24 years with the business.

A review of the composition of each Board Committee was conducted in December 2022, with changes becoming effective on 31st January 2023.

Neil Cooper will be standing down from the Board in September 2023 and we set out details on the process to recruit his successor in the report of the Nomination Committee on pages 128 to 131. I'd like to thank Neil for his contribution to the Board over the last 8 years and wish him well for the future.

Looking ahead

As part of our focus for 2023/24, we will continue to embed Bristol Water into the Group. We will focus on delivering against our environmental commitments, and ensuring we are well placed to meet the vital ambitions of the PR24 framework. And, as we look to our governance arrangements, we will continue with our ongoing and orderly succession planning strategy. There is much to do, and we have the talent and governance in place to achieve our ambitions.

I will be standing down as Chair, and from the Board, in 2024 and the search for my successor will begin later in the year. As for all new Board appointments, these will be managed under a formal, rigorous and independently conducted process, in line with the UK Corporate Governance Code.

I would like to take this opportunity to thank my Board colleagues, the management team and our wider workforce for their outstanding work over the year just gone. We will continue to focus on delivering against our strategic priorities in the year ahead, ensuring the wellbeing of our workforce as we build on the work of the last year in creating a successful and sustainable business.

Gill Rider
Chair

31 May 2023

Compliance with the UK Corporate Governance Code 2018 and other requirements

We continue to apply and comply with the 2018 UK Corporate Governance Code (the UK Code) in all our business activities. We believe that strong corporate governance is fundamental to our business, assuring our stakeholders that we act with their best interests in mind and to ensure long-term sustainable value that benefits everybody.

We provide details of how we have applied the principles that form the UK Code throughout this report; the table below provides some useful signposting. The Board confirms that throughout the year under review (and up to the date of this report), the Company has complied with all the relevant provisions of the UK Code. You can find information on the tenure of the Chair of the Board and succession planning on page 117.

The UK Code is published on the Financial Reporting Council (FRC) website. The introduction to this Corporate Governance report and the following sections have been made in accordance with the UK Code, Financial Conduct Authority (FCA) Listing Rule 9.8.6 and FCA Disclosure and Transparency Rules 7.1 and 7.2. They cover the work of our Board and its Committees, our internal control systems and procedures including risk management, our statements relating to share capital and control, our confirmation of the Company as a going concern and our Directors' responsibility statements. Finally, in accordance with reporting requirements, on page 125 the Board can confirm to shareholders that the Annual Report and Accounts taken as a whole is fair, balanced and understandable and provides the information necessary to assess the Company's position, performance, business model and strategy.

To read more on how we have applied the UK Code:

Board leadership and company purpose	Composition, Succession and Evaluation
Role of the Board – page 107	**Appointments and succession planning –** page 128
Purpose, values and monitoring culture – page 109	**Board composition –** page 116
Stakeholder and shareholder engagement – page 110	**Board evaluation –** page 117
Risk management – page 118	
Policies and practices – page 107	
Division of Responsibilities	**Audit, Risk and Internal Control**
Role of the Chair and Non-Executive Directors – page 114	**Committee roles –** page 107
Committee responsibilities – page 107	**Our approach to risk management –** page 118
Remuneration	
Remuneration report – page 136	

The Board

Working responsibly together

Gill Rider CBE E H N A R

Chair

Appointment to the Board

Gill was appointed to the Board as Non-Executive Director on 1 September 2012 and became Chair on 31 July 2020.

Current external appointments

Non-executive director and Chair of the Remuneration Committee of Intertek Group plc, President of the Marine Biological Association.

Skills and experience

Gill has a wealth of experience in leadership and governance across a broad range of sectors including professional services, education, not for profit and government. Formerly, Gill was Head of the Civil Service Capability Group at the Cabinet Office, reporting to the Cabinet Secretary. Prior to that, she held a number of senior positions with Accenture LLP culminating in the post of Chief Leadership Officer for the global firm. She was previously President of the Chartered Institute of Personnel and Development (CIPD) and Chair of the Council of the University of Southampton.

Susan Davy E H

Group Chief Executive

Appointment to the Board

Susan was appointed to the Board in February 2015 as Chief Financial Officer, having joined the Group as Finance Director of South West Water in 2007. Susan was appointed Group Chief Executive on 31 July 2020.

Current external appointments

Non-Executive Director, Audit Committee Chair and member of the Nomination and Remuneration Committees of Restore plc. Board member of Water UK and member of the Energy & Utilities Skills Partnership Council.

Skills and experience

Susan's knowledge of the industry, coupled with her financial and regulatory expertise, has underpinned the development of Pennon's strategy to become a leader within the water industry. Under Susan's leadership, the Group has expanded and taken a more water focused approach, through the disposal of Viridor, acquisition of Bournemouth Water and the most recent acquisition of Bristol Water.

In her 25+ years' experience in the utility sector, Susan has also held a number of other senior roles in the water sector, including at Yorkshire Water, giving her the knowledge to provide stability and thoughtful leadership to the Group.

Under her guidance, South West Water has become the only water company to have achieved fast-track status for two consecutive business plans – the first in 2014, the second in 2019.

Paul Boote E H

Group Chief Financial Officer

Appointment to the Board

Paul was appointed to the Board as Group Finance Director on 8 July 2020, having joined Pennon on 1 January 2010. Paul became Group Chief Financial Officer in September 2022.

Current external appointments

None

Skills and experience

Paul is a chartered accountant with over 20 years' experience. He has held several senior roles at Pennon, including Pennon's Director of Treasury, Tax and Group Finance. During this time, he was responsible for the development of Pennon's sector-leading sustainable debt portfolio, ensuring the Group maintained a responsible approach to tax, as well as leading on financial reporting matters.

Paul has also held senior finance roles at companies operating in the sport, construction, and environmental infrastructure industries.

Neil Cooper A E H N R

Senior Independent Director

Appointment to the Board

Neil was appointed to the Board as Independent Non-Executive Director on 1 September 2014 and became Senior Independent Director on 31 July 2020.

Current external appointments

Neil is currently the Chief Financial Officer of Currencies Direct, a foreign exchange broker and international payment provider.

Skills and experience

Neil brings to the Board extensive experience in a wide variety of corporate and financial matters. Previously, he was group finance director of Barratt Developments plc and before that, group finance director of William Hill plc and Bovis Homes plc. Neil also held senior finance positions at Whitbread plc, worked for PricewaterhouseCoopers as a management consultant and held several roles with Reckitt & Colman plc.

As Chair of the Audit Committee, Neil has been influential in directing Pennon's approach on several significant matters including internal control, governance and financial reporting.

Committee key

A Audit Committee | E ESG Committee | H Health & Safety Committee | N Nomination Committee | R Remuneration Committee | ■ Chair of Committee | ● Attended

Iain Evans CBE A E H N R

Independent Non-Executive Director

Appointment to the Board

Iain was appointed to the Board as Independent Non-Executive Director on 1 September 2018.

Current external appointments

Iain is a non-executive director of Bologna Topco Limited and HSM Advisory Limited and continues to act as an independent corporate strategy consultant.

Skills and experience

Iain has 40 years of extensive global experience in advising companies and governments on issues of complex corporate strategy. In 1983, he co-founded L.E.K. Consulting in London and built it into one of the world's largest and most respected corporate strategy consulting firms with a global footprint active in a wide range of industries.

Iain was appointed as a non-executive director of Welsh Water plc in 1989 and served on the board for nearly ten years, including five years as chair.

As chair of the ESG Committee, Iain is leading the development of a sustainability programme that underpins the delivery of Pennon's strategy.

Claire Ighodaro CBE A E H N R

Independent Non-Executive Director

Appointment to the Board

Claire was appointed to the Board as Independent Non-Executive Director on 1 September 2019.

Current external appointments

Chair of the Audit Board of KPMG LLP.

Skills and experience

Claire has held a number of senior roles and directorships with UK and international organisations and has extensive board experience, serving on their audit, remuneration and governance committees.

She is a past president of the CIMA (Chartered Institute of Management Accountants) and was the first female to lead this organisation. Claire spent most of her executive career with BT plc. She has also held non-executive directorships across a diverse portfolio including Governance Committee Chair of Bank of America's Merrill Lynch International, Audit Committee Chair of Lloyd's of London, Flood Re, The Open University and various UK public bodies including UK Trade & Investment and the British Council. Claire was also Non-executive Chair of the Board and Governance Committee at Axa XL – UK Entities until December 2022.

As Chair of the Remuneration Committee, Claire continues to guide Pennon's approach to executive remuneration, ensuring that it is aligned with and supports the Group's strategy and reflects the wider economic market.

Jon Butterworth A E H N R

Independent Non-Executive Director

Appointment to the Board

Jon was appointed to the Board as Independent Non-Executive Director on 8 July 2020.

Current external appointments

Chief Executive Officer at National Gas. Jon is also President of the Pipeline Industries Guild and a director of E.Tapp & Co Limited, Shopfittings Manchester Limited and TMA Property Limited.

Skills and experience

Jon has a distinguished track record and an immense depth of experience and knowledge within the utility sector, having begun his career over 40 years ago as an apprentice at British Gas. Jon was previously Managing Director of National Grid Ventures, driving growth across a range of commercial ventures outside the regulated energy sector in the UK and the US. He has also been the Managing Director of Northwest Gas, Global Environment and Sustainability Manager of Transco, National Operations Director of National Grid, Group safety, Resilience and Environmental Director of National Grid plc and formerly CEO of National Grid Ventures, building (£3 billion) of growth in renewables across the USA and Europe.

Jon's utility background makes him keenly aware of the importance of maintaining a balance between performance and safety. As Chair of Pennon's Health & Safety Committee, he constructively challenges the Board and management team, to continue to raise the bar in this area. He is an Ex-Chair of the CORGI Board, an Ex-Ambassador of the HM Young Offenders Programme and a trustee of the National Gas Museum Trust.

Dorothy Burwell A E N R

Independent Non-Executive Director

Appointment to the Board

Dorothy was appointed to the Board as Independent Non-Executive Director on 1 December 2022.

Current external appointments

Partner and Global Partnership Board Member of FGS Global, Non-Executive Director at Post Holdings, Inc, Trustee of the Consumers' Association charity, Which?.

Skills and experience

Dorothy has over 20 years experience in Banking and Communications, specialising in natural resources and advising clients around issues on sustainability, strategy, and corporate communications. She is well known for driving substantive diversity and inclusion agendas.

Between 2002 and 2006, Dorothy held analyst and senior roles at Goldman Sachs in the Investment Banking Division in both London and New York as well as in the firmwide Strategy group, where she focused on proprietary mergers and acquisitions and new business development.

Dorothy graduated from the Florida Agricultural and Mechanical University, USA with a Bachelor and Master of Business Administration, Finance and Management.

Loraine Woodhouse A E H N R

Independent Non-Executive Director

Appointment to the Board

Loraine was appointed to the Board as Independent Non-Executive Director on 1 December 2022.

Current external appointments

Non-Executive Director of The Restaurant Group plc and a member of their Audit, Remuneration and Nomination Committees, Non-Executive Director and Chair of the Audit Committee at British Land plc.

Skills and experience

Loraine is an experienced finance executive, with her experience focused in the retail and consumer sector, and more recently in real estate and infrastructure through her roles with Intu Properties plc and British Land Company plc.

Loraine was the Chief Financial Officer of Halfords Group plc for just under four years until June 2022, before which, she spent five years in executive and senior finance roles within the John Lewis Partnership, including Waitrose.

Prior to that, Loraine was Chief Financial Officer of Hobbs, Finance Director of Capital Shopping Centres Limited (subsequently Intu Properties plc) and Finance Director of Costa Coffee Limited.

Andrew Garard

Group General Counsel and Company Secretary

Appointment to the Board

Andrew was appointed to the Board as Group General Counsel and Company Secretary on 1 December 2022.

Current external appointments

Non-Executive Director at Zinc Media Group plc where he is Chair of the Remuneration Committee

Skills and experience

Andrew is a very experienced General Counsel having joined from Meggitt PLC where he was Group General Counsel and Director, Corporate Affairs, and a member of the Group Executive responsible for legal, commercial, trade compliance, government relations, ethics and contract management.

Previously, he was Group General Counsel and Company Secretary at ITV plc where he was a member of the Executive Board and led a global team responsible for legal and business affairs, secretariat, compliance, insurance, health & safety, rights management and corporate responsibility. Prior to this, he was Group General Counsel at Cable & Wireless plc and Head of Legal at Reuters Group plc.

Andrew founded the Legal Social Mobility Partnership in 2014 before creating the Social Mobility Business Partnership in 2017.

Committee key

A Audit Committee | E ESG Committee | H Health and Safety Committee | N Nomination Committee | R Remuneration Committee | ■ Chair of Committee | ● Attended

The Executive Team

Susan Davy

Group Chief Executive

See biography on page 102

Paul Boote

Group Chief Financial Officer

See biography on page 102

Adele Barker

Group Chief People Officer
BA hons, PCEC

Adele joined the Group in 2017 and was appointed Group Chief People Officer on 31 July 2020. Adele supports the Remuneration, Nomination, and Health & Safety Committees. Her areas of accountability include the Group wide Human Resources function, Health and Safety and Corporate Communications. Her background includes senior roles in FTSE organisations including British Gas, Barclays and Marks and Spencer.

Andrew Garard

Group General Counsel and Company Secretary

See biography on page 104

John Halsall

Group Chief Operating Officer

Appointment: February 2023

Experience: Before joining the Group, John was Regional Managing Director (Southern) for Network Rail for 14 years. Prior to that, he spent 17 years at Thames Water in various senior operational roles including Director of Water Services and Director of Operations.

Laura Flowerdew

Chief Customer and Digital Officer

Appointment: September 2022

Experience: Laura was Chief Financial Officer of Bristol Water plc from 2018, before taking on her new role within the Group after the Bristol Water acquisition. Laura continues to be a director of Pelican Business Services (billing and customer services across both Bristol Water and Wessex Water), a role she has held since 2019.

Lisa Gahan

Group Director of Regulation, Strategy and Asset Management

Appointment: Joined South West Water in 2021 and became Group Director of Regulatory, Strategy and Asset Management in September 2022

Experience: Prior to joining the Group, Lisa was a founding partner of ICS Consulting, where she spent over 20 year helping utilities organisations with economic regulation, customer engagement, and investment and strategy planning.

Richard Price

Chief Engineering Officer

Appointment: September 2022

Richard has previously held the roles Operations Director and COO in Bristol Water before becoming Chief Engineering Director for Pennon in September 2022. Before joining Bristol Water, Richard held extensive roles at Southern Water and so has in depth knowledge about the water industry. Richard's role within Pennon is to lead safe, efficient and innovative engineering and construction across the greater South West region.

David Harris

Group Drought and Resilience Director

Appointment: November 2022

He leads the organisation's drought planning activities as well the ongoing development of our longer term resilience.

With over 25 years of executive experience, David has successfully led performance and growth of large infrastructure businesses, both in the regulated water market and the competitive energy market in Australia. David brings experience from his time leading one of Australia's largest water companies through the worst droughts in the country's history, ensuring the constant supply of drinking water and the building of additional water resources.

Porthminster Beach, Cornwall

Board Leadership and Company Purpose

Governance structure and framework

Pennon Group plc Board

The Board is responsible for providing leadership and oversight of the Group's business, strategy and associated activities including promoting its long-term success. The Board's responsibilities include setting the Group's values, policies and standards, approving Pennon's strategy and objectives, and overseeing the Group's operations and performance. The Board makes decisions in relation to the Group's business in accordance with its schedule of matters reserved.

WaterShare+ Panel

CEO and Pennon Executive (PEx)

Responsible for defining and driving the business priorities that will achieve delivery of the Group's strategy and ensuring, to the extent of the authority delegated by the Board, the proper and prudent management of Group resources to create and maximise shareholder value while protecting the interests of the wider stakeholder group. Chaired by the Chief Executive Officer, the Executive meets regularly to receive reports from the management committees and to review and refine recommendations to be presented to the Board.

Ethics Management Committee

Water Business Review Meeting

Drought and Resilience

Investment Planning Committee

Pennon Group plc Committees

The terms of reference for each Committee are agreed by Board and can be found at https://www.pennon-group.co.uk/about-us/board-committees.

Audit Committee

Ensure the quality and integrity of the Group's financial reporting, assessing the application of accounting policies given underlying standards, probing and testing accounting judgements made in preparing financial reporting and evaluating whether the presentation of the Group's activities is fair, balanced and understandable.

Review and challenge the ongoing effectiveness of the internal control environment and the scope and adequacy of risk management processes across the Group.

Disclosure Committee

Draw up and maintain procedures, systems and controls for the identification, treatment and disclosure of inside information and for complying with other disclosure obligations falling on the Group.

Monitor compliance with the disclosure procedures and keeping the adequacy of these procedures under review.

ESG Committee

Ensure robust scrutiny of key aspects of environmental, social and governance (ESG) performance and to oversee Pennon's performance against its ESG strategy and strategic sustainability objectives.

Health and Safety Committee

Provide a 'review and challenge' function to support the Board and the Executive on all matters connected to health and safety including the deployment of the health and safety strategy, resilience and process safety.

Nomination Committee

Regular review of the structure, size and composition (including the skills, knowledge, independence, diversity and experience) required of the Board, compared to its current position and the skills and expertise needed in the future.

PR24 Committee

Plan, prepare for, oversee and drive the PR24 Business Plan, set and approve strategy for PR24, and appoint and oversee relevant executive committees and activities to ensure the delivery of the plan in line with the overall Group strategy.

Remuneration Committee

Ensure remuneration is aligned with the Group's strategy and reflects the values of the Group.

Advise the Board on the framework of executive remuneration for the Group and for the wider workforce.

Key activities of the Board in 2022/23

The key activities that were carried out by the Board during the year, together with an indication of the stakeholders affected and whose interests the Board considered in its discussions and decision-making are set out below. In 2022/23, the Board has considered a wide range of matters to meet its obligations.

Inform
Senior Leaders and management prepare written reports in advance of Board meetings as well as deep-dive presentations on key areas of the business = to inform and make recommendations for the Board's consideration. In addition, regular performance reports are shared with the Board to ensure they are continuously informed.

The agenda is agreed with the Chair in advance in conjunction with the CEO and Group General Counsel and Company Secretary.

Recommend and consider
Recommendations and deep dives from Senior Executives as well as external advisors to facilitate decision-making and accounting for stakeholder impact are presented to the Board for consideration.

Approve and action
The Board will consider matters and agree and approve actions to take forward.

Supported by: Operational site visits / Governance, legal and regulatory updates

Activity	Stakeholder link
Strategic	
Strategic direction through to 2050 Reviewing and approving the strategic direction through to 2050. Agreeing eight priorities and the enablers for change required to achieve these priorities.	Customers, People, Environment, Regulators
Bristol Water integration Reviewing the progress of the integration into South West Water and the need for a merged licence. Authorising the final steps to be taken to affect the integration.	People
Delivery of capital projects Reviewing and agreeing a new framework model for capital delivery. Implementing a new tender process to attract new partners into the delivery model.	Suppliers
Financial	
Reviewing and authorising the 2021/22 Annual Report and Accounts The payment of a final dividend of 26.83p per share and the holding of a successful Annual General Meeting.	Investors
Energy costs Reviewing the impact of higher power costs on operating costs. Identifying options to bring power and energy efficiencies across all assets.	Suppliers
WaterShare+ Approval of the special WaterShare+ resolution to shareholders at the 2022 AGM enabling the execution of the second issuance of the scheme. Approval of c.£20m to fund both the payment of the dividend to fund the share purchase, and the application of bill reductions, for both South West Water and Bristol Water customers.	Customers
Operational	
ODI improvements Meeting regulatory requirements, ongoing regulatory/innovation initiatives, monitoring via H&S reports and adapting plans where needed. Successful regulatory outcomes, safe customer and employee experience, enhancing day-to-day operations.	Customers, People, Environment, Regulators, Policy makers
Water Resource Management Reviewing the Water Resource Management Plan which sets out how the Company will ensure it meets demand for water over the next 25 years in line with Department for Environment, Food and Rural Affairs (DEFRA) and Environmental Agency (EA) requirements. Noting options for getting our specific strategic resource and demand plans onto the political agenda and for reducing per capita consumption to 110 l/day.	Environment

Activity	Stakeholder link
Environmental	
Drought management Reviewing the response to the drought given the dry and hot weather. Accelerating all engineering options, increased customer and water-saving communication and enhanced stakeholder engagement. Submission of Drought Order for Cornwall and instigation of a customer bill support initiative.	Environment, Customers, People, Regulators
Net Zero strategy, Pollution Incident Reduction Plan Green, Recovery investment programme and Environmental Plan Implementation and monitoring of each of the plans and adapting each where needed. Alignment of plans with our strategic priorities. Committing to key pledges. Delivery to achieve ever more stringent targets as well as greater public/regulatory scrutiny. Reinvestment of funds previously identified as wastewater efficiencies.	Environment, Customers, People, Regulators, Investors
Social	
Purpose and culture Reviewing the results of the Great Place to Work survey. Agreeing the next steps to improving purpose and culture and considering why scores around integrity and values were lower than the previous year. Identifying the types of training and competencies needed to support the business in its future development.	People
Supporting customers on low income Monitoring of customer service levels and plans to deliver improved diversity mix and adapting where needed. Continued alignment of plans to achieve ever more stringent targets as well as greater public/regulatory scrutiny.	Customers
Governance, Compliance, Legal and Regulatory	
Regular updates on Corporate Governance and key legal developments during the year. Continued alignment of plans to ensure appropriate compliance/ best practice governance.	Environment, Customers, People, Communities, Suppliers, Investors, Regulators, Policy makers
Risk	
Mitigation of key risks Ongoing focus on key risks, with deep dives at Audit Committee meetings. Continued alignment of plans to ensure appropriate risk mitigation	Environment, Customers, People, Communities, Suppliers, Investors, Regulators, Policy makers

Legend

Environment, People, Suppliers, Regulators, Customers, Communities, Investors, Policy makers

Monitoring purpose and culture

Monitoring and measuring the Group's purpose and culture is a key focus area for the Board. Our organisation couldn't deliver without our c.3,000 colleagues. Our purpose, ***Bringing water to life – supporting the lives of people and the places they love for generations to come*** underpinned by our values that we live by – trusted, responsible, collaborative, progressive – governs how we operate, behave and foster a diverse and inclusive culture. Everything we do, we do with our stakeholders in mind, be it offering our customers financial support when needed, providing help and funding for community initiatives, working with our regulators and the Government on ensuring the future is sustainable, celebrating and rewarding our colleagues or finding innovative ways to protect our environment.

Underpinned by the values we live by

Trusted –
we do the right thing for our customers and stakeholders

Responsible –
We keep our promises to our customers, communities, and each other

Collaborative –
We forge strong relationships working together to make a positive impact

Progressive –
We are always looking for new ways to improve and make life better

New employee panel – RISE

In June 2022, we launched our new people panel, RISE which aims to be a two-way, open and honest communication forum to discuss business topics and ensure that the views and opinions of colleagues are shared with the company. The RISE forum now has over 100 members stretching across all areas of the business.

Twice a year, RISE members meet with our CEO, Susan Davy and our Group Chief People Officer, Adele Barker to discuss feedback and ideas from across the business. The first one took place in January 2023 with seven RISE representatives.

This is a great opportunity for Susan and Adele to understand what is happening and what's important for our colleagues. Topics like wellbeing and mental health, cost of living, communication and hybrid working are just some of the topics covered with actions and responsibilities agreed to drive progress over the next quarter.

Our Executive team visiting Knapp Mill Water Treatment Works, Bournemouth

Stakeholder engagement

The Board understands the role the Group has to play in creating a more sustainable South West and UK as a whole. We are committed to carrying out our business in a responsible way and to continuously improving how we provide all our services for the benefit of all our stakeholders.

Our Section 172(1) statement describes in more detail how the Board considers the interests of all our stakeholders when carrying out its duties. This statement is on pages 112 and 113; you should read it alongside the sections on pages 27 to 39 to understand how the Board took stakeholder interests into consideration in all its decision-making during the year.

We actively engage with all our stakeholders, including our customers, our communities, our people, our suppliers and our investors. We are acutely aware that many of our stakeholders are struggling with the uncertainty posed by the cost -of-living crisis, the political landscape and wider economic environment.

We are committed to maintaining appropriate and regular dialogue to ensure our strategy and our performance objectives always reflect our stakeholders' expectations and needs. Our continuous engagement allows stakeholders to give feedback on matters they consider of importance to them and raise any issues which they would like to be addressed.

For engagement with the workforce, the Board has decided at this time not to adopt any of the three specific employee engagement methods referred to in the UK Code. Instead, our chosen method is to adopt a more enhanced approach which includes the conduct of a periodic 'Great Place to Work' engagement survey (including related management feedback sessions) and continuous employee feedback through our own in-house forums. These comprise our new RISE people panel, which has recently replaced our employee engagement forum, and the 'Big Chat', hosted by the Executive team. These forums not only give employees access to important up-to-date information on key business events; they also provide the opportunity to hear from the Directors, give feedback and ask questions. The Board believes Pennon's chosen approach is an effective way of communicating with employees and gathering essential feedback from across the business. This empowers the Board to consider the interests of all employees in its discussions and decision-making. You can find further information on employee engagement on pages 31 to 39

Shareholder and investor engagement

Shareholders are one of our key stakeholder groups and we continued to manage a comprehensive engagement programme with them throughout the year.

Members of the Executive met with 71% of our institutional investors during 2022/23, as well as attending 10 roadshows, events and conferences for investors, in North America, Australia and Europe. Alongside this programme, we also hosted a Spotlight Presentation and live Q&A in April 2022 – with focus on investing for sustainable growth. We also held 95 meetings and calls with current and prospective investors alike.

Pennon Group maintains a stable shareholder register of which around half of investors are based in the UK. Institutions hold the majority of our issued share capital, with the remainder largely held by private client investment managers. A small proportion is held by retail investors.

The Group Chief Financial Officer and Group Head of Investor Relations report regularly to the Board on the views of major shareholders, about the Group. To ensure the Board is always fully briefed on shareholder views and aspirations, our corporate brokers present frequently to the Board on equity market developments and shareholder perceptions.

Engaging with our suppliers

We work in partnership with our suppliers to deliver mutually beneficial outcomes that benefit all our stakeholders. We engage through formal RFP processes for each AMP period and periodic supplier review meetings thereafter.

Shareholder and Investor engagement calendar

2022

April

- Spotlight Presentation: Investing for Sustainable Growth
- Announcement of the second issuance of our pioneering WaterShare+ scheme, including Bristol Water customers.

May

- Announcement of Full Year Results 2021/22

June

- London and Europe Roadshow
- PCIM Roadshow – London and Edinburgh
- Credit Suisse Global Energy Conference
- RBC Utilities & Infrastructure Conference
- Watershare+ Advisory Panel meeting

July

- Annual General Meeting
- WaterShare+ Annual General Meeting

September

- Trading Statement

November

- Announcement of Half Year Results 2022/23
- Watershare+ Advisory Panel meeting

December

- London and Europe Roadshow
- PCIM Roadshow – London and Edinburgh
- Virtual North America Roadshow

2023

January

- Swiss Roadshow (Geneva & Zurich)
- Citi European Utilities Conference

February

- Bristol Water licence merger successfully completed

March

- Trading Statement
- North America Roadshow

May

- Watershare+ Advisory Panel meeting

Engaging with our regulators and policy makers

We have proactively engaged with our regulators and Government, both at a local level, including sharing platforms with local MPs at constituency meetings, and face to face discussions with DEFRA throughout the year.

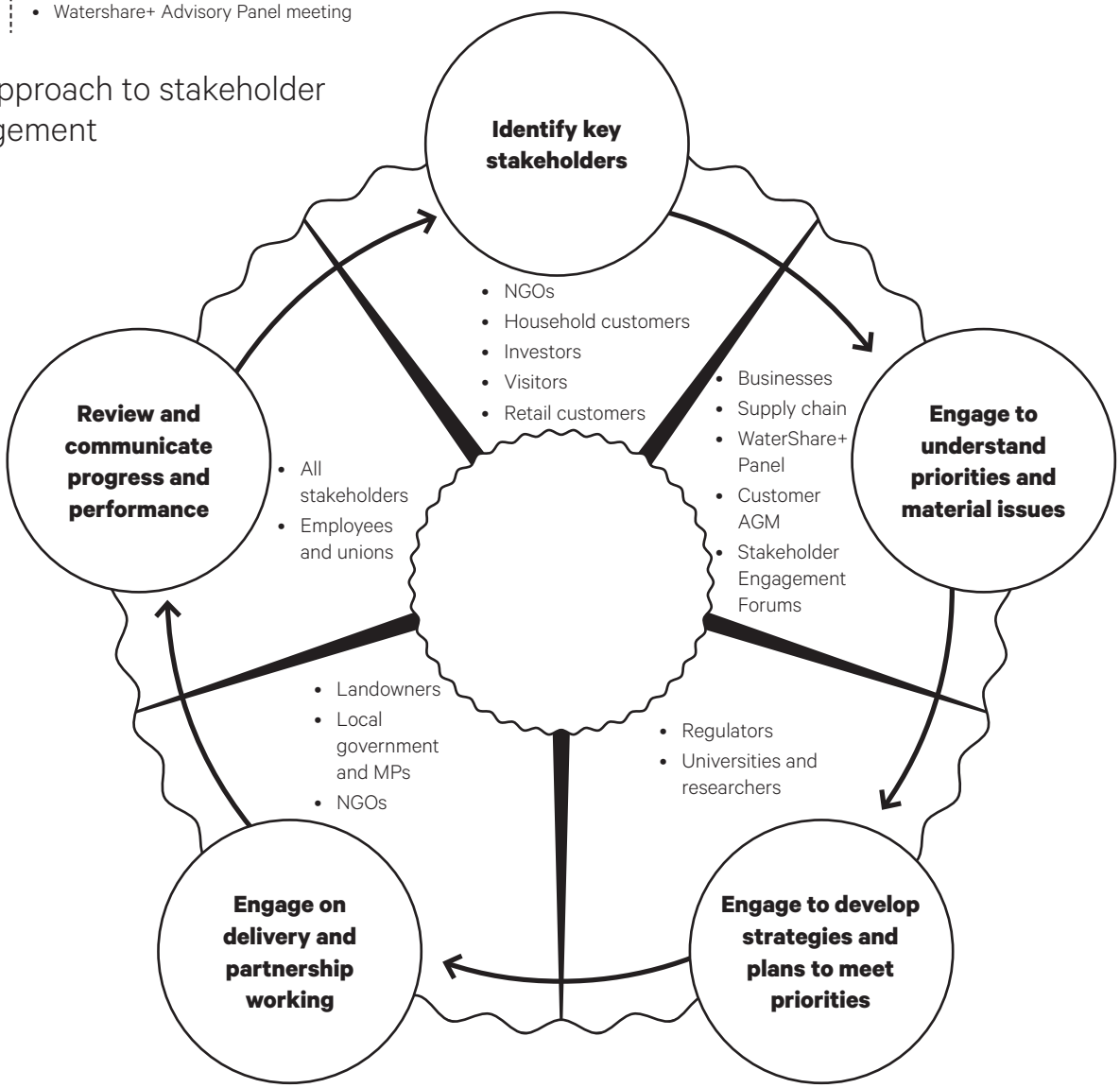
Pennon AGM

The AGM is an important forum where shareholders can meet with and question the Board, and we are keen to ensure that we continue to enable shareholder engagement. We enjoyed once again our discussions with shareholders in person last year, having been remote since the COVID-19 pandemic. We look forward to engaging with shareholders again at our 2023 AGM. We will set out information on our arrangements for our 2023 AGM in the Notice of AGM. The voting results of each AGM are fully disclosed to the London Stock Exchange, and we were pleased to see that every resolution at the 2022 AGM was passed with at least 94.45% votes in favour.

Customer AGM

Customers were able to see first-hand how water is supplied to the City of Plymouth using the latest technology and provide direct feedback and inform our WaterShare+ Advisory Panel. Lord Taylor, Chair of the Panel, was also on hand to provide an update on plans for the next year and discussed how Pennon Group was delivering against its in year objectives.

Our approach to stakeholder engagement



Section 172(1) Statement

All of the Board's decisions are considered against the importance of acting in a sustainable, ethical and collaborative way, understanding the views of our different stakeholders and weighing their competing interests, whilst being mindful of the regulatory obligations owed by Pennon Group's regulated subsidiary, South West Water limited. Our Board leads and sets the tone by carefully noting the priorities of our stakeholders during its discussions and when it takes decisions. We also know the importance of continually assessing the long-term impacts of our decisions. This helps us live our purpose and our values, as a responsible, trusted and sustainable business acting in a way which benefits all our stakeholders as much as possible. Properly understanding the impact of what we are doing has become part of how we operate, and it permeates everything we do at Pennon.

Each Director has a duty under section 172 of the Companies Act (s.172), to act in a way they consider, in good faith, would be most likely to promote the success of the Company for the benefit of members and stakeholders as a whole, and in doing so, must have regard to a range of broader issues. Therefore, when the Board makes a decision, we always take full account of the following:

- the long-term consequences of our decisions
- the interests of our employees
- the importance of having excellent business relationships with suppliers, customers and anyone else who we impact
- the impacts our operations have on our communities and our environment
- ensuring we maintain our reputation for the highest standards of business conduct
- we will always act fairly between our shareholders

As part of every decision we make, we look at how we will impact our stakeholders. To enable us to understand the points of view of our stakeholders and where our decisions could affect them, we have a stakeholder engagement programme. We see stakeholder engagement both as fundamental to development and delivery of our purpose and strategy and as critical for our long-term sustainable success. Although there are often competing interests and priorities involved, being clear on what matters to our stakeholders, allows our Board to weigh-up all relevant factors.

We have identified our stakeholders as:

- Environment
- Customers
- Our People
- Communities
- Suppliers
- Investors
- Regulators
- Policy makers

Examples of some of the key strategic issues considered and decisions made by the Board during the year and an explanation of how the Board considered the matters in Section 172(1) (a) – (f) when taking decisions are set out in the table below.

	Section 172 considerations	Our engagement	The Board's role
Drought Management	As a Group, we have recognised the challenges an impact of the unprecedented shortage of rainfall this year within the region, on our customers, communities, and wider stakeholders. We were quick to put in place measures to mitigate any adverse impacts We noted that next year's water resource position would start from a low base	We reviewed the implications of proceeding with a non-essential use drought order and drought permit options noting that two thirds of the required savings would need to be met from supply-side interventions. We considered the impact of financial incentives to customers who saved water.	We approved the submission of a Drought Order to cover Cornwall and the investments required to increase water resilience. We supported in principle the customer bill support initiative. We approved and implemented a recruitment strategy tailored and specialising in drought and water resource management to ensure future resilience. We approved £30m of initiatives and investments that are already underway. We approved £95m of additional investment including desalination to build future resilience. We debated key risks of the various options and used a broad range of scenario modelling.

	Section 172 considerations	Our engagement	The Board's role
Pollution and the Environment	We have a vital role to play in pollution reduction within our region which speaks to our commitment to operate in an environmentally sustainable and responsible manner. We further developed our Pollution Incident Reduction Plan. We strive to have a better relationship with our regulators.	We continued the measures implemented in 2021 which required working closely with customers, the Environment Agency and local communities.	We recognise the responsibility the Board has to the environment and implemented this view throughout the year. We noted the progress made on reducing our pollutions and reviewed the strategy together with our targets over the next two years. We noted the recent changes to penalise amenity-related pollutions within category 1 or 2 and progress against these. We reviewed strategies for preventing illegal connections. On WaterFit, we engaged with our key stakeholders including OFWAT and the EA.
Integration of Bristol Water	Following the clearance from the Competition and Mergers Authority on 7th March 2022, the Board was pleased to finalise the license merger with Bristol Water, on 1st February 2023, and welcome colleagues to the Group.	Following clearance for the merger we worked on the integration, licence merger and statutory transfer process.	We approved the submission of the required licence variation and the issue of the Section 8 notices. We endorsed the proposal to transfer the Bristol Water debt portfolio to South West Water. We delegated authority to the Group Chief Financial Officer and Group Treasurer to agree the final terms of documentation.
Water Resource Management	The long-term sustainability of the company and its continued ability to supply water to its customers is critical but needs to be balanced against the impact on the environment and communities.	We investigated long term interventions to shore up our ability to provide services including looking at other sources.	We considered options including new water sources (including Blackpool Pit and Leswidden Lake), installing desalination and dewatering. We noted the potential extent of these works and the need for full environmental assessments. We debated the restrictions on abstraction that the company is subject to and requested further reports on long-term water resource management.
Delivery of the WINEP programme	High standards of business conduct are critical to the company's operations and reputation. This includes alignment with regulatory guidance. As a company, we are committed to delivering our WINEP programme to meet our environmental obligations.	We considered the assurance activities undertaken in this respect noting the positive assessment provided by our external technical advisers. We considered the relationship between the cost of schemes and impacts into bills and affordability as well as resourcing challenges	We considered the relationship between the cost of schemes and impact on bills. We considered the assurance activities undertaken in this respect, noting the positive assessment provided by our external advisers. We delegated authority to the Executive to approve the submission of the proposals, noting our statutory obligations, non-statutory requirements and the priority drivers of the EA and Natural England.
Affordability	As a Group, we do not only recognise the needs of our wider stakeholders and investors but also the needs of our people and customers. This year, the Board has had the cost of living crisis at the forefront of their minds when supporting our colleagues and customers.	We investigated means of providing incentives to our customers and reducing the cost of their water supplies	Building on the success of the first WaterShare+ scheme, we approved the second WaterShare+ initiative, with £20m being given to South West Water, Bournemouth Water, and, for the first time, Bristol Water customers, in the form of a Pennon share or £13 credit added to their bill. We approved the launch of the 'Stop the Drop' initiative, which asked all customers in Cornwall to come together to help 'Stop the Drop' in reservoir levels. The Board was happy to give support to customers and approve £30 credit to customers' bills, in Cornwall, if Colliford Reservoir rose to 30% storage capacity by 31st December 2022.

Division of responsibilities

There is a clear separation of responsibilities between the Chair and the Chief Executive Officer, divided between managing the Board and the business, while maintaining a close working relationship.

All Directors are equally accountable for the proper stewardship of the Group's affairs and have specific roles, which include those set out below:

Non-Executive Directors

Chair

Gill Rider

- Leading the Board and setting its agenda.
- Promoting the highest standards of integrity and probity and ensuring good and effective governance.
- Managing Board composition, performance, and succession planning.
- Providing advice, support, and guidance to the Chief Executive Officer.
- Representing the Group and being available to shareholders.
- Discussing separately with the Non-Executive Directors performance and strategic issues.

Senior Independent Director

Neil Cooper

- Assisting the Chair with shareholder communications and being an additional point of contact for shareholders.
- Acting as a sounding board for the Chair.
- Being available to other Non-Executive Directors if they have concerns that are not satisfactorily resolved by the Chair.
- Ensuring an annual performance evaluation of the Chair, with the support of the other Non-Executive Directors.

Non-Executive Directors

Claire Ighodaro, Iain Evans, Jon Butterworth, Dorothy Burwell, Loraine Woodhouse

- Critically reviewing the strategies proposed for the Group.
- Critically examining the operational and financial performance of the Group.
- Evaluating proposals from management and constructively challenging its recommendations.
- Contributing to corporate accountability through being active members of the Committees of the Board.

Executive Directors

Group Chief Executive Officer

Susan Davy

- Managing the Group and providing executive leadership.
- Developing and proposing Group strategy.
- Leading the operation of the Group in accordance with the Board decisions.
- Coordinating with the Chair on important and strategic Group issues and providing input to the Board's agenda.
- Contributing to succession planning and implementing the organisational structure.
- Leading on acquisitions, disposals, business development and exploiting Group synergies.
- Managing shareholder relations.

Group Chief Financial Officer

Paul Boote

- Supporting the Group Chief Executive in providing executive leadership and developing Group strategy.
- Reporting to the Board on performance and developments across the business.
- Implementing decisions of the Board.
- Managing specific business responsibilities.
- Managing investor relations including financing and treasury activities.

Company Secretary

Simon Pugsley (to 30 November 2022),
Andrew Garard (from 1 December 2022)

- As Group General Counsel, with remit covering compliance, statutory duties and governance, providing strategic legal and commercial advice to the Group and the Board in its deliberations. As Group Company Secretary, attending and supporting all Board and associated Committee meetings of Pennon Group plc, South West Water Limited and Bristol Water plc.

Managing the Group and its subsidiaries

Following the acquisition of Bristol Water in June 2021, the South West Water Board and the Bristol Water plc Board operated as separate independent boards in accordance with Ofwat's principles on board leadership, transparency and governance until February 2023. The refocus of the Group on UK water means the interests of the non-regulated and regulated businesses are more closely aligned and provide for more effective leadership and governance. Because the three boards were run concurrently, the Directors were well-positioned to assess matters holistically and provide continuity to the Group as it moves to a water-only enterprise. Despite this concurrency, the Group's rigorous conflicts of interest process safeguarded the South West Water and the Bristol Water plc Boards' ability to set and have accountability for all aspects of the regulated business' strategy thereby ensuring and strengthening South West Water's and Bristol Water plc's regulatory ringfence.

While certain matters may be delegated to the Board Committees and to the Executive Directors, as appropriate, the matters reserved for the Board include:

- All acquisitions and disposals.
- Major items of capital expenditure.
- Authority levels for other expenditure.
- Pennon's dividend policy.
- Risk management process and monitoring of risks.
- Approval of the strategic plan and annual operating budgets.
- Group policies, procedures and delegations.
- Appointments to the Board and its Committees.

The Board also endorsed certain decisions taken by the South West Water and Bristol Water plc Boards, including major capital projects and investments, long-term objectives and commercial strategy, the five-year regulatory plans, annual budgets, and certain decisions relating to financing. This approach was compatible with Ofwat's principles on board leadership, transparency and governance because such decisions were ultimately reviewed and approved by the South West Water and Bristol Water plc Boards. Approval of South West Water's and Bristol Water plc's dividend policy and the declaration of dividends to be paid by South West Water or Bristol Water plc to Pennon also were reserved for the South West Water and Bristol Water plc Boards, respectively.

Conflicts of interest

In accordance with the Directors' interest provision of the Companies Act 2006 and the Company's Articles of Association, the Board has in place a procedure for the consideration and authorisation of Directors' conflicts or possible conflicts with the Company's interests. The Board considers this has operated effectively during the year.

Each Director has a duty under the Companies Act 2006 to avoid a situation in which they have or may have a direct or indirect interest that conflicts or might conflict with the interests of the Company. This duty is in addition to the duty owed to the Company to disclose to the Board any interest in a transaction or arrangement under consideration by the Company.

A register of Directors' conflicts is maintained and reviewed at each Board meeting. Authorised conflicts disclosed on the register currently involve cross-directorships with Pennon Water Services Limited and the trustee board of the Group's defined benefit scheme. Other potential conflicts of interest that were examined during the year included:

- The appointment of Claire Ighodaro to her role at KPMG
- Neil Cooper's disclosure of his interest in a holiday home potentially impacted by a South West Water commercial agreement.

Related parties

The processes outlined above in relation to conflicts of interest, together with the commissioning of frequent share register analysis, enable the Board to monitor the Group's related parties so that any related party transactions may be quickly identified and compliance with the Listing Rules ensured.

Composition, succession and evaluation

Board support and training

Directors have access to the advice and services of the Company Secretary, and the Board has an established procedure whereby Directors may seek independent professional advice at the Company's expense to fulfil their duties. The Company Secretary is responsible for ensuring that the Board operates in accordance with the governance framework and that information flows effectively between the Directors, the Board, and the Committees.

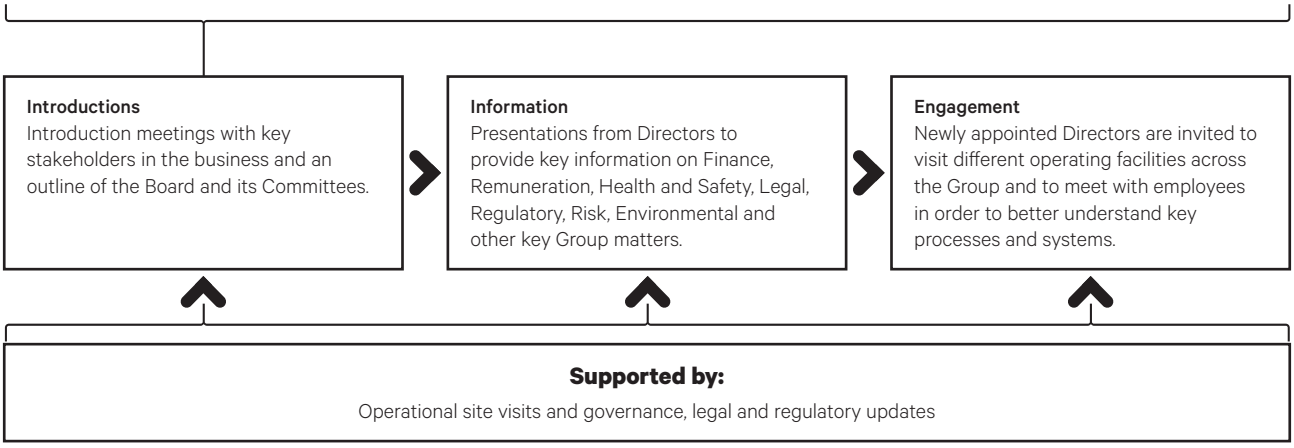
The training needs of Directors are reviewed as part of the Board's performance evaluation process each year. Training may include attendance at external courses organised by professional advisors and also internal presentations from senior management.

During the year, updates were provided to the Board and Committees via the Group General Counsel and Company Secretary and/or the Company's external advisors. These included updates on mandatory reporting and recent legal or governance changes, including shareholder guidelines. Specifically, the Board received updates on:

- Proposed changes to the Corporate Governance Code noting the move towards an outcome-based approach backed up with specific reporting and assurance requirements.
- The potential new regulator to replace the FRC announced in May 2022 that will have new powers to tackle breaches of company directors' duties relating to corporate reporting and auditing.
- The Data Protection and Information Bill introduced to Parliament on 18 July 2022 with the aim to "update and simplify" the UK's data protection framework.

Induction programme

Newly appointed Directors receive a formal, tailored induction.



Non-Executive Director induction programme

As part of Dorothy and Loraine's induction to Pennon and its Group companies, they took the opportunity with Andrew to visit several sites across the region including a drinking water treatment site, a sewage treatment site and a reservoir catchment project.

The two days of site visits were complimented by a full day briefing session on topics ranging from Governance and Group Finance to the Group's approach to Health and Safety and key risks and opportunities faced by Pennon and the wider UK water industry.

Pennon Board composition, independence, and experience

The Board comprises the Chair, six Non-Executive Directors, two Executive Directors and the Company Secretary. At year end, female representation on the Board was at 55%, exceeding the Board's target of 40% and the target of the FTSE Women Leaders Review and the Listing Rules.

All of the Non-Executive Directors are considered by the Board to be independent. Noting their intentions of retiring as set out below and given their longer service a particularly rigorous review was undertaken in respect of their respective re-elections, the Board remains satisfied that, based on their participation at meetings and their contribution outside of the boardroom, both Gill Rider and Neil Cooper continue to demonstrate independence of character and judgement in the performance of their role. An explanation regarding the Board's recommendation that Gill Rider and Neil Cooper remained in office during 2022/23 notwithstanding their long service to the Board, is shown below.

Neil Cooper will be retiring from the Board in September 2023 and Gill Rider will be stepping down as Chair in 2024. Details of the recruitment process for their successors is set out in the Nomination Committee Report on page 128.

All Directors are subject to re-election each year. All the Non-Executive Directors are considered to have the appropriate skills, experience in their respective disciplines and personality to bring independent and objective judgement to the Board's deliberations. Their biographies on pages 102 to 104 demonstrate collectively a broad range of business, financial and other relevant experience.

Neil Cooper is Chair of the Audit Committee and in accordance with the UK Code and FCA Disclosure Guidance and Transparency Rule 7.1.1, has recent and relevant financial experience and competence in accounting and auditing (as set out in his biography on page 103). The Board is satisfied that the Audit Committee has competence relevant to the sector in which the Group operates.

Succession planning

Neil Cooper

Neil Cooper has served eight years following the Board agreeing that his term be extended to nine years last year. The Board recommends Neil's re-election at the 2023 AGM ahead of his stepping down in September 2023. Information on our succession planning for the Audit Committee Chair role is in the Nomination Committee Report on page 128.

Gill Rider

In 2021, noting that Gill's tenure as a Non-Executive Director was approaching nine years and following an independent review and extensive consultation with shareholders, the Board was satisfied that an extension of no more than three years from July 2021 as Chair was appropriate. The rationale for this was set out in the 2022 Annual Report. The Board believes that these factors remain relevant this year. Gill will retire from the Board no later than July 2024 and the Board believes that continuity of leadership and strategic leadership between now and then is important as the Group continues to re-position itself as a major operator in the UK Water sector.

The Board considers that the extension of Gill's term as Chair both facilitates effective succession planning and the development and continuation of a diverse Board. For these reasons, and mindful of the recommendations of the UK Corporate Governance Code, the Board believes it to be in the best interests of the Company and its shareholders, for Gill to remain as Chair, and recommends her re-election at the 2023 AGM. It therefore recommends her re-appointment to the Board as Chair for one more year.

Further information on succession is provided in the Nomination Committee Report on page 128.

External appointments

Susan Davy

Susan Davy continued as a Non-Executive Director of Restore plc throughout 2022/23. The Board is of the opinion that the experience gained from external appointments provides additional and different business experience and a fresh insight into the role of an Executive Director. She is also a Non-Executive Director of Water UK, the membership body representing the UK water industry.

Chair and Non-Executive Directors

Information on the other business commitments of the Chair and Pennon's Non-Executive Directors is on pages 102 to 104.

Board effectiveness review

The Board undertakes a formal and rigorous review of its performance and that of its Committees and Directors each year. This ensures that they continue to operate effectively and are identifying opportunities for improvement and best practice, as well as helping to inform future agenda items and areas of focus. This year the review was undertaken by a third party, Equity Culture, by means of online interviews with a number of the Board, in consultation with the Chair and respective Committee Chairs, in January and February 2023. The outcome of the review concluded that the Board, its Committees, and individual Directors continued to demonstrate a high degree of effectiveness and collaboration, and that the Board had a forward-thinking mindset and a good understanding of opportunities for growth and risks facing the business, with the following positives, negatives and/or actions suggested. The detailed areas of assessment, commentary/ feedback and actions is included within the Nomination Committee report on pages 130 to 131.

In parallel with the Board effectiveness review the Committee undertook a 360-degree evaluation of the executive committee members and ensured the feedback was shared with the Group's senior leadership.

Audit, risk and internal control

Risk management and the Group's system of internal control

The Board is responsible for maintaining the Group's system of internal control to safeguard shareholders' investments and the Group's assets and for reviewing its effectiveness. The system is designed to manage rather than eliminate the risk of failure to achieve business objectives and can only provide reasonable and not absolute assurance against material misstatement or loss. An ongoing process for identifying, evaluating and managing the significant risks faced by the Group has been in place throughout the year and up to the date of the approval of this Annual Report and Accounts and is regularly reviewed by the Board.

The Group's system of internal control is consistent with the Financial Reporting Council's (FRC) 'Guidance on Risk Management, Internal Control and Related Financial and Business Reporting' (FRC Internal Control Guidance).

The Board confirms it applies procedures in accordance with the UK Code and the FRC Internal Control Guidance, which bring together elements of best practice for risk management and internal control by companies. The Group's internal audit function undertakes specific risk assessments to identify vulnerable risk areas in the Group. The Board's risk framework described on page 53 of the Strategic Report provides for the identification of key risks, including ESG risks, in relation to the achievement of the business objectives of the Group, monitoring of such risks and ongoing and annual evaluation of the overall process. ESG risks identified and assessed by the Board cover areas such as health and safety, climate change and tax compliance. Details of the key risks affecting the Group are set out in the Strategic Report on pages 52 to 62.

Key performance indicators are in place to enable the Board to measure the Company's ESG performance on pages 65 and 66 and a number of these are linked to remuneration incentives on page 137.

As part of the review evaluating the system of risk management and internal control under the Group risk management policy, all Executive Directors and senior managers are required to certify on an annual basis that they have effective controls in place to manage risks and to operate in compliance with legislation and Group procedures.

The Group's processes and policies serve to ensure that a culture of effective control and risk management is embedded throughout the Group and that the Group is able to react appropriately to new risks as they arise.

Code of Conduct and policies

The Group's Code of Conduct was reviewed and re-endorsed in November 2022. The Code of Conduct and related policies set out Pennon's commitment to promoting and maintaining the highest ethical standards. Areas covered in the Code of Conduct and related policies include our impact on the environment and our communities, our workplace, and our business conduct.

The Code of Conduct sets out the values and principles by which we operate and provides a framework for ethical business practices. It is further supported by several policies that guide our workforce and suppliers, so that we can identify and deal with suspected wrongdoing, fraud or malpractice, maintain the highest standards of compliance, and apply consistently high standards of ethics. We aim to maintain a culture that fosters the reporting of any concerns, and trust and confidence that we will act upon them.

Anti-bribery and anti-corruption

The Group's policy on anti-bribery and anti-corruption strictly prohibits employees across the Group from offering or accepting bribes, facilitation payments and kickbacks. The policy requires proper due diligence checks of third-party suppliers and contractors doing business with the Group, including a corruption risk assessment to examine the nature of the proposed work or transaction. The policy provides a framework that requires everyone who works with or for the Group to always act honestly and with integrity. The policy has been rolled out comprehensively into all parts of the Group, with regular online training arranged by the legal compliance team. The Group ensures compliance with the policy in line with our risk-based approach by conducting planned and ad hoc checks, providing both general and specific training, and carrying out detailed investigations into allegations of potential wrongdoing (whistle blows) received from employees, customers and suppliers. The potential consequences on colleagues and the Group itself are clearly set out in the policy as are the processes for raising concerns.

To mitigate risk, targeted authorisation and oversight processes are applied to the areas that have been identified as being more vulnerable and additional training is provided.

The legal compliance team likewise actively assesses high-risk areas based on information gained through its close working relationship with the Group internal audit function. Assessments are undertaken using several entry points, including using the output of reviews with the executive teams, during and following face-to-face training, and analysing whistleblowing reports. Any foreign trading operations, procurement activities, business development and back-office functions continue to be specifically reviewed for compliance with anti-bribery and anti-corruption requirements. Comprehensive operating procedures are in place to address risks in those areas, with regular reviews taking place to ensure the assessment of risk remains up to date.

The anti-corruption and anti-bribery policy also sets out the employment consequences for its breach and potential legal sanctions under bribery laws. Any breaches or failure to adhere to the Group's strict standards of integrity and honesty will be subject to disciplinary action, up to and including dismissal from the Company. All employees are required to read, understand, and comply with the policy and report any circumstances or any suspicions of fraud, bribery, corruption or other irregularities, either to a line manager or by using the Group's confidential whistleblowing service Speak Up. There were no confirmed cases of bribery, corruption, fraud, or business ethics violations during the year.

Allegations of bribery or corruption are reported to the Audit Committee together with investigation outcomes and details of any action taken, which are disclosed to our external auditors

Training and communications

Our comprehensive programme of training and internal communications continues with targeted messaging and interactive training sessions. This programme addresses the business's key compliance risk areas and has been designed to increase resilience, heighten awareness, and promote a culture of doing the right thing.

Whistleblowing policy – Speak Up

The Speak Up service encourages employees to raise concerns about suspected wrongdoing or unlawful or unethical conduct, explains how any such concerns should be raised and ensures that employees are able to do so without fear of reprisal. The Group's whistleblowing policy specifically covers and encourages reporting of:

- Endangering someone's health and safety.
- Anything that is against the law.
- Stealing or fraud.
- Corrupt or dishonest activity.
- Damage to the environment.
- Covering up wrongdoing.
- Abuse of authority.
- Intentionally misreporting to a regulatory body.
- Bullying, harassment and/or victimisation.

The Speak Up service comprises telephone and web-based reporting channels operated for Pennon by independent provider NAVEX Global.

Following receipt of a report, the allegation will be assessed, and an investigation started promptly. The investigation process is overseen by the Ethics Management Committee and will be undertaken fairly, impartially, and thoroughly by appropriately trained investigators with strict confidentiality being maintained at all stages of the investigation. After each investigation, a confidential review is undertaken by the Head of Legal Compliance to identify any lessons learnt, or organisational improvements or training requirements. Other improvements identified are always acted upon, while ensuring the paramount requirement of operating a whistleblowing process that protects the identity of individuals and the independence and integrity of the process. Our whistleblowing process is designed to support our staff, reflect shared responsibility, promote a positive culture, provide unique insights and is central to our system of checks and balances.

Legal Compliance policies and our Code of Conduct

The Group has policies in place covering the acceptance of gifts and hospitality, anti-facilitation of tax evasion and conflicts of interest, which require our people to disclose any situation which may conflict with their responsibilities as Pennon employees.

Our Code of Conduct and other key compliance policies can be found in the Governance and Remuneration section of our Group website at www.pennon-group.co.uk/sustainability/code-conduct-and-policies under Internal Control.

Audit Committee Report

The Audit Committee is focused on ensuring sound financial and risk management to support the Group's strategy

Neil Cooper
Chair of the Audit Committee

Committee members	Date of appointment to Audit Committee	Attendance
Neil Cooper	September 2014	✓✓✓✓
Claire Ighodaro	September 2019	✓✓✓✓
Iain Evans[1]	September 2018	✓✓✓
Jon Butterworth[1]	July 2020	✓✓✓
Loraine Woodhouse	December 2022	✓
Dorothy Burwell[1]	December 2022	

1. Following a review of Board Committee composition Iain Evans, Jon Butterworth and Dorothy Burwell ceased to be members of the Audit Committee effective 31st January 2023.

Role of the Audit Committee

- Ensure the quality and integrity of the Group's financial and regulatory reporting.
- Monitor and review the effectiveness of the internal control environment.
- Challenge the scope and adequacy of the Group's risk management processes.

The Committee's focus for 2022/23

- Ensure the 2023 Annual Report and Financial Statements are fair, balanced and understandable.
- In depth review of the key financial reporting judgements.
- Risk "deep-dives" in key focus areas.
- Consideration of the FRC's review of the external auditor's 2022 audit of Pennon Group plc.
- Scrutiny of our responses to address the risks posed by rising inflation and the resultant cost of living crisis.

Dear Shareholder

On behalf of the Board, I am pleased to present the Audit Committee's report for the year ended 31 March 2023. This report is intended to provide shareholders with an insight into the work of the Audit Committee ('the Committee') together with details of how the Committee has discharged its responsibilities throughout the year and overseen the process of assurance over the integrity of the 2023 Annual Report and Financial Statements ('the 2023 Annual Report').

As in previous years, we have focused on the following key priority areas:

- Ensuring the quality and integrity of the Group's financial reporting; this is done through the assessment of the application of accounting policies given underlying standards, challenging management through the review of the use of accounting judgements made in preparing financial reporting and the Committee's assessment of the quality of financial reporting of the Group in terms of whether its presentation is fair, balanced and understandable.
- Ensuring the 2023 Annual Report is aligned with the requirements and guidance from regulators, and that all matters reported on and disclosed meet the needs of our various stakeholders.
- Monitoring and reviewing the ongoing effectiveness of the internal control environment.
- Challenging the scope and adequacy of risk management processes across the Group. In doing this, we monitor the expression of the Group's risk appetite and undertake "deep dive" reviews of higher risk areas.

The Committee uses its collective expertise, with input from the External Auditor, to provide a robust challenge to the approach and judgements made by management in the treatment of financial matters and their resulting disclosures within the financial statements. One of our key roles is to advise the Board that we are satisfied that the 2023 Annual Report is fair, balanced and understandable and that it provides the information necessary for shareholders to assess the Group's position, trends in performance, business model and strategy. In doing so, we ensure that management's disclosures reflect the supporting detail, or challenge them to explain and justify their explanation and, if necessary, re-present the information. As part of fulfilling these commitments, we carefully consider the key financial reporting judgements of the management as set out on page 123. Significant matters considered by the Committee both during the year and in relation to the year-end financial statements are laid out in this report. The External Auditor supports this process in the course of the statutory audit.

The Committee was pleased to advise the Board that the 2023 Annual Report met these criteria. Details of our review process can be found on page 125.

The Committee discharges its responsibilities throughout the year in accordance with a schedule of business reflecting the annual external reporting cycle of the Group, allowing for appropriate consideration at the right point. This scheduling also allows for consideration on an ad-hoc basis of events as they have arisen.

In regard to risk, the process starts with the Group's Executive Risk Committee formulating its risk appetite as well as its ongoing monitoring of key risks and their mitigation. The Committee then considers this formally, as well as homing in on key risk areas.

During the year, these key risk deep dives covered a wide range of topics including the risks posed by:

- Cyber security breaches.
- Non-recovery of customer debt.
- Regulatory planning for PR24.
- Availability of financing for our accelerated investment programme.

More detail on our risk management processes, principal risks and their associated mitigations can be found on pages 52 to 62.

Alongside this focus on our risk processes, we formally review the output of the Group's financial resilience and health assessments; for a 12-month 'look forward' period through our assessment of the Group's going concern status and over a period of five years to assess the Group's continuing viability. This viability assessment has considered a range of financial projections arising from the current challenging and complex external environment with ongoing uncertainties in relation to economic growth, inflation prospects and the indirect impact of the ongoing conflict in Ukraine. These are modelled through internal scenarios around the deployment of Group cash reserves and which now incorporate the integration of Bristol Water's operating licence into South West Water. While the Group maintains a five-year viability assessment period, being appropriate for an acquisitive group, South West Water, now including the operating commitments of Bristol Water, has continued to use a longer assessment period to 2030, since it has a greater visibility of future cash flows, being a regulated businesses. Our viability statement is reported on pages 63 and 64.

Throughout the year, the Group has remained focused on delivering a resilient performance in UK water, despite a difficult period of cost inflation, as we execute our twin-track growth strategy of utilising both organic and acquisitive levers to drive long-term sustainable growth. We are focused on delivering sustainable results for all stakeholders.

Key considerations for the Committee in the last year in delivering these commitments include:

- Consideration of the FRC's review of the External Auditor's 2022 audit of Pennon Group plc and its thematic review of acquisition disclosures, which included Pennon
- The impact of unprecedented weather conditions and demand in Cornwall, with a combination of temperature and drought leading to a 1-in-200-year water resource shortfall and the appropriate disclosure of the financial impact of this
- Scrutiny of our responses to address the risks to the business posed by rising inflation and the resultant cost of living crisis
- Challenging our financial projections and scenario analysis to ensure we are well placed to deliver our environmental investment commitments.

I am pleased to welcome Loraine Woodhouse to the Committee as part of our Board succession planning. I will be stepping down as Chair during 2023 as I reach the end of my nine-year tenure at Pennon and am confident that Loraine, who will succeed me, has the experience and gravitas to both oversee a smooth transition and perform the role successfully going forward. I would like to thank the members of the Committee past and present, the management team, the internal auditors and our External Auditors and advisors for their continued commitment and for the contribution they all provide in support of the work of the Committee, not just for the year under review, but during my tenure as Committee Chair.

Neil Cooper
Chair of the Audit Committee

31 May 2023

Exeter Quay taken on one of our litter pick days

Audit Committee composition

All members of the Committee are Independent Non-Executive Directors of the Board. In accordance with the UK Code, the Board is satisfied that Neil Cooper, Claire Ighodaro, Loraine Woodhouse, Iain Evans and Jon Butterworth, all of whom served on the Committee during the year under review have recent and relevant financial experience and also, in accordance with FCA Rule 7.1.1R of the FCA's Disclosure Guidance and Transparency Rules have competence in accounting or auditing. Following a review of the composition of Board Committees, Iain Evans and Jon Butterworth stood down from the Audit Committee in March 2023.

Only members of the Committee have the right to attend Committee meetings. Other regular attendees at meetings, at the invitation of the Committee, include the Chair of the Board, the Group Chief Executive, the Group Chief Financial Officer, the Group General Counsel and Company Secretary, Director of Risk and Assurance, Group Financial Controller and the External Auditor.

The Committee regularly holds private discussions with the External Auditor without management present. Further, the Committee Chair regularly communicates with the Group Chief Financial Officer, the External Auditor and with Committee members outside the meetings to better understand any issues or areas for concern.

Matters of significance in 2022/23

Financial reporting	• Reviewed and discussed reports from management on the financial statements, considered management's significant accounting judgements and the policies being applied, and assessed the findings of the statutory audit in respect of the integrity of the financial reporting of full and half year results. • Reviewed the internal assessment of going concern and longer-term viability on behalf of the Board. • Reviewed in detail the 2023 Annual Report and advised the Board that the presentation of the 2023 Annual Report is fair, balanced and understandable in accordance with reporting requirements, including the consideration of climate risk in the preparation of the financial statements, and recommended the Board give approval for publication.
External auditor	• Oversaw the 2022/23 statutory audit, including the key audit risks and level of materiality applied by the External Auditors. • Assessed the effectiveness of the External Auditor and made a recommendation to the Board on their reappointment. • Agreed the statutory audit fee for the year ending 31 March 2023. • Reviewed and approved the non-audit services and related fees provided by the External Auditors for 2022/23.
Internal controls and risk management	• Reviewed the effectiveness of the Group's risk management framework and its integration into Board and Committee Reporting. • Reviewed the Group's Risk Appetite Statement prior to making a recommendation to the Board. • Monitored fraud reporting and incidents of whistleblowing, including a review of the Group's whistleblowing processes and procedures and reporting to the Board on this. • Reviewed the Group risk register and considered appropriate areas of focus and prioritisation for the internal audit work programme for the financial year. • Carried out deep dives at Committee meetings on principal risk areas.
Governance	• Considered and approved Group accounting policies and judgements used in the preparation of the financial statements, including any required alignments of Bristol Water's accounting policies. • Reviewed and considered internal financial policies. • Confirmed compliance with the UK Code. • Held regular meetings with the external auditor and the Group Director of Risk and Assurance without members of management being present.

Regarding monitoring of the integrity of the financial statements, which is a key responsibility of the Committee identified in the UK Code, the significant areas of judgement considered in relation to the financial statements for the year ended 31 March 2023 are set out in the following table, together with details of how each matter was addressed by the Committee. At the Committee's meetings throughout the year, the Committee and the external auditor have discussed the significant matters arising in respect of financial reporting during the year, together with the areas of particular audit focus, as reported on in the independent auditor's report on pages 162 to 169. In addition to the significant matters set out in the table below, the Committee considered presentational disclosure matters including the use of non-underlying performance metrics and ensuring a fair presentation of statutory and non-statutory performance and financial measures.

During the year, the Committee's areas of focus included:

Area of focus	How the matter was addressed by the Committee
Revenue recognition	• Given the nature of the Group's revenue, the key areas of income statement judgement for South West Water, Bristol Water and Pennon Water Services continue to be in respect of revenue recognition relating to income from water services. While the Committee relied on South West Water's, Bristol Water's and Pennon Water Services' processes for assessment of water into supply, it challenged the robustness and timeliness of the methodology used, resulting in management streamlining the calculation approach. The Committee welcomed this improvement and continues to scrutinise the track record of accuracy by comparing actual outturns with accruals at previous year ends to form a judgement about the quality of decision making. The Committee also closely considered the work in respect of these areas at year end by the external auditor as well as reviewing disclosures around revenue recognition accounting policies.
Bad and doubtful debts	• Regular updates on progress against debt collection targets and other contractual payments due are received by the Board. Performance is monitored regularly across the Group against historical standards and compared to the track records of other companies in the relevant sectors. The Committee was particularly mindful of the ongoing impacts of affordability on the assessment of expected credit losses in determining the bad debt provision, noting the significant increases in inflation arising from macro-economic developments. At the year end, the external auditor reported on the work it had performed, which, together with the detailed analysis reported, enabled the Committee to conclude that management's assessment of the year-end position and its provisions for expected credit losses were reasonable.
Going concern basis for the preparation of the financial statements and viability statement	• A report from the Group Chief Financial Officer on the financial performance of the Group, including forward-looking estimates of covenant compliance and funding levels under different scenarios including inflation scenarios, is provided to the Board on a periodic basis. Rolling five-year strategy projections and the resultant headroom relative to borrowings are also regularly reviewed by the Board, including the application of scenarios to enable the Committee to better understand the potential range of outcomes. At the end of each six-month period the Group Chief Financial Officer prepares for consideration by the Committee a report focusing on the Group's liquidity over the 12-month period from the date of signing of either the Annual Report or half-year results. The Committee also reviewed a report from the Group Chief Financial Officer on the Group's financial viability over an appropriate period, in connection with the UK Corporate Governance Code's requirement for a viability statement to be given by the Board. The Board considers the appropriate period to assess the Group's viability remains unchanged at five years which recognises both the longer-term visibility in the regulatory environment of the South West Water and Bristol Water businesses and the corporate activity, including acquisitions and other non-regulatory investments, such as the recent Bristol Water acquisition and our investments in solar energy generation, undertaken by Pennon. • Similarly, this report also considered the viability of the Group, taking into account the potential manifestation of other adverse events modelled from the Group's principal risks and resultant sensitivity scenarios. In performing its own viability assessment, South West Water (now incorporating the operating licence of Bristol Water) uses a longer assessment period to 2030, noting a greater visibility of future cash flows, being a regulated water business. Consideration of these reports and constructive challenge on the findings of the reports, including the scenario testing carried out by management, has enabled the Committee to form its assessment and satisfy itself that it remains appropriate for the Group to continue to adopt the going concern basis of accounting in the preparation of the financial statements and in addition advise the Board on providing the viability statement set out on page 63.

In addition to the matters above, the Committee also reviewed and considered communications with the FRC in respect of their thematic review of acquisition disclosures, which included Pennon. Positively, this review highlighted areas of our disclosure in respect of the Bristol Water acquisition as examples of best practice. Less positively, the FRC also queried the inclusion of an element of cash outflow relating to acquisition costs within the investing activities section of the cash flow statement. Having considered this matter, the Company has acknowledged that the acquisition cost cash outflow should have been presented within operating activities but that a restatement of presentation was not proposed as the effect of the change is not material. Following our responses, we are pleased to report the FRC has satisfactorily concluded this review.

The Audit Committee notes that the FRC's review was based on the 2022 annual report and accounts and does not benefit from detailed knowledge of our business or an understanding of the underlying transactions entered into. It is, however, conducted by staff of the FRC who have an understanding of the relevant legal and accounting framework. We also note that the FRC provides no assurance that the annual report and accounts is correct in all material respects; the FRC's role is not to verify the information provided but to consider compliance with reporting requirements. The FRC's letters are written on the basis that the FRC (which includes the FRC's officers, employees and agents) accepts no liability for reliance on them by the company or any third party, including but not limited to investors and shareholders.

Effectiveness of the external audit process

Receiving high-quality and effective audit services is of paramount importance to the Committee. We continue to carefully monitor the effectiveness of our External Auditor as well as their independence, while recognising there is a need to use our External Auditor's firm for certain non-audit services. We have full regard to the FRC's Ethical Standard and ensure that our procedures and safeguards meet these standards.

The FRC's Audit Quality Review (AQR) team completed an inspection of the audit of the financial statements of Pennon Group plc for the year ended 31 March 2022. The AQR's overall assessment of the audit was that there were no key findings arising from the inspection.

The Committee has carefully considered the three other findings that were raised in the AQR's report and has concluded that these do not present any significant concerns on overall External Audit effectiveness when taken with the External Auditor response immediately below.

The External Auditor produced a detailed audit planning report in preparation for the year-end financial statements, which reflects appropriate consideration of improvements to address the AQR report's other findings and which has assisted the auditor in delivering the timely audit of the Group's Annual Report and which was shared with, and discussed by, the Committee in advance.

The effectiveness review of the External Auditor is considered as part of the Committee's annual performance evaluation, which also examines the relationship and communications between the Committee and the external auditor. Further details of the Committee evaluation are provided on page 124. No issues were raised during that review. The Committee concluded that the Auditor was effective during the year and that the relationship and communications were open and constructive.

The Committee considered it was appropriate that the External Auditor be reappointed and has made this recommendation to the Board. The Committee Chair has also met privately with the External Auditor to discuss key matters.

Auditor independence

The Committee regards independence of the External Auditor as absolutely crucial in safeguarding the integrity of the audit process and takes responsibility for ensuring the three-way relationship between the Committee, the External Auditor and management remains appropriate.

The External Auditor reported on its independence during the year and again since the year end, confirming to the Committee that, based on its assessment, it was independent of the Group.

Provision of non-audit services

The Committee adopts a robust policy for the engagement of the External Auditor's firm for non-audit work. The Committee receives a regular report covering the auditor's fees including details of non-audit fees incurred.

Recurrent fees typically relate to agreed procedures regarding annual regulatory reporting obligations to Ofwat; work which is most efficiently and effectively performed by the statutory auditor. The policy is for non-audit fees not to exceed 70% of the audit fee for statutory work and for the Committee Chair to approve all non-audit work performed by the statutory auditor. The policy uses the average of the last three years' audit fees disclosed in the accounts and certain non-audit fees for services that are required to be performed by the auditors that are excluded from the assessment.

The Committee carefully reviews non-audit work proposed for the statutory auditor, taking into consideration whether it was necessary for the auditor's firm to carry out such work, and only grants approval for the firm's appointment if it was satisfied that the auditor's independence and objectivity would be safeguarded. If another accounting firm could provide the required cost-effective level of experience and expertise in respect of the non-audit services, then such firm would be chosen in preference to the External Auditor.

The level of non-audit fees payable to the External Auditor for the past year is 14% of the three-year average audit fee, which is within the Group's 70% non-audit fee limit.

The Group Chief Financial Officer regularly reports to the Committee on the extent of services provided to the Company by the External Auditor and the level of fees paid. The fees paid to the External Auditor's firm for non-audit services and for audit services are set out in note 7 to the financial statements on page 188.

External auditor reappointment and statement of compliance with CMA order

The Group complies with the Statutory Audit Services for Large Companies Market Investigation (Mandatory Use of Competitive Tender Processes and Audit Committee Responsibilities) Order 2014.

We last undertook a formal comprehensive audit tender process for statutory audit services in 2014. The current External Auditor, Ernst & Young LLP (EY), were appointed following a comprehensive audit tender process and approval by shareholders at the Company's 2014 AGM. EY commenced their appointment as auditor and presented their first report to shareholders for the year ended 31 March 2015. The lead audit partner must change every five years. Christabel Cowling, who has considerable audit experience of other FTSE 100 utility companies, has held the role since 2019.

This year-end audit has been EY's ninth consecutive year in office as statutory auditor. As previously indicated, the Committee will be running a full tender for the Group's external audit services during the year ending March 2024, before the next rotation would become due. This allows for any potential new audit firm to take up the role for the year ending March 2025 and, if required, affords appropriate time for a smooth transition of responsibilities.

Internal audit

The internal audit activities of the Group are a key part of its internal control and risk management framework. At Group level there is a long-standing and effective centralised internal audit service, which supports the Committee in delivering its responsibilities and has continued to operate effectively. The current Group internal audit plan was approved in March 2022, following a thorough review to ensure it provided adequate coverage over the Group's key risks for the year ahead and was sufficiently flexible to respond to emerging risks. In developing the plan, account is taken of the principal risks, the activities to be undertaken by the External Auditor, and the Group's annual and ongoing risk management reviews. This approach seeks to ensure that there is a programme of internal and external audit reviews focused on identified key risk areas throughout the Group. Looking ahead, the intention of the Committee is to establish formal internal audit plans covering each six-month period, given the volatility of the operating environment.

The Group Director of Risk and Assurance reported regularly through the year to the Committee on the outcomes and findings of internal audit activity. There were regular discussions, correspondence and private meetings between the Director of Risk and Assurance and the Committee Chair. The Committee continues to monitor the performance of the internal audit function as part of its annual assessment of the effectiveness of the function. As required by IIA standards, the next cyclical external review of the internal audit function will take place before the end of 2026/27 (the last having been undertaken in 2021/22).

Fair, balanced and understandable assessment

To enable the Committee to advise the Board in making its statement that it considered that the Company's Annual Report is fair, balanced and understandable (FBU) on page 101, the Committee applied a detailed FBU review framework that takes account of the Group's well-documented verification process undertaken by management in conjunction with the preparation of the 2023 Annual Report. This was in addition to the formal process carried out by the External Auditor to enable the preparation of the independent auditor's report, which is set out on pages 162 to 169.

In preparing and finalising the 2023 Annual Report, the Committee considered a report on the actions taken by management in accordance with the FBU process and an FBU assessment undertaken by the Pennon Executive. This assisted the Committee in carrying out its own assessment and being able to advise the Board that it considered that the Annual Report taken as a whole is fair, balanced and understandable and provides the information necessary for shareholders to assess the Company's position, performance, business model and strategy.

Looking forward

During the forthcoming year, the Committee will remain focused on the key areas of responsibility delegated to it by the Board, ensuring that standards of good governance are maintained and that appropriate assurance is obtained across all areas of the business, with a particular focus on the Group's principal risks, control environment and approach to financial reporting, noting the volatility in the global economy, and taking into account developments in reporting responsibilities including those recommended by the Task Force on Climate-related Financial Disclosures (TCFD), the consideration of climate risk in preparation of the financial statements and potential changes in the governance environment. The Committee will further assist, with its usual diligence, the transition from the outgoing Committee Chair to the new Chair during the year.

Fernworthy Reservoir, Dartmoor National Park, Devon

ESG Committee report

The ESG Committee supports the Company's ongoing commitment to environmental stewardship.

The Committee's focus for 2022/23

- Reviewed the external 2022 ESG Assessment scores and approved the work being undertaken to improve these.
- Successfully achieved majority of 2022/23 ESG targets.
- Successful progress made against majority of environmental KPIs, including sewer flooding and biodiversity.
- Approved an updated Sustainable Finance Allocation and Impact Report.
- Reformulated the future ESG targets to align with executive remuneration targets.
- Carried out deep dive reviews on storm overflow discharges and the Spillsure programme noting the enhanced level of community engagement being proposed.
- Continued delivery of TCFD recommendations including detailed appraisal of transition risks and opportunities and scenario analysis.
- Enhanced ESG reporting including our disclosures aligned to the Sustainability Accounting Standards Board (SASB) reporting framework and new ESG DataBook.
- Integration of Bristol Water ESG activity into Group ESG reporting.

Dear Shareholder

I am pleased to report on the ESG Committee's activities and achievements during 2022/23. There have been no changes to the Committee this year. I continue to be supported by an experienced Committee who focus on governing our ESG activity and disclosure and ensure we continue to be a responsible business, creating a positive long-term impact on the environment and all our stakeholders and I'd like to thank them for their work and input this year.

Our approach to ESG ensures that everything we do supports our commitment to provide environmental stewardship and to support our customers and local communities. As a responsible employer, we remain focused on employee development alongside a robust health, safety and wellbeing programme. This is underpinned by a strong governance framework that upholds our core values within the organisation and throughout our supply chain. Sustainability is at the heart of our business and is part of everything that we do. During the year, the Committee considered a wide range of matters while fulfilling its duties in accordance with its terms of reference.

Our refreshed Group ESG targets through to 2025 reflect the priority issues identified by stakeholders in our materiality assessment that were not already addressed in existing regulatory commitments and plans. These targets support us in aligning our approach and priorities for PR24. You can read more on the outcomes of the materiality assessment on pages 66.

With effect from 6 April 2022, we are required to disclose climate-related financial information on a mandatory basis in line with requirements from the TCFD. These disclosures evidence our strategy to reduce emissions within our operations and through our supply chain to achieve Net Zero by 2030 driven by three pillars – sustainable living, championing renewals, and reversing carbon emissions.

This Annual Report provides an integrated assessment to show how a responsible approach to sustainability helps us to balance the immediate and longer-term needs of society with the delivery of sustained commercial success.

ESG performance

The ESG Committee continues to assess performance against a range of challenging targets for the Group, set as part of the business planning process. The Committee reviewed and approved 2025 targets noting that the metrics, ODIs, Operational Service assessments and ESG

Iain Evans
Chair of the ESG Committee

Committee members	Date of appointment to ESG Committee	Attendance
Iain Evans	September 2018	✓✓✓✓
Gill Rider	September 2012	✓✓✓✓
Susan Davy	March 2018	✓✓✓✓
Jon Butterworth	July 2020	✓✓✓✓
Paul Boote	July 2020	✓✓✓✓
Claire Ighodaro[1]	September 2019	✓✓✓
Neil Cooper[1]	July 2020	✓✓✓
Dorothy Burwell	December 2022	✓
Loraine Woodhouse[1]	December 2022	

1. Following a review of Board Committee composition, Gill Rider, Neil Cooper and Loraine Woodhouse ceased to be members of the ESG Committee with effect from 31 January 2023.

Role of the ESG Committee

- Review the policies, management, initiatives and performance of the Group with respect to the environment, workplace policies, group governance and corporate policies relating to responsible and ethical business practice, the role of the Group in society and customer service and engagement.
- Review the overarching environmental performance of the business, ensuring a focus on key areas of improvement.
- Review the actions of the Group to determine the suitability of the workplace environmental policies and practices of key suppliers and contractors.
- Review the extent and effectiveness of the Group's external reporting of sustainability performance and its participation in relevant external benchmarking indices.
- Regularly report to the Board.
- Advise the Audit Committee of any material non-financial risks.

targets are aligned to the strategic themes identified in the Committee's materiality assessment. ESG targets were rebased and reformulated to align with executive remuneration targets. The Committee agreed that the targets for 2023/24 should be published in this Annual Report on page 66.

In addition, the South West Water ESG Committee provides assessment and oversight of South West Water's performance against sustainability targets that are core to the successful delivery of its five year business plan. This is consistent with Ofwat's requirement for independent governance of the regulated business.

As at the 31 March 2023 Pennon achieved 14 of our 16 targets for 2023 and are currently on track to meet our 2025 targets. Whilst we have continued to invest in solar generation, the increase in energy usage has resulted in generation as a proportion of total usage being lower than targeted and despite our lowest number of lost time injuries this was ahead of the number targeted for the year.

Materiality assessment

During the year, we embedded the results of our extensive materiality assessment into our 2025 targets. The outcome of this materiality assessment showed the following as of highest importance to all stakeholders:

- Net Zero.
- Freshwater stewardship.
- Water quality.
- Climate resilience.
- Drinking water quality.
- Amenity and recreation.
- Trust and transparency.

There has been no change in the areas of materiality which have the highest importance for the Group.

Enhanced reporting and assurance

With a growing focus on ESG reporting, we are increasing our 2023 reporting suite and providing enhanced disclosure through our SASB disclosure which can be found on pages 70 to 72 and ESG databook which is available to view at **www.pennon-group.co.uk/sustainability**.

Pennon's ESG reporting is integrated throughout the strategic report and specifically in the following sections:

Section	Page
Chair's letter	2
Chief Executive Officer's review	4
Business model	8
Strategy overview	10
Key performance indicators	17
Environment performance	66
Social performance	66
Governance performance	66
Stakeholder overview	110
Our people strategy	31
Our operations	22

Other related reporting including our Gender Pay Gap report, Climate Change Adaptation Report and Net Zero plan can be found on our website **www.pennon-group.co.uk/sustainability**.

Pennon's ESG performance and reporting has been assured by DNV, an independent management consultancy specialising in technical assurance in the utility sector. DNV's method of assurance includes testing the assumptions, definitions, methods, and procedures that are followed in the development of data and the auditing thereof to ensure accuracy and consistency. The assurance statement can be found on our website **www.pennon-group.co.uk/sustainability**.

Certain disclosures within this Annual Report that relate to the sustainability performance of South West Water and Bournemouth Water have been subject to an independent audit of regulatory data conducted by Jacobs. DNV has reviewed the consolidation of these into total Pennon data where stated, but not their preparation.

Jacobs are engaged to independently audit South West Water's and Bristol Water's technical (non-financial) data relating to our Outcome Delivery Incentives published in its Annual Performance Report (APR), this includes all regulatory targets, including a suite of environmental performance indicators. This year Turner and Townsend has conducted an independent audit of other non-financial also included in the APR. This includes all South West Water regulatory targets, including the suite of environmental performance indicators. Jacobs provide a report on this audit within South West Water's APR. Similarly, Turner & Townsend conduct an independent audit of Bristol Water's technical (non-financial) data also published in its APR.

Benchmarking

It's important to us to ensure we are regularly benchmarked against the expected industry standards. This ensures we are continuing to provide up to date disclosure for our stakeholders. Certain leading indices assess companies on their disclosures relating to stringent environmental, social and governance criteria, and their position to capitalise on the benefits of responsible business practice. Pennon is a constituent within the FTSE4Good Index, Sustainalytics, CDP Climate Change, S&P Global CSA, and a number of other leading external ESG assessments. FTSE4Good and similar leading indices are designed to facilitate investment in companies that meet globally recognised corporate responsibility standards.

Our latest external assessment scores as at 31 March 2023 are included on page 65 with improvements seen in 7 out of 8 assessments.

Focus areas for 2023/24

- Embed the assessment and identification of climate-related risks without our investment appraisal processes.
- Integrate our climate risks within our existing risk management systems and risks registers across the Group.
- Continue to explore options to develop quantitative metrics for our key climate risks and opportunities.
- Further integration of ESG across the entire Group.
- Expansion of community impact evaluation and reporting.
- Review performance on how the company is fulfilling its purpose and its external ESG benchmarking.
- Undertake matters of Committee governance such as its rolling calendar of agenda items, annual Committee evaluation and examination of Committee's terms of reference.

Iain Evans
ESG Committee Chair

31 May 2023

Nomination Committee report

The role of the Nomination Committee is to ensure that the Group has the pre-requisite skills, experience, breadth and depth of talent to meet longer-term strategic objectives.

The Committee's focus for 2022/23

- Overseeing the effectiveness of the Board's succession plan and identifying two new non-executives, ensuring that the Board has the appropriate mix of skills, experience and diversity.
- Conducting the annual review of Board Effectiveness and Board composition.
- The annual review and approval of the Group policy on Diversity, Respect and Inclusion and the Group's progress on diversity in line with the Parker review, including the outcome of the FTSE Women Leaders Review and the Group's position on Gender Pay and Ethnicity Pay.
- Ongoing review, development, and evolution of the Executive Leadership team, including succession planning and the integration of Bristol Water.
- Reviewing terms of reference for the Committee to ensure they continue to be appropriate.

Dear Shareholder

I am pleased to present the Nomination Committee's report for the year ended 31 March 2023.

This year, the Committee has been pleased to welcome Loraine Woodhouse and Dorothy Burwell to the Board as independent Non-Executive Directors, from 1 December 2022. The appointments are in line with our succession planning with relevant skills and diversity of perspective. Loraine will succeed the Audit Committee Chair when Neil Cooper steps down in the summer. I am delighted they have chosen to join Pennon, and would also like to recognise Neil's considerable contribution to the Group since he was appointed in 2014.

As noted in the 2022 Committee Report at page 157, Russell Reynolds Associates was appointed as independent consultants, to conduct the search activity, providing the Committee with a long list of suitable candidates, ensuring candidates were apprised of the expectations required as a member of the Board, the time commitment and professional conduct and values. A rigorous selection process was undertaken, including meetings with appropriate stakeholders as well as the interview process with Board members. The induction process for Dorothy and Loraine is detailed on page 116.

The Committee has also supported the ongoing evolution of the wider executive, with the integration of Bristol Water, and key external appointments including Andrew Garard as Group Counsel and Company Secretary and John Halsall as Chief Operating Officer.

Gill Rider
Chair of the Nomination Committee

Committee members	Date of appointment to Nomination Committee	Attendance
Gill Rider	September 2012	✓✓✓✓
Neil Cooper	September 2014	✓✓✓✓
Iain Evans	September 2018	✓✓✓✓
Jon Butterworth	July 2020	✓✓✓✓
Claire Ighodaro	July 2020	✓✓✓✓
Loraine Woodhouse	December 2022	✓
Dorothy Burwell	December 2022	✓

Role of the Nomination Committee

- Regularly review the structure, size and composition (including skills, knowledge, independence, diversity and experience) required of the Board.
- Consider succession planning for the Board and Senior Management overseeing the development of a diverse pipeline.
- Identify and nominate candidates to fill Board vacancies.
- Assist the annual Board evaluation process to assess performance and effectiveness of the Board and its Committees.
- Evaluate the balance of skills, knowledge, independence, diversity and experience on the Board.
- Review the leadership needs of the Group, both executive and non-executive, with a view to ensuring the continued success of the Group.
- Review the Group's policy on Diversity, Respect and Inclusion (see www.pennon-group.co.uk/about-us/governance-and-remuneration), including gender, and the progress against objectives.
- Review membership of the Board Committees.

The Committee maintains its strong interest in the Group's progress in championing diversity, whether gender, ethnicity, or social mobility, and regularly reviews the demographics of the workforce as well as the leadership and was pleased to see Pennon shortlisted in the Balance in Business awards.

The Nomination Committee met four times during the year to fulfil the duties set out in its terms of reference.

Only the members of the Committee are entitled to attend the Committee meetings, although other regular invitees to Committee meetings during the year included the Group Chief Executive Officer, the Group Chief People Officer and the General Counsel and Company Secretary. Committee members are also excluded from participating when their own positions are under discussion.

Further information on the Board biographies, can be found on pages 102 to 104.

Board diversity

At Pennon, we believe that a diverse and inclusive culture is a strategic imperative, treating it in the same way as we do each strategic priority - setting the tone from the top, holding leaders accountable and delivering against a clear action plan.

We believe having a diverse mix of minds has helped to deliver a step change in our culture, as a more caring and considerate business, that places significant focus on wellbeing, and evidenced in achieving Great Place to Work status for two years running.

As at 31 March 2023, female representation on the Board stood at 56% and Pennon Executive gender diversity at 44%. Our overall score in the Bloomberg GEI scorecard increased to 69.6%, up from 65% and reflecting a disclosure score of 97% for 2022. We also maintained first place in the FTSE Women Leaders Review for utilities.

Despite progress across the FTSE, Pennon is still one of only a few businesses in the UK to have both a female Chief Executive Officer and Chair. Given this, we have continued our membership of the 30% Club, and I am an ambassador of 25 x 25, the initiative to increase the number of women CEOs in UK business.

The Group is an advocate of Sir John Parker's review for ethnic board diversity, meeting the external targets required of a responsible and inclusive business ahead of the required dates. This year, in line with our commitment to the Change the Race Ratio campaign, we have voluntarily published our ethnicity pay gap of 10.3%. The Committee will continue to monitor pay gaps. Building our representation across the Group is a focus, given the area we serve has lower representation than the national average where ethnic representation is 2.2%. Nonetheless we are making good progress and our ethnic diversity across the Group has improved to 3%.

Board Diversity and Inclusion policy

The Board requires the Committee to review and monitor compliance with the Board's Diversity and Inclusion Policy and report on the targets, achievement against those targets and overall compliance in the Annual Report each year. The Policy was reviewed in March 2023.

The Board's diversity and inclusion policy confirms that the Board is committed to:

- The search for Board candidates being conducted, and appointments made, on merit, against objective criteria whilst promoting the widest forms of diversity, including gender, social and ethnicity. In this context, the Board will endeavour to achieve and maintain:
  a. A minimum of 40% female representation on the Board
  b. A minimum of 40% female representation on the Group's senior management team
  c. At least one member of diverse ethnicity on the Board
- Satisfying itself that plans are in place for orderly succession of appointments to the Board and senior leadership
- Maintain an appropriate balance of skills and experience within the Group and on the Board.

The approach to Company-wide diversity is detailed on page 37 and is also fully applicable to our Remuneration, Audit and Nomination Committees, and as each Committee is comprised of members of the Board, the Board's Diversity and Inclusion Policy detailed above, similarly applies. I can confirm we exceed the Policy.

Colleagues are asked to provide personal information for the purposes of monitoring equality and for statutory reporting purposes, including Gender Pay Gap. This is collected during recruitment and on-boarding and colleagues are asked to periodically review and update as necessary. Information is stored on the Group's HR management system, including the data used to populate the table on the following page. Employees are encouraged to provide information on a voluntary basis.

The ethnic representation of our Board and leadership

	Number of Board members	% of the Board	Number of senior Board positions (CEO, CFO, SID, Chair)	Number in executive management	% of executive management
White, British or other White (incl. minority white groups	7	78	4	9	100
Mixed / multiple Ethnic Groups	0	-	0	0	-
Asian / Asian British	0	-	0	0	-
Black / African / Caribbean / Black British	2	22	0	0	-
Other ethnic group including Arab	0	0	0	0	-
Not specified / prefer not to disclose	0	0	0	0	-

The gender representation of our Board and Leadership

	Number of Board members	% of the Board	Number of senior Board positions (CEO, CFO, SID, Chair)	Number in executive management	% of executive management
Men	4	44	2	5	57
Women	5	56	2	4	43
Other categories	0	-	0	0	-
Not specified / prefer not to disclose	0	-	0	0	-

Talent management and succession planning

During 2022/23 we have overseen the reshaping of the wider executive, ensuring that the Group has the requisite skills and experience and breadth of talent to meet the Group's longer-term strategic objectives. As we worked to enact our integration blueprint, following the acquisition of Bristol Water, Paul Boote became Group Chief Financial Officer. At the same time, we strengthened the overall executive with the external appointments of Andrew Garard as General Counsel and John Halsall as Chief Operating Officer. Mel Karam, Chief Executive Officer of Bristol Water, post the TUPE transfer of Bristol Water to South West Water, chose to step down. The Committee thanks him for his six years of service.

The Committee, supported by the Group Chief People Officer, also regularly reviews both the executive and non-executive leadership as part of its standing agenda, reviewing both short- and long-term skills requirements, opportunities for positive support to minority groups, and early identification of high potential. In line with our commitment to Change the Race Ratio, we have set stretching targets to develop diversity in our leadership levels below Executive Committee level and the Committee will continue to review progress on this important goal. As part of the regular reports received by the Committee, rates of participation by many characteristics are provided, noting this is also subject to employees' wish to disclose certain characteristics or sensitive information.

Board effectiveness review

The Board undertakes a formal and rigorous review of its performance and that of its Committees and Directors each year. This ensures that they continue to operate effectively and are identifying opportunities for improvement and best practice, as well as helping to inform future agenda items and areas of focus. This year the review was undertaken by a third party, Equity Culture, by means of online interviews with a number of the Board, in consultation with the Chair and respective Committee Chairs, in January and February 2023. The outcome of the review concluded that the Board, its Committees, and individual Directors continued to demonstrate a high degree of effectiveness and collaboration, and that the Board had a forward-thinking mindset and a good understanding of opportunities for growth and risks facing the business, and the table shows the positives, negatives and/or actions suggested. In parallel with the Board effectiveness review the Committee undertook a 360 degree evaluation of the executive committee members and ensured the feedback was shared with the Group's senior leadership.

Summary of evaluation

	Area of assessment	Commentary/feedback	Actions
Pennon Board	Conduct of meetings	• The Board is open, honest, respectful, engaged and committed	
	Board meetings, papers and presentation	• The volume of papers provides a challenge for the Board to manage but this reflects the open culture of the Group • The annual cycle of Board meetings and topics is appropriate. • There is a reassuring balance between appropriate challenge and support between NEDs and Executive • The meetings are well-managed • Governance is a strength of the Group	• Review the structure of Board papers
	Board oversight	• Maintain increased visibility around pollutions.	• Continue to ensure appropriate processes for monitoring, reporting and addressing pollution incidents
	Group strategy and Governance	• The Board continues to provide helpful support to management • The Board offers good strategic direction and governance	• Key themes are developing strategic lines of communication to drive climate delivery and growth
	Communications strategy	• The Board is keen to help with advocacy • Further Board appointments could consider broadening the expertise in regulatory and Government affairs	• Ensure the Group has the appropriate capacity to meet its challenges

	Area of assessment	Commentary/feedback	Actions
	Succession and talent planning	• Recent Board and Executive appointments have been very positive • The appointment of a new SID and Chair is high on the priority list of the Board • The CEO is very highly regarded	• The bench strength of the Executive needs to be kept under review
	Strategy	• The annual strategy day is well received • ESG matters are well embedded • Social initiatives are high on the Group's agenda	• The focus should remain on ensuring that the Group has the human resources to deliver its ambitions
	Risk	• The Group has good structures and processes in place • Scrutiny of risk remains a priority for the Board agenda	• Top-level risks should be regularly reviewed
	Committees	• The Committees work well and are well chaired • The frequency of meetings of the Health and Safety Committee should be kept under review	
Audit Committee	Committee operation and effectiveness	• The Audit Committee provides useful support to the Board and management • The Committee operates good governance, is up to date with changing legislation and has a strong relationship with financial management • Overall, it was felt that the Audit Committee functions well, with multiple members with deep finance experience	• Continue with existing processes
ESG Committee	Committee operation and effectiveness	• Relationships and communication between the ESG Committee and key executives are open and constructive • The Committee makes effective use of KPIs and benchmarking to understand ESG performance, with external sustainability performance reported on regularly • Overall, the Committee provides good direction in an ever-evolving area and has developed well over the last 18 months • Environmental issues particularly around CSOs have emerged more prominently this year • The Committee and the Board have work to do, to deal with the pollutions and CSO challenges, with the right executive support	• Ensure sufficient flexibility to further improve Net Zero activities and outcomes • Continue the vital focus on environmental issues and CSOs • Continue to review and assess processes in this area
Remuneration Committee	Committee operation and effectiveness	• The Remuneration Committee has performed well, with well-honed processes and in noting the evolving external environment	• Continue to evolve the framework as required and build on existing processes
Nomination Committee	Committee operation and effectiveness	• The Nomination Committee has performed well and needs to continue its track of Board succession planning and Executive succession activities	• Continue with existing processes, focused on succession
H&S Committee	Committee operation and effectiveness	• The H&S Committee provides effective support to both the Board and management • The Committee is now well established and focused on supporting the Board's aspirations with recent reports on investigations felt excellent.	• A developing Committee that should continue its deep dives into H&S performance and incidents.

A key area for focus in 2023/24 will be seeking a successor for the role of Chair. The current Board reflects Pennon's commitment and belief in the importance of diversity, and Pennon will be mindful of both the Company-wide and Board-specific diversity policies when selecting a replacement Chair. The succession planning process will consider candidates from diverse backgrounds, experiences, and perspectives and we will provide an update on the process followed in next year's report. As detailed on page 117 the Board recommended an extension of up to three years to the Chair's term from July 2021, as being appropriate, to provide continuity during the strategic business review and acquisition of Bristol Water. Shareholders voted in favour of this decision. The addition of Loraine and Dorothy to the Board means this is the right time to review the responsibilities of Board members ensuring we are maximising skills to best lead the Group for the future. The process of seeking a successor for the Chair will be led by the Senior Independent Director with no involvement from the current Chair.

Gill Rider
Chair

31 May 2023

Health and Safety Committee report

The Health and Safety Committee promotes a culture of safety within the Company.

Jon Butterworth
Chair of the Health and Safety Committee

Committee members	Date of appointment to Health & Safety Committee	Attendance
Jon Butterworth	November 2020	✓✓✓✓
Gill Rider	November 2020	✓✓✓✓
Iain Evans	November 2020	✓✓✓✓
Susan Davy	November 2020	✓✓✓✓
Paul Boote	November 2020	✓✓✓✓
Neil Cooper[1]	November 2020	✓✓✓
Claire Ighodaro[1]	November 2020	✓✓✓
Dorothy Burwell	December 2022	✓
Loraine Woodhouse[1]	December 2022	

1. Following a review of Board Committee composition, Neil Cooper, Claire Ighodaro and Loraine Woodhouse ceased to be members of the H&S Committee with effect from 31 January 2023.

Role of the Health & Safety Committee

- Review and challenge to support the Board and Executive on all matters connected to Health and Safety.
- Review the extent and effectiveness of the Group's reporting of health and safety performance and compare to external benchmarks.
- Regularly report to the Board.
- Advise the Audit Committee of any material non-financial risks.

The Committee's focus for 2022/23

During the year, the Committee considered a wide range of matters in the course of fulfilling its duties in accordance with its terms of reference:

- Six-monthly comprehensive reviews of the Group's Health & Safety performance.
- A review of the next phase of the HomeSafe strategy through to 2025.
- A deep dive into the wellbeing strategy with a focus on mental health.
- A review and challenge of potential near-miss events to ensure lessons are learnt.
- Visiting operational sites to engage with front-line colleagues and the wider Health and Safety teams.

Dear Shareholder

I am pleased to provide an update on the Health & Safety (H&S) Committee's activities during the year.

I believe the key to ensuring we keep employees safe and well in the workplace, is through empowering everyone to take responsibility for the health, safety and wellbeing of each other and for themselves. Simply put, it's about culture, leadership and accountability.

Our dedicated Board Committee focused purely on H&S ensures the Board continues to support our HomeSafe strategy and the Group's vision that everyone goes home safe every day. We continue to strive to be a leader of H&S by 2025 in our sector, and leadership from the top is critical. The Board has dedicated time to visit operational sites, discuss and review performance, offer support, encourage learning and meet leaders and employees from across the business.

Reviewing the Group's health and safety performance, effectiveness of health and safety policies and procedures, including the continued roll-out of the HomeSafe strategy, has been core, with significant improvements already noted.

Importantly, the Committee reviews deep dives of High Potential Incidents with a particular focus on lessons learned, getting to the root cause, encouraging a learning mindset.

I was personally delighted to be able to attend and present to over 170 colleagues at the first new Pennon Group H&S conference in Bristol in February this year, opened by Susan Davy. The conference was attended by representatives throughout the business from water treatment operational colleagues through to supply chain directors, with the aim of empowering everyone to recognise "It could happen to you" and "Take 5" to ensure it doesn't. This theme developed from an investigation into a High Potential Incident we reviewed at our Committee.

H&S Committee composition

All Board members are attendees and served throughout the year, with support from the Group Chief People Officer and Pennon's H&S Director.

Reporting

In addition to the regular Board report by the Group Chief Executive Officer, detailed performance is reviewed six-monthly, focusing on performance, benchmarking, and lead activities such as leadership and engagement, hazard rectification, asset health and working environment. The corresponding improvements in outcome metrics have been noted, with the Lost Time Injury Frequency Rate (LTIFR) reducing through the year by 15%.

The HomeSafe strategy continues to drive improvements and is regularly reviewed to ensure it drives us towards our 2025 aims. The Committee will continue to review and challenge plans and performance to support our HomeSafe ambitions, with a detailed roadmap to 2025 built on six key pillars.

Jon Butterworth
Chair of the Health and Safety Committee

31 May 2023

HomeSafe strategy

The Group's flagship H&S programme, HomeSafe, continues to provide the framework for driving significant improvements in all health and safety activities and impacts. HomeSafe is built on the six strategic pillars:

Managing Risk

Sharing and Learning

Working Together

Protecting Health

Enabling Leaders

Being Resilient

Read more on pages 35 and 36

Susan at the 'Keeping it flowing', Kier Live event, Exeter Racecourse, Devon

Remuneration Committee report

The role of the Remuneration Committee is to set and implement executive pay in a fair and socially responsible manner.

Role of the Remuneration Committee

- Ensure remuneration is aligned with the Group's strategy and reflects the values of the Group.
- Set and review the Remuneration Policy to ensure it remains appropriate, considering shareholders' views and best practice.
- Advise the Board on the framework of executive remuneration for the Group.
- Setting the remuneration for the Chair, the Executive Directors and senior executives of the Group and reviewing the remuneration arrangements of the wider workforce.
- Approve the design and determine targets for any performance-related pay schemes.
- Determine the appropriate outturn of any incentive arrangements.

The Committee's focus for 2022/23

- Consider the remuneration and terms of engagement of the Executive Directors, senior executives and Chair of the Group and the remuneration of the wider workforce.
- Determine targets that remain stretching, relevant to the Group's strategy and values and reflect best practice and wider stakeholders' views.
- Undertake the review of the Remuneration Policy, taking into consideration the Group's strategic goals, shareholders' views, regulatory commitments and evolving best practice, ahead of the 2023 AGM.

Claire Ighodaro
Chair of the Remuneration Committee

Committee members	Date of appointment to Remuneration Committee	Attendance
Claire Ighodaro	July 2020	✓✓✓✓✓
Gill Rider[1]	September 2012	✓✓✓✓
Neil Cooper	September 2014	✓✓✓✓✓
Iain Evans[1]	September 2018	✓✓✓✓
Jon Butterworth[1]	July 2020	✓✓✓✓
Loraine Woodhouse	December 2022	✓
Dorothy Burwell	December 2022	✓

1. Following a review of Board Committee composition, Gill Rider, Iain Evans and Jon Butterworth ceased to be members of the Remuneration Committee with effect from 31 January 2023.

Dear Shareholder

I am pleased to present the Directors' remuneration report for the year ending 31 March 2023.

We are a purpose-led business, shaped by our values and culture. Our approach to all matters, including pay, is informed by the perspective of our various stakeholders, including our investors, customers, colleagues communities and the environment.

The economic downturn over the past year has impacted the business, our colleagues and our customers. Climate-related issues have also dominated the landscape, and the driest, hottest summer on record for the region resulted in record demand for water. With this challenging backdrop, we are mindful of the need to build and maintain trust on the sensitive topic of executive pay, by clearly demonstrating our commitment to socially responsible business.

Despite the external backdrop, this has been a year of progress. Our robust performance over the last financial year has created c.£198 million cumulative out-performance over K7 to date, enabling reinvestment that will improve service quality over the longer term. We have reduced storm overflow use by 30% and have maintained 100% bathing water quality for the second year in a row. We also remain on track to deliver our ambitious Net Zero programme by 2030. However, it is recognised that there remains scope for improvement in certain areas as we work towards our stretching ambitions. Although our PBT and EPS results reflect the impact of exceptional levels of UK inflation on our debt instruments, the underlying financial results remain robust as demonstrated by EBITDA of £307.8 million.

We were able to keep bills lower than inflationary increases. We have increased the number of customers benefiting from one or more of our social tariffs by 23%. The second phase of our innovative WaterShare+ scheme was also launched in November 2022, and almost 90,000

customers have opted to become shareholders, via the scheme, since its introduction in 2021.

Supporting our colleagues

We are proud to be the largest employer in the region, with c.3,000 employees. The global financial pressures which face our customers, are also affecting our colleagues. Building on the support that was provided during the pandemic, the business has continued to support our colleagues during the well-documented cost-of-living crisis.

The 2023 pay settlement represented our largest-ever pay award, in recent times, with a focus on higher increases for lower-paid, customer-facing roles. The increase of 7% was backdated to 1 January 2023, which further enhanced the effective increase for the year to 9.2%. Increases for more senior roles were scaled down, with those earning in excess of £80,000 awarded an increase of 4.6%. The 2023/24 increases for Executive Directors were capped at 3.5%.

The business also implemented a rounded package of measures to support employees, including wellbeing support, access to financial information and guidance through an external provider and hardship support. An interim bonus payment was paid to front-line teams.

Our HMRC-approved share schemes continue to be popular with c.60% of colleagues in either the Sharesave or Share Incentive Plan. During the year, our 2017 five-year plan and 2019 three-year plan reached maturity with colleagues seeing growth of up to 45% on their investment. We have once again provided expanded disclosure on our approach for the wider workforce, and this is set out on page 140.

CEO incentives

The Chief Executive Officer's annual bonus for the 2022/23 financial year and the long-term share awards (LTIP) granted in 2020 subject to three-year performance to 31 March 2023, were each based on scorecards intended to capture a rounded assessment of overall performance. Based on the formulaic assessment of performance, the annual bonus delivered an outcome of 26% of maximum and the 2020 LTIP vested at 45% of maximum. Further detail on the targets and outcomes is set out in the main body of the report. There were clear areas of under and over performance, and this is reflected in the scorecard results. The Committee was satisfied that these outcomes fairly captured overall Group performance over the relevant performance periods.

However, having reflected on the exceptional economic backdrop, the Chief Executive Officer recommended to the Committee that her bonus and 2020 LTIP awards were foregone in full. An equivalent value is to be diverted into a future issuance under the Company's WaterShare+ scheme. The WaterShare+ scheme directly benefits our customers by either providing money off their bill or via ownership of Pennon shares.

While recognising the performance delivered, the Committee reflected on the broader environment and approved the Chief Executive Officer's recommendation regarding her awards. Therefore, the Chief Executive Officer's single figure for 2022/23 does not include any variable incentives and is significantly lower than outcomes in prior years.

Remuneration Policy review

Our current Remuneration Policy was last approved by shareholders in 2020. In accordance with the normal three-year renewal timetable, we will be seeking shareholder approval for a new Policy at our 2023 AGM.

We are not proposing any material changes to our Remuneration Policy, and therefore the previous policy has been largely rolled-forward. For the current year, we have instead focused on refining the metrics applicable to incentive awards (see below).

Overall remuneration levels under the policy remain modestly positioned against our FTSE 250 peers, and no increases are being proposed as part of the policy renewal. We also continue to have a number of safeguard mechanisms to avoid payments for failure including use of clear performance measures, stakeholder and other feedback, operation of a discretion framework before approving incentive outcomes and robust malus and clawback provisions.

However, the Committee is aware of the external environment, particularly in the context of our business plan submission for the next regulatory review cycle, due to Ofwat in October 2023. Following the AGM, we intend to undertake a review of our pay structure taking account of our strategic priorities and continuing best practice guidance. This review will reflect on the range of approaches seen in the market, from alternative performance metrics through to structural changes such as the use of restricted shares. We will also consider any refinements that are needed to in-flight arrangements. To the extent that further changes to the remuneration structure for Executive Directors are proposed, we will engage with our key stakeholders and seek relevant approvals.

Incentives for 2023/24 - clearer link to customers, communities and the environment

When considering the implementation of the policy for the coming year, the Committee was mindful of evolving Ofwat guidance on incentives for senior executives, in particular the desire for a substantial portion of awards to be linked to delivery for customers, communities and the environment.

For 2023/24, the annual bonus structure has been revised, and balances our focus on operational and strategic objectives related to customers, communities and the environment (60%) and maintains an appropriate weighting on financial results (40%).

For 2023 LTIP awards, the balance of measures has been refined to respond to both Ofwat guidance and recent feedback from our shareholders. A significant portion of the awards will be based on return on regulated equity (50% weighting, increased from 33%), as this is a key measure for our shareholders and the regulator. As the performance period concludes during the next price review period, the targets have been expressed as returns above the allowed cost of equity, but require the same level of out-performance as the 2022 LTIP. Customer experience has also been maintained as a measure (20% weighting). A new measure linked to water quality and the environment (30% weighting), has been introduced, with long-term objectives relating to our EPA rating, reductions in pollution incidents and combined storm overflows. The targets are detailed in the main body of the report.

Although the scorecard has been simplified by removing the sustainable dividend measure, we acknowledge the ongoing importance of the dividend to investors. In practice the continued focus on profitability in the bonus plan and RoRE in the LTIP will together ensure that the Company delivers strong and resilient financial performance, which in turn enables us to deliver sustainable returns to our shareholders and stakeholders over the long term.

The Remuneration Committee is very aware of the need to clearly demonstrate a measured and responsible approach to executive pay. Over a number of years we have a track record of taking a fair and modest approach and this has been reflected in voting support at previous AGMs and decisions set out in this year's report. In this context we look forward to your continued support at the 2023 AGM.

Claire Ighodaro CBE
Chair of the Remuneration Committee

31 May 2023

Directors' remuneration report

At a glance

What is the structure of executive pay?

	Year 1	Year 2	Year 3	Year 4	Year 5
Base salary	→				
Benefits	→				
Retirement Benefits	→				
Bonus: 50% in cash	→	50% deferred into shares for three years →			
LTIP: subject to three-year performance period		→		Subject to a two-year holding period →	
Shareholding guideline: Executive Directors are expected to build up a shareholding equivalent to 200% of salary				→	

What safeguards are in place?

Robust performance conditions
Variable pay linked to a rounded assessment of performance against stretching targets

→

Discretion framework
Holistic review of performance to consider if formulaic incentive outcomes are fair and appropriate

→

Deferral and holding periods
Bonus and LTIP awards are deferred for a further period to provide long-term alignment

→

Malus and clawback
Provisions in place for variable pay to safeguard against payments for failure

How does executive pay link to our strategy?

Performance measures	Customer measures ●●	ESG ●●●	Water quality ●●●	Profit measures ●●	Return on Regulated Equity ●●
2023/24 bonus	✓	✓	✓	✓	
2023 LTIP	✓	✓	✓		✓

Our Strategic pillars: ● Growth in Environmental Infrastructure ● Pioneering Solutions ● Leadership in UK water

How did we perform?

Performance highlights

£358m record capital investment
part of our largest environmental programme to date

c.50% reduction in wastewater pollution incidents
in K7 to date

100% bathing water quality
for the second consecutive year

>50% RCV growth forecast over K7
including our successful acquisition of Bristol Water

Investing c.£160m
in renewable energy generation

c.£40m returned to customers in K7
through our unique WaterShare+ mechanism

What were the outcomes under the incentive scorecards?

2022/23 bonus outcome (% of max)

Customer & Operational (30%)	36%
ESG (20%)	78%
Financial (50%)	0%

CEO: Nil — Bonus forgone
CFO: 26% — of max

2020 LTIP vesting outcome (% of max)

EPS (40%)	0%
Sustainable dividends (40%)	85%
RoCE (20%)	55%

CEO: Nil — 2020 LTIP award waived
CFO: 45% — of max

What were the remuneration outturns for 2022/23?

Susan Davy (CEO)

22/23	£543k
21/22	£1,527k

Paul Boote (CFO)

22/23	£644k
21/22	£618k

■ Fixed pay ■ Bonus (cash) ■ Bonus (shares) ■ LTIP

Summary of Remuneration Policy and Implementation in 2023/24

The previous Directors' Remuneration Policy was approved by shareholders at the 2020 AGM and continues to operate as intended. Although no major changes are proposed, a new policy will be presented for approval at the 2023 AGM in line with the normal three-year cycle. The 2023 Directors' Remuneration Policy is set out in full on pages 152 to 157.

Fixed Pay

No change in policy

Salary increases below that of the wider workforce.

Retirement benefits aligned with maximum rate available to wider workforce.

Salary

The Group Chief Executive Officer respectfully declined salary increases for both 2021 and 2022. Salary increases effective for 2023/24 for the wider workforce range from 9.2% for colleagues on lower and mid pay ranges, to 4.6% for those earning over £80,000. Increases for Executive Directors have been capped at 3.5%.

Salaries from 1 April 2023: Group Chief Executive Officer – **£491,625** Group Chief Financial Officer – **£319,815**

Benefits, including pension-related benefits

Benefits currently include the provision of a Company vehicle, fuel, health insurance, income protection and life assurance. Other benefits may be provided if the Committee considers it appropriate. Executive Directors may participate in HMRC approved all-employee share plans on the same basis as employees.

Executive Directors pension-related benefits are in line with the maximum rate available to the wider workforce (10% of salary).

Annual Bonus

No change in policy

Maximum potential is unchanged for 2023/24 at 125% of salary.

Normally 50% of bonus is deferred into shares released after three years.

Malus and clawback provisions apply.

For 2022/23 our bonus was based on:

Customer + operational (30%)	Basket of service and customer metrics
ESG (20%)	Basket of measures linked to environment, social goals and good governance
Financial (50%)	Underlying PBT

2023/24 - Clearer link to Customer, Communities and Environment

For 2023/24, increased portion of bonus linked to measurable goals that are key to meeting goals for our customers, communities and the environment:

- **Financial metrics (40%) –** stretching profit objective
- **Customers, communities and the environment (60%) –** scorecard of various metrics linked to operational, customer and environmental performance as well as broader ESG metrics.

Details of bonus targets are closely aligned to strategy, and as such are considered commercially sensitive. Further disclosure will be provided on a retrospective basis in next year's report.

Long-term incentive plan (LTIP)

No change in policy

Maximum annual award is unchanged for 2023/24 at 150% of base salary.

Three-year performance period, two-year holding period.

Malus and clawback provisions apply.

2022 LTIP targets:

Measure	Threshold (100%)	Maximum (100%)
Return on Regulated Equity (33.3%)	6%	8%
Sustainable dividends (33.3%)	2.6x	3.6x
Basket of customer measures (33.3%)	Basket of customer measures, includes C-MeX, R-MeX, D-MeX, MPS and our Trustpilot Score	

2023 LTIP - Clearer link to customer, communities and environment

For the 2023 LTIP, RORE will be up-weighted to 50%, increasing from 33%. An element linked to Water quality and the Environment will be introduced, with the balance of the award linked to Customer Experience. An underpin continues to apply.

Measure	Weighting	Threshold	Maximum
Return on Regulated Equity (50%)		allowed cost of equity +1.81%	allowed cost of equity +3.81%
Water Quality and Environment (30%)			
Scorecard assessment based on various measures including:			
EPA	10%	• Improvement of EPA rating towards 4 star • Minimisation of Category 1-2 pollution incidents and material reduction of Category 3-4 incidents • Material reduction of Storm Overflows	
Wastewater Pollution reduction	10%		
Storm overflow reduction	10%		
Maximum vesting under this element would require out-performance across each performance area. Detailed metrics are deemed to be commercially sensitive. Full disclosure of targets and the basis for outcomes will be provided at the end of the performance period.			
Customer Experience (20%)			
Customer metrics (15%) C-Mex (60%), D-Mex, R-Mex, MPS (10% each) Trustpilot Score (10%)		Median 4.5	Upper-Quartile 5.0
WaterShare+ participation (5%)		Maintain	10% increase

Shareholding requirements

No change in policy

Executive Directors are expected to build up a shareholding equivalent to 200% of salary.

Departing Executive Directors will normally be expected to hold 200% of salary (or actual relevant holding, if lower) on departure, reducing to 100% of salary after 12 months.

Annual report on remuneration

Remuneration approach for wider employees

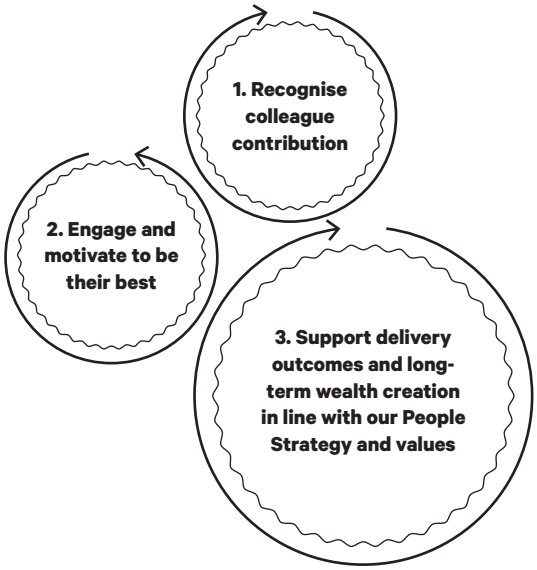
The Remuneration Committee pays close attention to the approach taken to remuneration for the wider workforce and considers this when making decisions regarding remuneration for the Executive Directors. The Committee reviews a pay dashboard twice a year, which contains information on elements of financial and non-financial reward, the wider labour market, demographics and pay statistics across the organisation. This detail provides important context to ensure that a consistent approach is adopted across the Group, including the Executive Directors. Progress in delivering the reward strategy is also reviewed regularly and the Committee reflects on progress made in relation to our gender and ethnicity pay gaps. Alongside this, the Committee hears feedback from employees from the RISE engagement forum through the CEO on matters concerning remuneration arrangements.

Reward strategy

Our well-established People Strategy across the Group is centred around talented people doing great things for customers and each other and creating the best place to work.

Our Reward Strategy

Pennon's Group Reward Strategy has three aims:



Supporting our colleagues

Salary increases for wider workforce

We have supported colleagues during the cost-of-living crisis, prioritising increases for those who need it most. For 2023/24, colleagues with a base salary below £40,000 have been awarded a pay increase of 7%. This was also backdated resulting in an effective increase of 9.2% for this population. For those earning between £40,000 to £80,000 a tapered approach has been taken, with those earning above £80,000, receiving a pay increase of 4.6% from 1 April 2023.

Interim bonus

We paid an interim bonus payment to all employees below leadership, helping colleagues meet the additional costs of Christmas at a time when they need it most.

Financial wellbeing and wider benefits

We offer a comprehensive package of support, including the roll out of a financial wellbeing partner for colleagues and their families, as well as hardship loans. We have also lifted the limits on our cycle to work scheme, enabling colleagues to take advantage of electric bikes (subject to affordability) helping them reduce their commuting costs and their own carbon footprint.

Saving for the future

Our Sharesave scheme was launched in 2022, enabling over 300 new participants to join, meaning that circa 60% of employees now enjoy one of the Group's share plans, having a stake and say in the business.

We have also rolled out participation in the Share Incentive Plan and our Sharesave scheme across Bristol Water.

Living Wage Foundation

In 2021, we announced our Living Wage Foundation (LWF) Accreditation. Further investment has been made in our critical customer service roles to maintain pay at a level above the LWF rates for all colleagues.

Wider workforce remuneration dashboard

In accordance with the 2018 UK Corporate Governance Code, the Committee reviews the level of information provided on pay matters in the wider organisation. The Wider Workforce Remuneration Dashboard provides the Remuneration Committee with an overview of the approach to pay across the Group:

- Helps support the Committee in reviewing workforce remuneration and related policies which continually evolves to provide greater insight
- Provides an overview of pay arrangements across the business and key statistics on pay in different areas of the business
- Updates on progress on our Reward Strategy implementation
- Oversight of the wider remuneration landscape to provide more external context, industry specifics and to inform on our developments on financial wellbeing
- Covers information on workforce demographics, employee engagement, gender pay, pay ratios, pension and benefits and incentive outcomes in different areas.

The Committee intends to keep the content of the dashboard under review to ensure it remains suitable.

Reward framework

Our Reward framework supports our People Strategy:

Talented people doing great things

For our customers and each other

- **Culture**
- **Attracting and retaining talent**
- **Training and competence**
- **Compliance**
- **People processes**
- **Leadership and succession**

Rewarded by our framework

Total reward = **Base pay** + **Variable pay** + **Saving for the future** + **Benefits**

Underpinned by the Pennon values

- **Trusted**
- **Responsible**
- **Collaborative**
- **Progressive**

Supported by:

Strategy and Governance, Job Evaluation and Benchmarking, Systems and Data

Pillar	Highlights
Base pay	The Group's overarching principles for basic pay are as follows: • Be competitive to support attraction and retention • Be fair, meeting all legislative requirements • Reflect the market and region in which the role operates • Reviewed annually – we engage with employee forums and trades unions as appropriate. The 2023 pay settlement represented our largest pay award in recent years, focusing on our lower-paid and customer- facing roles, see page 135. SWW is also proud to be one of the minority of UK companies to be an accredited Living Wage Employer and these standards apply to all Group companies.
Variable pay	The Group operates variable pay schemes, including annual bonus arrangements and all employees and temporary workers are eligible to participate. Throughout the main bonus schemes, there is strong correlation in the targets, to align the whole organisation on goals linked to customer, communities and the environment. The maximum bonus levels are based on seniority and level of responsibility. At leadership level a portion of the bonus is deferred into shares for three years. Long-term incentive share awards are available to senior executives and Executive Directors, consistent with market practice. Our front-line teams receive overtime, call-out and standby payments, ensuring that when workloads are high, employees benefit. We remain mindful of the need to balance working hours and available resource against the health, safety and wellbeing of our colleagues.
Saving for the future	Membership of the Group pension scheme remains high with a 96% participation rate in our Defined Contribution (DC) scheme. As part of our Saving for the Future, all employees can participate in our HM Revenue and Customs-approved Sharesave and Share Incentive Plan, with a strong emphasis on employee buy-in and ownership. In 2022, the Share Incentive Plan was launched to Bristol Water colleagues to sit alongside the Sharesave. 10% of eligible employees chose to participate. We supported the 2022 Sharesave with a number of drop-in sessions and presentations, ensuring new colleagues fully understood the schemes. We saw over 1,000 colleagues enter into a savings plan, of which c.330 were new to employee share ownership. Not only do our share schemes provide a mechanism for sharing in the long-term success of the Group, but mean that colleagues and customers have a say and stake in the business.
Benefits	Benefits are available to all colleagues. During 2023, the Group continued to build on the additional benefits to support employees' physical and mental wellbeing in line with our reward strategy. We have launched an online health programme providing self-assessment and guidance for a healthy life plan. Total Reward Statements are available through our Reward Hub platform and for Bristol through a flexible benefits platform. Our buy and sell holiday scheme launched in 2022, gives employees the opportunity to either have more holiday to suit their lifestyles or have more of their reward in cash to use for other benefits as they prefer. We have developed further the colleague support groups and Time to Talk sessions established in 2022. Financial wellbeing has grown in priority for colleagues this year and we have partnered with an external financial wellbeing service to deliver this much-needed support to colleagues and their families.

Gender and Ethnicity pay reporting

During 2022, in line with our Change the Race Ratio commitments, we published our Ethnicity Pay Gap data for the first time. The results reflect our journey in building representation of ethnic minority groups and gender diversity across Pennon, noting that the South West, where a large proportion of our business is based, has a lower diversity mix than other parts of the UK.

The mean ethnicity pay gap for the Group is 10.3%. Across the Group we have been working hard to attract a greater number of ethnically diverse candidates to apply for job vacancies, and we offer dedicated support to new employees through our graduate programme and support the 10,000 Black Interns Programme. We will continue to work to progress our diversity actions to build greater representation.

Our Group gender pay gap improved slightly during 2022 with an improvement of 0.8% - the gap for the Group now stands at 8.4%. As we look to develop female representation at all levels, we continue to create an environment for women to thrive and develop their careers.

During the year we have been recognised for our progression in gender equality by external bodies. In Spring 2023, Pennon was rated in the Bloomberg Gender Equality Index with an overall score of 69% up from 65% in 2022. The index measures gender equality across five key areas. Our placement in the FTSE Women Leaders report revealed we were again first in the Utilities sector.

We are committed to deliver on our ambitions to build diversity and inclusion across the Group and the water Industry.

Colleague engagement

In early 2022, we launched RISE our people forum, providing a two-way dialogue for all colleagues across the Group. This is regularly attended by senior leadership including the Group Chief Executive Officer, Group Chief People Officer and other members of the Pennon Executive. RISE is now embedded as an established group provoking healthy debate and discussion on areas that matter to employees. Engagement survey results and action planning are a discussion area for this group and as there is now a RISE member for every 30 employees, representation of all different departments and individuals is well catered for. This group continues to be a key source of dialogue and employee views for shaping future reward developments. The Committee is kept informed of themes and feedback from RISE discussions.

As we prepared to transfer Bristol employees to South West Water as an outcome of the statutory transfer, we conducted a thorough communication and consultation process with colleagues, with regular Town Hall events, meetings with union and employee representatives and regular team meetings. The transfer concluded smoothly on 1 February 2022.

The use of Yammer also continues to grow as a feedback loop for colleagues who can post questions and comments on any topic, creating the culture that enables colleagues to feel comfortable raising questions on remuneration is an important step in open dialogue. Employees can create groups for information sharing on wide-ranging topics from social activities to innovation ideas. We have seen colleagues use this to voluntarily share Health and Safety posts reflecting the success of colleagues' engagement with HomeSafe, a priority for the Group, as well as thoughts on energy saving, efficiencies, and well-being techniques.

The Big Chat, which is our regular cascade mechanism from the Executive, has regular sessions to inform colleagues on remuneration topics, such as the Sharesave launch, details of the annual salary review, benefits, and bonus news. Employees can post questions live during sessions or post follow up questions that will always be answered. The Big Chat is recorded to ensure that front-line workers who are not always able to attend can access these broadcasts and this is supported by a weekly newsletter to all employees.

We hold regular meetings with the union representatives, keeping them informed of business developments and the People Strategy and recognising their role for colleague feedback and the insights they can provide on behalf of their members. Their constructive approach to the 2023 pay settlement enabled us to pay colleagues as early as possible supporting them with the many cost increases that come in April.

We held our annual engagement survey in late spring of 2022 and were pleased that we were again accredited as a Great Place to Work for the second year running. As in prior years, local results are discussed and agreed at team level with Company-level actions agreed with our RISE representatives and the Executive Committee. Continuing our programme of wellbeing activities has been strongly supported by all colleagues. During 2023 we will be engaging with employees across the Group as we collectively continue to embed the Pennon values.

How our remuneration approach meets Section 40 of the UK Corporate Governance Code

Clarity – remuneration arrangements should be transparent and promote effective engagement with shareholders and the workforce.	The Committee advocates for transparent disclosure of remuneration arrangements, with full details of executive remuneration provided within the Remuneration Report each year. Incentive outcomes and the performance levels achieved against pre-set targets are clear. Consistent frameworks for annual incentives are used throughout all levels of the organisation, providing clarity of performance levels expected. The Committee welcomes dialogue on remuneration arrangements, with shareholders, our WaterShare+ Advisory panel and our colleagues either through our RISE panel or other employee forums.
Simplicity – remuneration structures should avoid complexity and their rationale and operation should be easy to understand.	The remuneration arrangements in place are simple, comprising base pay, pension, benefits, short-term and long-term incentive awards and in fundamental construct remain consistent over time. Performance ranges where applicable are straightforward in nature. Maximum remuneration levels are set within the policy.
Risk – remuneration arrangements should ensure reputational and other risks from excessive rewards, and behavioural risks that can arise from target-based incentive plans, are identified and mitigated.	Remuneration arrangements are carefully considered by the Committee, to ensure they reflect our values and those of a responsible business. Long-term sustainable performance is central to our delivery for all stakeholders and this is reflected in our long-term incentive plan, balancing both financial resilience and customer and environmental standards. All incentive payments are scrutinised by the Committee and levels of reward positioned so that excess is avoided. The provisions for malus and clawback are in place across all leadership schemes.
Predictability – the range of possible values of rewards to individual directors and any other limits or discretions should be identified and explained at the time of approving the policy.	The Remuneration Policy sets the maximum levels for variable remuneration and for retirement benefits and other benefits, these are aligned to the wider organisation. All incentive payments are carefully scrutinised by the Committee using a discretion framework to assess audited results and making adjustment as appropriate when considering wider performance outcomes.
Proportionality – the link between individual awards, the delivery of strategy and the long-term performance of the company should be clear. Outcomes should not reward poor performance.	Careful consideration is given to the stretching targets that are selected, taking into account the long-term strategy of the Group and the expectations of all our stakeholders.
Alignment to culture – incentive schemes should drive behaviours consistent with company purpose, values and strategy.	Delivery for customers, communities, the environment and all stakeholders is at the forefront of our incentive arrangements. The Committee receives regular information on remuneration outcomes and arrangements for the wider workforce, employee engagement and interacts with colleagues across the business.

Single total figure of remuneration table (audited information)

	Susan Davy[3] (£000)		Paul Boote (£000)	
	2022/23	2021/22[1]	**2022/23**	2021/22[1]
Base salary	**475**	475	**309**	300
Benefits[1] (including Sharesave)	**21**	29	**16**	17
Pension-related benefits[2]	**48**	55	**31**	30
Total fixed pay	**543**	559	**356**	347
Annual bonus (cash)	**0**	91	**51**	57
Annual bonus (deferred shares)	**0**	91	**51**	58
Long-term incentive plan[4,5,6]	**0**	786	**186**	156
Total variable pay	**0**	968	**288**	271
Total remuneration	**543**	1,527	**644**	618
Total fixed pay	**543**	559	**356**	347
Total variable pay (actual)	**0**	968	**288**	271
Total variable pay (forgone)	**440**	-	**-**	-

1. Benefits comprise a car allowance, fuel allowance, medical insurance, and income protection.
2. See page 145 for further information on retirement benefits.
3. For 2022/23, the CEO recommended that her bonus and 2020 LTIP award were forgone in full. An equivalent value is to be diverted into a future issuance under the Company's WaterShare+ scheme. Further detail is provided in the narrative below.
4. For 2022/23, the 2020 LTIP has been valued based on the average share price during the three-month period to 31 March 2023 of 891.86p and a vesting outcome of 45%, as referred to on page 145, together with an estimate of the accrued dividends payable on the vesting shares. Of the vested amount, none of the award is attributable to share price appreciation over the performance period. Vested awards are subject to a two-year holding period
5. For 2021/22, the 2019 LTIP value reflects the share price at the date of vesting of 970.5p and a vesting outcome of 88.2%. The value includes accrued dividends over the vesting period. The Committee did not exercise any discretion in relation to share price changes. These LTIP awards are subject to a two-year holding period.
6. For 2021/22, the 2019 LTIP award granted to Paul Boote relates to his previous role, prior to his appointment to the Board but is included in the table above for transparency.

Notes to the single figure table

Fixed pay

For 2023/24, the Remuneration Committee awarded the Executive Directors a salary increase of 3.5%, effective from 1 April 2023. This was set with reference to the increases awarded to the wider workforce, which ranged between 4.6% to 9.2% depending on pay levels. For the Chief Executive Officer, this will be the first salary increase that she has accepted since she was appointed to the role in 2020.

Retirement benefits for both Executive Directors have been set at 10% of salary since appointment, which is aligned to the rate available to the majority of the wider workforce. Further detail on pension arrangements is set out on page 145.

Variable pay

CEO incentive awards

Further detail regarding the outcomes of the 2022/23 annual bonus and 2020 LTIP are set out in the relevant sections below. Both incentive awards are based on scorecards which consider performance from a number of different perspectives. The overall outcomes reflect this rounded assessment of performance.

In line with best practice, the Remuneration Committee considers the broader performance context before approving outcomes. Reflecting on the exceptional economic backdrop and in particular the cost-of-living crisis faced by many of our customers, the Chief Executive Officer recommended to the Committee that she forgo her 2022/23 bonus and 2020 LTIP award. The Company will instead divert an equivalent value into a future issuance under the Company's WaterShare+ scheme. The WaterShare+ scheme directly benefits our customers through either providing money off their bill or via ownership of Pennon shares.

While recognising the performance delivered, the Committee reflected on the broader environment and subsequently approved the Chief Executive Officer's recommendation regarding her awards. Therefore, the Chief Executive Officer's single figure for 2022/23 does not include any variable incentives and is significantly lower than outcomes in prior years.

Annual bonus outturn for 2022/23

Consistent with prior years, the bonus is based on a rounded assessment of performance. In line with regulatory guidance a substantial portion of the bonus is linked to delivery of stretching objectives for our customers, communities and the environment. The bonus includes profit measures which ensures that the Company maintains a focus on financial discipline, enabling us to invest in the future and deliver robust and sustainable performance for all of our stakeholders.

Whilst the Executive Directors have combined roles as Group Executive Directors and executives of the underlying water companies owned by the Group, in the interests of transparency, they continue to be incentivised under a single bonus structure. This ensures that there is an appropriate balance between Group measures and objectives directly linked to our regulated water businesses.

The table below provides further details on the annual bonus structure. As shown below, a significant portion of the bonus was linked to objectives relating to customer, communities and environmental measures.

	Link to strategy	Water business role	Group role
Customer & Operational (30% weighting)	Focus on customer and operational measures assessed by Ofwat, our customers, communities and wider stakeholders.	✓	
ESG – Natural (6.7% weighting)	Support our commitment to provide environmental stewardship and to support our customers and local communities.	✓	
ESG – Social (6.7% weighting)	Objectives include a number of elements which matter for our customers – including reduced carbon emissions, onsite water usage and diversity & inclusion.	✓	
ESG – Governance (6.7% weighting)		✓	✓
Financial (50% weighting)	Underlying profit before tax is a key measure of the Group's financial performance and is one of our LPIs. Overall financial stability enables us to continue to make sustainable capital investments which benefit our customers over the long term. Through the unique WaterShare+ scheme, customers have a direct interest which is aligned with our shareholders. They are therefore able to benefit directly from strong financial performance.	✓	✓

In recognition of the Executive Directors' broader roles, 70% of their remuneration is recharged to the individual water companies (50% to South West Water and 20% to Bristol Water) with the balance of 30% attributable to other Group activities including Pennon Water Services. In practice, this means that 87.5% of salary of the total opportunity is allocated to the water businesses and 37.5% of salary to the Group role.

For 2022/23, the detailed measures and corresponding outcomes are shown below:

Customer and operational measures – 30% weighting	Target	Actual outturn	Target achieved	Bonus outturn (% of element)
Measures				
Bathing water quality improvements	4 Cumulative	8 Cumulative	Yes	
Wastewater pollution incidents, per 10,000km sewer	23	62	No	
Internal sewer flooding, per 10,000 connections	1.58	0.68	Yes	
Sewer collapses per 1,000km	15.54	8.01	Yes	
Leakage (3-yr rolling average) SWW	113 Ml per day	113 Ml per day	Yes	
Leakage (3-yr rolling average) BRL	34.3 Ml per day	37 Ml per day	No	
Environment Agency EPA[1]	3 star	2 star	No	
CRI Water Quality Score SWW[1]	2	2.4	No	
CRI Water Quality Score BRL[1]	1.5	4.6	No	
Interruptions to supply per property SWW	5 mins 45 seconds	8 mins 42 seconds	No	
Interruptions to supply per property BRL	5 mins 45 seconds	8 mins 03 seconds	No	36.4%

1. Awaiting regulator confirmation in July 2023

ESG Measures – 20% Weighting	Target	Actual outturn	Target achieved	Bonus outturn (% of element)
Measures				
Reduce carbon emissions in support of our Net Zero strategy by 2030	65%	65%	Yes	
Increase renewable generation	7%	6.89%	No	
Reduce onsite water usage	5 Ml/d	6.13 Ml/d	Yes	
Great Place to Work accreditation	Maintain	Maintained	Yes	
Reduce Lost time injuries	22 (18% reduction)	28 (12% reduction)	No	
FTSE Women Leaders Review position (Hampton Alexander)	20th	14th	Yes	
Achieve a Sustainalytics ESG	75	80	Yes	
New debt through Sustainable Financing Framework	60% of new debt	100% of new debt	Yes	
Fair Tax Accreditation	Maintain	Maintained	Yes	77.8%

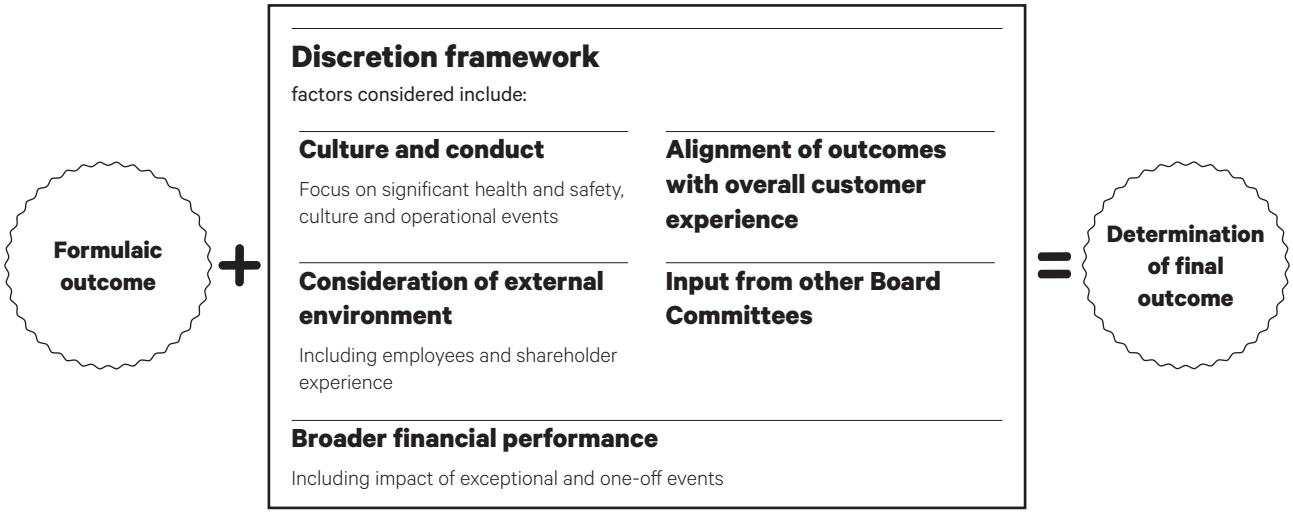
Group financial measures – 50% weighting

Financial performance for the bonus was based on underlying profit before tax. The outcomes for the year predominantly reflects the impact of the exceptional inflationary environment on finance costs. EBITDA for the year was £307.8m.

Measure	Threshold (£m)	Target (£m)	Maximum (£m)	Actual outturn (£m)	Bonus outturn (% of element)
Underlying PBT (50% weighting)	97.7	99.7	104.7	16.8	0 %

Assessment of overall performance

Each year, the Remuneration Committee undertakes a holistic review of performance to consider whether formulaic outcomes are appropriate in the context of overall performance. In line with best practice, the formal review process considers the following factors before approving outcomes for incentive arrangements.



For 2022/23, the Committee reviewed the formulaic outcome of the annual bonus against the various perspectives set out above. The Committee noted that there has been a drive to improve our underlying EPA performance, with a c.30% reduction in pollution incidents during 2022. There has been a similar reduction in the releases from storm overflows and our water resilience initiatives have continued to progress well. While targets had not been achieved in certain areas, this was reflected in the scorecard outcomes. Performance against our customer and operational and ESG elements were therefore considered to be appropriate.

While the formulaic outcome for the financial element reflected the external inflationary environment, the overall financial results were robust as reflected in delivery of operating profit of £153.1 million and Group Return on Regulated Equity of 10.5% for 2022/23 (South West Water 11.1%, Bristol Water 4.6%).

Taking into account the factors set out above, the Committee were satisfied that the bonus outcome fairly reflected underlying performance over the financial year. As noted above the CEO did not receive a bonus in respect of the year.

Bonus outturn

			Bonus outturn	
		Weighting	CEO	CFO
Customer & Operational measures		30%	10.9%	10.9%
ESG measures		20%	15.6%	15.6%
Financial measures		50%	0%	0%
Formulaic outturn	% of maximum	100%	26.5%	26.5%
	£000		£157k	£102k
Actual outturn			**Nil**	**£102k**

One half of the bonus paid to the Chief Financial Officer will be deferred into shares for three years. Malus and clawback provisions apply in relation to the bonus awards in respect of the year.

Long-term incentive outturn for 2022/23

The awards in the single figure table relate to the LTIP awards granted on 3 August 2020 which are due to vest on 2 August 2023. These share awards were subject to performance targets relating to earnings per share (EPS), sustainable dividends and return on capital employed (RoCE).

The table below provides an overview of performance against the targets set:

Measures	Threshold (25% of maximum)	Maximum (100% of maximum)	Achievement	Outcome (% of maximum)
EPS (40% of award)	30.8p	32.6p	7.3p	0%
Sustainable dividend measure (40% of award)	2.6x	3.6x	3.4x	34%
RoCE (20% of award)	8%	10%	8.8%	11%
			Overall vesting outcome	**45%**
			CEO's award	**Forgone**

1. Average of opening and closing capital employed.
2. For below-threshold performance for any of the performance conditions, 0% vests in respect of that performance condition.
3. Straight-line vesting between points.

Assessment of overall performance

Vesting of the award is subject to an 'underpin' relating to overall Group performance. Consistent with prior years and in line with industry best practice, the Committee utilises a structured discretion framework to support this review which considers performance from number of different perspectives. This review is intended to ensure vesting outcomes are justified based on an in-the-round assessment of performance.

For the 2020 LTIP, the following factors were noted:

- Substantial capital investment into future infrastructure to improve service quality – capital investment programme of c.£358 million, with investment in FY23 seeing a record increase of c.49% compared to the prior year.
- Supporting our customers –over £85 million customer benefits delivered over the regulatory period to date.
- Service delivery despite climate challenges – responding to record demand for water as a result of the driest, hottest year on record across the region.
- Sharing success – the second phase of our innovative WaterShare+ scheme was launched in November 2022, and almost 90,000 households have benefited from this scheme since launch.
- Water quality – continued progress but scope for improvement towards stretching goals.

As part of the review, the Remuneration Committee was mindful of recent Ofwat guidance for incentive awards to have a clearer link to customer, community and environmental objectives. The 2020 LTIP award was the final LTIP scheme to be based solely on financial performance. Since 2021, LTIP awards have included targets relating to customer performance, and as noted on page 154, for the 2023 LTIP grant a water quality measure has also been introduced. Further reassurance was provided by the fact the vesting outcome would have remained broadly similar if the targets for the 2023 LTIP had been retrospectively applied to the 2020 award.

Based on the factors set out above, and the strategic progress made by the Group, the Committee was satisfied that the vesting outcome of 45% of maximum represented a fair reflection of overall Group performance over the last three years. The grant price for this award was substantially higher than the price used the awards granted in the prior year, due to the market's positive response to the completion of the sale of Viridor in 2020. Therefore an adjustment for potential windfall gains was not deemed to be necessary.

The CFO's vested awards will remain subject a two-year holding period and will remain subject to malus and clawback provisions. As noted above the CEO has waived her right to this award.

Retirement benefits and entitlements (audited information)

Details of the Directors' pension entitlements and pension-related benefits during the year are as follows. Effective from 1 August 2020, the maximum pension contribution made by the Company is 10% of salary.

	Company contributions to defined contribution arrangements (£000)	Cash allowances in lieu of pension (£000)	Total value for the year (£000)	Age and date of retirement (for pension purposes)
Susan Davy	4	44	48	65 (17 May 2034)
Paul Boote	–	31	31	65 (29 June 2043)

Susan Davy received an overall pension benefit from the Company equivalent to 10% of her salary for the period 1 April 2022 to 31 March 2023. For 2022/23 this comprised an employer's contribution of £4,000 and a cash sum of £43,500. She is a member of Pennon Group's defined contribution pension arrangements and is entitled to access the retirement fund in the Master Trust from age 55.

The employer's contribution to the pension for Susan Davy is deducted from the overall pension allowance.

Paul Boote received a pension contribution of 10% of his salary. This is paid as a cash allowance of £30,900. He makes personal contributions to the Group's Defined Contribution pension scheme and is entitled to access the retirement fund in the Master Trust from age 55.

No additional benefits will become receivable by a Director if the Director retires early.

Non-Executive Directors' remuneration

Single figure of remuneration (audited)

	2022/23			2021/22		
	Fees (£000)	Taxable benefits (£000)	Total fees (£000)	Fees (£000)	Taxable benefits (£000)	Total fees (£000)
Gill Rider	232	0	232	225	0	225
Neil Cooper	88	0	88	86	0	86
Iain Evans	76	0	76	74	0	74
Claire Ighodaro	76	0	76	74	0	74
Jon Butterworth	68	0	68	66	0	66
Loraine Woodhouse[1]	23	0	23	-	-	-
Dorothy Burwell	21	0	21	-	-	-

1. A payment of £2,600 was made to Loraine Woodhouse in respect of attendance at the November Board meeting prior to commencement of her service agreement on 1 December 2022.

Non-Executive Directors' fees and benefits

During the year, the fees for Non-Executive Directors and Chair were reviewed and increased with effect from 1 April 2023. Fees were increased by 3.5%, which is below the average increase awarded to the wider workforce which ranged between 4.6% and 9.2% depending on pay level. The table below sets out the fee structure in full.

Non-Executive Director fees

Set at a market level to attract Non-Executive Directors who have appropriate experience and skills to assist in determining the Group's strategy.

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	From 1 April 2023	From 1 April 2022
Chair fee[1]	£239,860	£231,750
Basic Non-Executive Director fee	£64,550	£62,365
Additional fees		
Senior Independent Director	£10,660	£10,300
Chair of Audit Committee	£15,990	£15,450
Chair of Remuneration Committee	£13,870	£13,400
Chair of ESG Committee	£13,970	£13,400
Chair of Health and Safety Committee	£5,330	£5,150

1. When appropriate for the efficient carrying out of her duties, the Chair is provided with a driver and a vehicle. She is entitled to expenses on the same basis as for other Non-Executive Directors.

Directors' service contracts and letters of appointment

The dates of Directors' service contracts and letters of appointment and details of the unexpired term are shown below.

Executive Directors	Date of appointment	Notice period
Susan Davy	31 July 2020	12 months
Paul Boote	8 July 2020	12 months

A previous service contract dated 1 February 2015 was held by Susan Davy in respect of her appointment as Chief Financial Officer.

Non-Executive Directors	Date of initial letter of appointment	Expiry date of appointment
Gill Rider	22 June 2012	31 August 2024[1]
Neil Cooper	17 July 2014	31 August 2023
Iain Evans	16 June 2018	31 August 2024
Claire Ighodaro	1 September 2019	31 August 2025
Jon Butterworth	1 August 2020	31 July 2023
Loraine Woodhouse	1 December 2022	30 November 2025
Dorothy Burwell	1 December 2022	30 November 2025

1. Gill Rider was appointed as Chair of the Board as of 31 July 2020 and as such is providing ongoing strategic support and continuity of the Board until 2024.

The policy is for Executive Directors' service contracts to provide for 12 months' notice from either side. The contract has a normal retirement age of 67, except where otherwise agreed by both the Executive Director and the Company.

The policy is for Non-Executive Directors' letters of appointment to contain a three-month notice period from either side. All Non-Executive Directors are subject to annual re-election and letters of appointment are for an initial three-year term.

Copies of Executive Directors' service contracts and Non-Executive Directors' letters of appointment are available for inspection at the Company's registered office.

The dates of Directors' service contracts and letters of appointment and details of the unexpired term are shown above.

Outside appointments

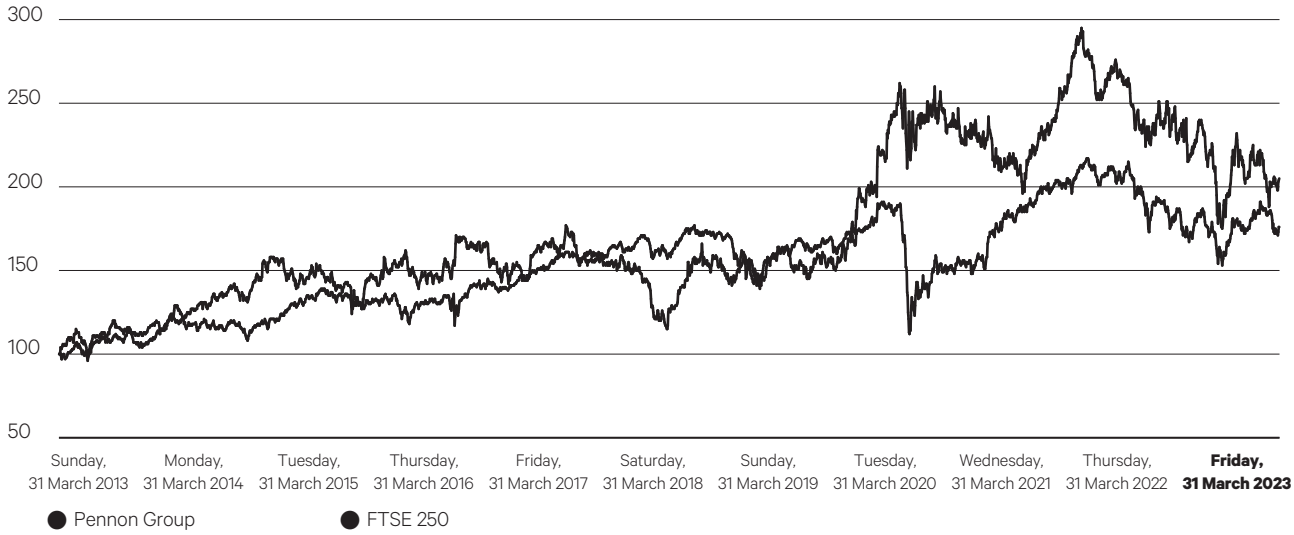
Executive Directors may accept one board appointment in another company. Board approval must be sought before accepting an appointment. Fees may be retained by the Director. Susan Davy remained a non-executive director of Restore plc throughout 2022/23. No other outside company appointments are held by the Executive Directors other than with industry bodies or governmental or quasi-governmental agencies.

Additional contextual information

Historical TSR

The graph below shows the value, over the 10-year period ended on 31 March 2023, of £100 invested in Pennon Group on 1 April 2013 compared with the value of £100 invested in the FTSE 250 Index. The FTSE 250 Index is a broad equity market index of which the Company was a constituent until the end of the period.

Total shareholder return – since April 2013



Historical Chief Executive Officer remuneration

As the Company did not have a Chief Executive Officer until 1 January 2016, the table below provides historical single figure information in the form of the average remuneration of the Executive Directors for years up to and including 2014/15. Their remuneration was considered to be the most appropriate to use as they were the most senior executives in the Company.

From 2015/16 onwards the Chief Executive Officer's remuneration for the year is shown.

	2013/14	2014/15	2015/16[1]	2016/17	2017/18	2018/19	2019/20	2020/21[2]	2020/21[2]	2021/22	2022/23[3]
	Average Executive Director	Average Executive Director	Chris Loughlin	Chris Loughlin	Chris Loughlin	Chris Loughlin	Chris Loughlin	Chris Loughlin	Susan Davy	Susan Davy	Susan Davy
Single figure of remuneration (£000)	962	762	1,119	1,318	1,153	1,351	2,135	1,337	1,930	1,527	543
Annual bonus pay-out (% of maximum)	67.6	68.2	84.0	84.0	87.0	91.0	78.0	79.2	78.1	30.7	0.0
LTIP vesting (% of maximum)	30.2	0.0	37.9	20.4	0.0	32.0	86.6	89.9	89.9	88.2	0.0

1. Group Chief Executive Officer for the year, including remuneration received between 1 April 2015 and 31 December 2015 when in position as Chief Executive of South West Water.
2. Chris Loughlin stepped down as Chief Executive Officer on 31 July 2020 and was succeeded by Susan Davy. Consistent with the single figure, the figures for Susan Davy relate to the whole of 2020/21, including the portion of the year when she was Chief Financial Officer. The LTIP award for Chris Loughlin was pro-rated to reflect service within the performance period.
3. For 2022/23, Susan Davy recommended that her bonus and 2020 LTIP were forgone. An equivalent value is to diverted into a future issuance under the Company's WaterShare+ scheme. Further detail is provided on page 142.

Percentage change in Directors' remuneration

The table below shows the annual percentage change in base salary, benefits and annual bonus of all Directors, including both Executive Directors and Non-Executive Directors, and all employees over the three financial years to 31 March 2023.

As Pennon Group plc has a relatively small number of employees, we have also shown below the percentage change against our UK employees. For comparison purposes, this is considered to be a more relevant peer group than the Pennon Group plc entity.

	Percentage change in salary /fees 2020/21	Percentage change in benefits 2020/21	Percentage change in annual bonus 2020/21	Percentage change in salary/fees 2021/22	Percentage change in benefits 2021/22	Percentage change in annual bonus 2021/22	Percentage change in salary/fees 2022/23	Percentage[3] change in benefits 2022/23	Percentage change in annual bonus 2022/23
Executive Directors									
Susan Davy	10.7%	0%	34.8%	4.2%	–23.0%	–58.4%	0%	-27%	-100%
Paul Boote	-	-	-	36.9%	27.0%	–44.7%	3.0%	-6%	-11.3%
Non-Executive Directors									
Gill Rider[1]	126%	0%	-	27.8%	–	–	3.0%	–	–
Neil Cooper[1]	16%	0%	-	7.5%	–	–	3.0%	–	–
Iain Evans[1]	4%	0%	-	1.4%	–	–	3.0%	–	–
Claire Ighodaro[1]	97%	0%	-	8.8%	–	–	3.0%	–	–
Jon Butterworth[1]	-	0%	-	34.7%	–	–	3.0%	–	–
Loraine Woodhouse[2]	-	-	-	–	–	–	n/a	–	–
Dorothy Burwell[2]	-	-	-	–	–	–	n/a	–	–
All employees									
Pennon Group plc	-11.8%	3.1%	10.7%	2.8%	–27.8%	-10.9%	4.2%	-30.4%	-73.5%
UK employees	1.22%	5.7%	17.8%	2.0%	–19.5%	-14.3%	3.9%	-20.3%	-45.4%

1. In July 2020, there were a number of changes to the composition of the Board and the Committees which has impacted the year-on-year percentage changes for 2020/21 and 2021/22. This includes the Chief Executive Officer and Group Chief Financial Officer who were appointed to their roles on 31 July 2020 and 8 July 2020 respectively. The Chief Executive Officer was previously in role as Chief Finance Officer. Full detail on these changes has been provided in the 2022 Directors' Remuneration Report.
2. Loraine Woodhouse and Dorothy Burwell were appointed to the Board 1 December 2022.
3. The percentage change in benefits is attributed to a reduction in the cost of vehicle leasing costs and reduced cost in healthcare premium.

Relative importance of spend on pay

	2022/23 (£ million)	2021/22 (£ million)	Percentage change
Overall expenditure on pay[1, 2]	98.9	90.4	9.4%
Distributions to ordinary shareholders	101.5	91.8	10.6%
Purchase of property, plant, and equipment (cash flow)	323.3	240.1	34.7%

1. Excludes non-underlying items.
2. Relates to continuing Group including Bristol Water.

The above table illustrates the relative importance of spend on pay compared with distributions to equity holders. The purchase of property, plant, and equipment (cash flow) has also been included as this was the most significant outgoing for the Company in the past financial year. Where relevant the numbers have been provided for the continuing Group to enable year on year comparability.

Chief Executive Officer pay ratio

Our CEO pay ratio stands at 16:1 for the median employee. This is considerably lower than the ratio in preceding years. This is predominantly due to the decision by the CEO to forgo her 2020 LTIP and the 2022/23 annual bonus award. Had the variable pay elements been paid to the CEO the ratio would have stood at 28:1.

Year	Method	25th percentile (P25) pay ratio	Median (P50) pay ratio	75th percentile (P75) pay ratio
2022/23[1] *actual outcomes*	A	20:1	16:1	12:1
2022/23[2] *formulaic outcomes*	A	36:1	28:1	21:1
2021/22	A	59:1	44:1	36:1
2020/21[3]	A	95:1	69:1	55:1
2019/20	A	87:1	68:1	50:1

1. For 2022/23, the CEO recommended that her bonus and 2020 LTIP award were forgone. An amount of the equivalent value is to be diverted into a future issuance under the Company's WaterShare+ scheme. The CEO pay ratio for this year therefore does not include any variable incentive pay.
2. This shows the values for 2022/23 had the CEO accepted her variable incentive pay awards.
3. The CEO ratio for 2021/22 is lower than previous years, partially due to the lower salary and pension benefit received by Susan Davy, compared to her predecessor. The total single figure used in the ratio in 2020/21 was a combined total single figure pro-rated to reflect the change in CEO mid-year.

Option A has been used for the calculations as per the disclosure regulations. The employees at the lower quartile, median and upper quartile (P25, P50 and P75 respectively) have been determined based on a calculation of total remuneration for the financial year 1 April 2022 to 31 March 2023.

Base salary for part-time employees and new joiners within the applicable period has been converted to full-time equivalents for the purpose of the calculations.

Estimated values for employee P11D data have been used to establish the ordering of employees, given the timing of publication. This will be validated and amended in due course to account for any variances.

The validated P11D data and restated total singe figure for the CEO for 2021/22 led to a small adjustment in the published ratios for P25, P50 or P75, leading to a revised ratio at median of 44:1 and reducing the ratio at P25 to 59:1.

For 2022/23 the total remuneration for the employees identified at P25, P50 and P75 is £27,035, £34,871 and £45,909 respectively. The base salary of 2022/23 for the employees identified at P25, P50 and P75 is £24,835, £31,244 and £37,223 respectively.

As the Committee spends a considerable amount of time on matters relating to remuneration arrangements for the wider workforce, we are comfortable that the median pay ratio is consistent with our wider policies on pay, reward and progression and reward for the Group as a whole. In a normal year, a greater proportion of the CEO's remuneration would be made up of the variable pay from their bonus and LTIP award. This year as the CEO has forgone her variable pay award, the value of total remuneration is considerably lower.

Share awards and shareholding disclosures (audited information)

Share awards granted during 2022/23

The table below sets out details of share awards made in the year to Executive Directors.

Executive Director	Type of interest	Basis of award	Face value £000	Percentage vesting at threshold performance	Performance/restricted period end date
Susan Davy	LTIP	150% of salary	713	25% of maximum	12 June 2025
Paul Boote			463		
Susan Davy	Deferred bonus	50% of bonus awarded	91		
Paul Boote			58	n/a	18 July 2025

LTIP awards were calculated using the share price of £10.376 being the average closing price over the five dealing days preceding the date of grant, which was 13 June 2022. LTIP awards are also subject to an additional two-year holding period. Deferred bonus awards were calculated using the average share price at which shares were purchased on the market on 19 July 2022 to satisfy the award, which was £9.8794.

Directors' shareholding and interest in shares

The Remuneration Committee believes that the interests of Executive Directors and senior management should be closely aligned with the interests of shareholders.

To support this the Committee operates shareholding guidelines of 200% of salary for both the Chief Executive Officer and Group Finance Director. Deferred bonuses and LTIP awards subject to a holding period only may count towards the guidelines on a net-of-tax basis. Shareholding requirements are noted on page 137.

The beneficial interests of the Executive Directors in the ordinary shares (61.05p each) of the Company as at 31 March 2023 and 31 March 2022 together with their shareholding guideline obligation and interest are shown in the table below.

	Share interests (including connected parties) at 31 March 2023	Share interests (including connected parties) at 31 March 2022	Vested LTIP awards in holding period[1]	Deferred bonus shares[1]	SAYE	Performance shares (subject to performance conditions)	Shareholding guideline	Shareholding guideline met?
Susan Davy	132,887	77,486	159,869	31,901	2,047	194,936	200%	Yes
Paul Boote[2]	29,554	13,571	36,885	16,160	2,047	126,098	200%	No

1. These shares awards are not subject to further performance criteria and may therefore count towards the guideline on a net-of-tax basis.
2. Paul Boote was appointed on 8 July 2020. It is therefore expected that his shareholding will be built up over the course of his tenure.

Since 31 March 2023, 97 and 66 additional ordinary shares in the Company have been acquired by Susan Davy and Paul Boote respectively as a result of their direct participation in the Company's Share Incentive Plan and reinvestment of dividends under that Plan via the Dividend Reinvestment Plan (DRIP). There have been no other changes in the beneficial or non-beneficial interests of the above Directors in the ordinary shares of the Company between 1 April 2023 and 1 June 2023.

Non-Executive Directors' shareholding

The beneficial interests of the Non-Executive Directors, including the beneficial interests of their spouses, civil partners, children, and stepchildren, in the ordinary shares of the Company are shown in the table below.

Director	Shares held at 31 March 2023	Shares held at 31 March 2022
Gill Rider	2,407	2,407
Neil Cooper	-	–
Iain Evans	-	–
Claire Ighodaro	-	–
Jon Butterworth	-	–
Loraine Woodhouse	-	–
Dorothy Burwell	-	–

There have been no changes in the beneficial interests or the non-beneficial interests of the above Directors in the ordinary shares of the Company between 1 April 2023 and 1 June 2023.

There is no formal shareholding guideline for the Non-Executive Directors; however, they are encouraged to purchase shares in the Company.

Shareholder dilution

The Company can satisfy awards under its share plans with new issue shares or shares issued from treasury up to a maximum of 10% of its issued share capital in a rolling 10-year period to employees under its share plans. Within this 10% limit the Company can only issue (as newly issued shares or from treasury) 5% of its issued share capital to satisfy awards under discretionary or executive plans. The percentage of shares awarded within these guidelines and the headroom remaining available as at 1 June 2023 is as set out below:

	Awarded	Headroom	Total
Discretionary schemes	1.5%	3.5%	5%
All schemes	4.7%	5.3%	10%

Details of share awards

(a) Long-term incentive plan

In addition to the above beneficial interests, the following Directors have or had a contingent interest in the number of ordinary shares (of nominal value of 61.05p each) of the Company shown below, representing the maximum number of shares to which they would become entitled under the plan should the relevant criteria be met in full. In 2021 ordinary shares were consolidated at a ratio of 3:2 following the payment of a special dividend to shareholders. For simplicity, outstanding LTIP awards did not accrue an entitlement to the special dividend and were therefore unaffected by the consolidation.

Director and date of award	Vested awards held at 1 April 2022[1,2]	Conditional awards held at 1 April 2022	Conditional awards made in year	Market price upon award year	Vesting in year[3]	Value of shares upon vesting (before tax) 2022	Vested awards held at 31 March 2023[4]	Vested awards released in year[5]	Conditional awards held at 31 March 2023	Date of end qualifying conditions to be fulfilled	Expected date of release
Susan Davy[6]											
25/08/17	74,045	–	–	802.70p	–	747	-	78,747	–	24/08/20	24/08/22
02/07/18	78,875	-	–	790.12p	–	928	78,875	–	–	01/07/21	01/07/23
04/07/19	–	82,062	–	752.72p	80,994	786	80,994	–	-	03/07/22	03/07/24
03/08/20	–	63,812	–	1071.90p	–	–	–	–	63,812	02/08/23	02/08/25
01/07/21	–	62,456	–	1140.80p	–	–	–	–	62,456	30/06/24	30/06/26
13/06/22	–	–	68,668	1037.60p	–	–	–	–	68,668	12/06/25	12/06/27
Paul Boote[7]											
25/08/17	15,961	–	–	802.70p	–	161	-	16,974	–	24/08/20	24/08/22
02/07/18	20,836	–	–	790.12p	–	245	20,836	–	–	01/07/21	01/07/23
04/07/19	–	16,261	–	752.72p	16,049	156	16,049	–	–	03/07/22	03/07/24
03/08/20	–	41,982	–	1071.90p	–	–	–	-	41,982	02/08/23	02/08/25
01/07/21	–	39,446	-	1140.80p	–	–	–	–	39,446	30/06/24	30/06/26
13/06/22	–	–	44,670	1037.60p	–	–	–	–	44,670	12/06/25	12/06/27

1. 86.6% of the awards granted on 25 August 2017 vested on 24 August 2020 at a market price of £10.085 per share.
2. 89.9% of the awards shares granted on 2 July 2018 vested on 1 July 2021 at a market price of £11.7698 per share.
3. 88.2% of the awards granted on 4 July 2019 vested on 3 July 2022 at a market price of £9.705 per share.

In respect of (1), (2) and (3) above, the total number of shares that vested included additional shares equivalent in value to such number of shares as could have been acquired by reinvesting the dividends which would otherwise have been received on the vested shares during the three-year performance period. The balance of the award lapsed.

4. Vested award; no longer subject to performance conditions.
5. Awards released in year at a market price of £9.8717 per share, inclusive of additional shares equivalent in value to such number of shares as could have been acquired by reinvesting the dividends which would otherwise have been received on the vested shares during the two-year holding period.
6. Following year-end, the CEO recommended that her 2020 LTIP award was forgone.
7. Paul Boote's LTIP awards include those he received in his previous position as Director of Treasury, Tax and Group Finance, in which he will retain an interest following his appointment to the Board as Group Finance Director on 8 July 2020.

(b) Annual incentive bonus plan – deferred bonus shares (long-term incentive element)

The following Directors had or have a contingent interest in the number of ordinary shares of the Company shown below, representing the total number of shares to which they have or would become entitled under the deferred bonus element of the Annual Incentive Bonus Plan (the bonus plan) at the end of the relevant restricted period:

Director and date of award	Restricted awards held at 1 April 2022	Restricted awards made in year	Market price of each share upon award in year	Restricted awards post-share consolidation (restated)[1]	Released in year[2]	Value of shares upon release (before tax) £000	Restricted awards held at 31 March 2023	Date of end of restricted period
Susan Davy								
24/07/19	24,449	–	755.5386p	16,299	16,299	160		
14/07/20	15,011	–	1079.47p	10,007	–	–	10,007	13/07/23
30/06/21	18,993	–	1150.45p	12,661	–	–	12,661	29/06/24
19/07/22		9,233	987.94p	–	–	–	9,233	18/07/25
Paul Boote[3]								
24/07/19	9,033	–	755.5386p	6,021	6,021	59		
14/07/20	5,026	–	1079.47p	3,350	–	–	3,350	13/07/23
30/06/21	10,469	–	1150.45p	6,979	–	–	6,979	29/06/24
19/07/22		5,831	987.94p	–	–	–	5,831	18/07/25

1. All shares held under the AIBP at the 5 July 2021, were adjusted on that date to reflect the share consolidation activity at a ratio of 3:2 into shares of 61.05p each.
2. These shares were released on 23 July 2022 at 979.75p per share.
3. Paul Boote's deferred bonus share awards include those he received in his previous position as Director of Treasury, Tax and Group Finance, in which he will retain an interest following his appointment as Group Finance Director on 8 July 2020.

During the year, the Directors received dividends on the above shares in accordance with the conditions of the bonus plan as follows: Susan Davy £17,491; Paul Boote £7,864.

(c) Sharesave Scheme

Details of options to subscribe for ordinary shares (61.05p each) of the Company under the all-employee Sharesave Scheme were:

Market value

Date of award	Options held at 1 April 2022	Granted in year	Exercised in year	Exercise price per share	Market price of each share on exercising	Market value of each share at 31 March 2023	Options held at 31 March 2023	Exercise period/ maturity date
Susan Davy								
06/07/21	2,047	–	–	879.00p	–	874.0p	2,047	01/09/24–28/02/25
Paul Boote								
06/07/21	2,047	–	–	879.00p	–	874.0p	2,047	01/09/24–28/02/25

The Remuneration Committee and its advisors

Claire Ighodaro and Neil Cooper were members of the Remuneration Committee throughout the year. Loraine Woodhouse and Dorothy Burwell joined the Committee on their appointment to the Board on 1 December. Gill Rider, Iain Evans, and Jon Butterworth stepped down from the Committee on the 31 January 2023, and now attend by invitation as required. During the year, the Committee received advice or services which materially assisted the Committee in the consideration of remuneration matters from Adele Barker (Group Chief People Officer) and from Deloitte LLP.

During 2018/19, Deloitte LLP was reappointed directly by the Committee with a refreshed advisory team, following a comprehensive re-tendering process. Deloitte LLP's fees in respect of advice which materially assisted the Committee during 2022/23 were £120,975 (arrived at from an hourly rate basis of charging). During the year, Deloitte LLP also provided broader reward services to the Group. Deloitte LLP is a member of the Remuneration Consultants Group and as such voluntarily operates under the code of conduct in relation to executive remuneration consulting in the UK. The Committee is satisfied that the advice it has received from Deloitte LLP has been objective and independent.

Statement of voting at general meeting

The table below sets out the voting by the Company's shareholders on the resolutions to approve the Directors' remuneration report at the 2022 AGM and the remuneration policy at the 2020 AGM, including votes for, against and withheld.

Annual report on remuneration (2022 AGM)	
For % (including votes at the Chair's discretion)	98.34
Against %	1.66
Withheld number	10,730,076
Remuneration policy (2020 AGM)	
For % (including votes at the Chair's discretion)	91.50
Against %	8.50
Withheld number	407,344

A vote withheld is not counted in the calculation of the proportion of votes for and against a resolution.

Directors' remuneration report compliance

This Directors' remuneration report has been prepared in accordance with the provisions of the Companies Act 2006 and the Large and Medium-sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013. It also complies with the requirements of the Financial Conduct Authority's Listing Rules and the Disclosure and Transparency Rules. The UK Corporate Governance Code also sets out principles of good governance relating to directors' remuneration, and this report describes how these principles are applied in practice. The Committee confirms that throughout the financial year the Company has complied with these governance rules and best practice provisions. The above regulations also require the external auditor to report to shareholders on the audited information within the annual report on remuneration which is part of the Directors' remuneration report. The external auditor is obliged to state whether, in its opinion, the relevant sections have been prepared in accordance with the Companies Act 2006.

The external auditor's opinion is set out on page 162 and the audited sections of the annual report on remuneration are identified in this report.

On behalf of the Board

Claire Ighodaro CBE
Chair of the Remuneration Committee

31 May 2023

Remuneration policy 2023

Introduction

The previous Directors' Remuneration Policy was approved by shareholders at the 2020 AGM on 31 July 2020. Under the normal three-year renewal cycle, a new Remuneration Policy, as described in this part of the report, will be presented to shareholders for approval at the 2023 AGM on 20 July 2023, and if approved will come into effect from this date.

The Directors' Remuneration Policy will be displayed on the Company's website at www.pennon-group.co.uk/investor-information, immediately after the 2023 AGM and will be available upon request from the Group Company Secretary.

Changes to remuneration policy

During the year, the Committee carefully considered the Director's remuneration policy for 2023, reflecting on its' purpose to incentivise performance, reward excellence and attract and retain Executive Directors. The current pay structure remains relatively conventional (i.e. bonus plus performance-based LTIP) and reflects mainstream FTSE market and best practice. Overall remuneration is modestly positioned against FTSE 250 peers and maximum incentive opportunities will remain unchanged under the proposed Policy.

As part of the Policy review, the Committee reflected on the expectations of Ofwat and shareholder input. Consideration was also given to the principles of clarity, simplicity, risk-management, predictability, proportionality and alignment to culture (see page 141 for further details). Input was sought from the management team, while ensuring that conflicts of interests were suitably mitigated.

In light of the quickly evolving external environment, and in particular the time-frame for submission of business plans for the next regulatory review cycle which are due to Ofwat in October 2023, the Committee determined that no major changes to our pay model should be proposed at this stage. The Policy set out on the following pages has therefore largely been rolled-forward from the previous Policy. Minor changes have been made to refine language in line with evolving market and best practice and to aid the operation of the Policy.

Following the 2023 AGM, the Committee intends to undertake a more comprehensive review of our pay structure. This review will take into account our strategic priorities, the upcoming price review and evolving best practice guidance. To the extent that further changes to the remuneration structure for Executive Directors are proposed, the Committee will suitably engage with our major stakeholders and seek relevant approvals as appropriate.

Future policy table – Executive Directors

The table below sets out the elements of the remuneration package for the Executive Directors.

Fixed pay	
Base salary	
Purpose and link to strategy	Set at a competitive level to attract and retain high calibre candidates to meet the Company's strategic objectives in an increasingly complex business environment. Base salary reflects the scope and responsibility of the role as well as the skills and experience of the individual.
Operation	Salaries are generally reviewed annually and any changes are normally effective from 1 April each year. In normal circumstances, salary increases will not be materially different to general employee pay increases. However, the Committee reserves the right to make increases above those made to general employees, for example in circumstances including (but not limited to) an increase in the scope of the role, or to reflect an individual's development in a role.
Maximum	When reviewing salaries the Committee has regard to the following factors: • Salary increases generally for all employees in the Company and the Group. • Market rates. • Performance of individual and the Company and/or development in the role. • Other factors it considers relevant. There is no overall maximum.
Performance framework	None, although individual and Company performance are factors considered when reviewing salaries.
Benefits	
Purpose and link to strategy	Benefits provided are consistent with the market and level of seniority to aid retention of key skills to assist in meeting strategic objectives.
Operation	Benefits currently include the provision of a company vehicle, fuel, health insurance and life assurance. Other benefits may be provided if the Committee considers it appropriate. In the event that an Executive Director is required to relocate, relocation benefits may be provided.
Maximum	The cost of insurance benefits may vary from year to year depending on the individual's circumstances. There is no overall maximum benefit value but the Committee aims to ensure that the total value of benefits remain proportionate.
Performance framework	None.
Pension-related benefits	
Purpose and link to strategy	Provides funding for retirement and aids retention of key skills to assist in meeting the Company's strategic objectives.
Operation	The Executives are eligible to participate in the Pennon Group Defined Contribution Scheme at the same level of benefit as the wider workforce. A cash allowance may be provided as an alternative and/or in addition where pension limits have been reached.
Maximum	The maximum pension benefit will normally be capped at a level comparable to the pension benefit available to the majority of employees. This is currently 10% of salary.
Performance framework	None.

Remuneration policy 2023 continued

All-employee share plans	
Purpose and link to strategy	Align the interests of all employees with Company share performance.
Operation	Executive Directors may participate in all-employee plans, including HMRC approved plans, on the same basis as employees.
Maximum	The maximum will be consistent with other employees. For HMRC approved plans, the maximum will be as prescribed under the relevant legislation governing the plans.
Performance framework	None.
Variable pay	
Annual bonus	
Purpose and link to strategy	Incentivises the achievement of annual performance objectives aligned to the strategy of the Company.
Operation	Annual bonuses are calculated following finalisation of the financial results for the year to which they relate. A portion of any bonus is deferred into shares in the Company which are normally released after three years. Normally 50% is deferred. Dividends (or equivalents) may be paid/accrued on deferred shares. Awards are subject to malus and clawback provisions. Further details are set out on page 154.
Maximum	The maximum bonus potential is 125% of base salary.
Performance framework	Performance targets may relate to financial, operational, strategic and environmental objectives, which are reviewed each year. Performance criteria will reflect strategic priorities and regulatory requirements. The level of payment for threshold performance will vary depending on the nature of the metric and the stretch of the target set. There is normally scaled payment for performance between the threshold and maximum performance hurdle. The measures, weighting and threshold levels may be adjusted for future years. Following the financial year end the Committee, with advice from the Chair of the Board and following appropriate input from other Board Committees, assesses the extent to which targets are met and determines bonus levels accordingly. The Committee may exercise its discretion in certain circumstances; further details are set out on page 154.
Long-term incentive plan (LTIP)	
Purpose and link to strategy	Provides alignment to the achievement of the Company's strategic objectives and the delivery of sustainable long-term value to shareholders.
Operation	Annual grant of conditional shares (or equivalent). Share awards vest subject to the achievement of specific performance conditions normally measured over a performance period of no less than three years. In addition, a two-year holding period will apply in respect of any shares which vest at the end of the three-year performance period. Dividends (or equivalents) may accrue on share awards that vest. Awards are subject to malus and clawback provisions. Further details are set out on page 154.
Maximum	The maximum annual award is 150% of base salary.
Performance framework	Performance metrics and targets are set to reflect the long-term strategic priorities of the Group. Performance criteria are linked to our long-term strategy and may include a combination of financial, operational and/or shareholder-related measures. An 'underpin' applies which allows the Committee to reduce or withhold vesting if the Committee is not satisfied with the underlying performance of the Company. No more than 25% of maximum vests for minimum performance. The Committee will keep the performance measures and weightings under review and may change the performance condition for future awards if this were considered to be aligned with the Company's interests and strategic objectives, as well as the impact of regulatory changes. In certain circumstances, the Committee may exercise its discretion and adjust performance outcomes. Further details are set out on page 154. The Committee would seek to consult with major shareholders in advance of any proposed material change in performance measures.
Shareholding guidelines	
Purpose and link to strategy	Create alignment between Executives and shareholders and promote long-term stewardship. During the course of their tenure, Executive Directors are expected to build up a shareholding equivalent to 200% of salary. Departing Executive Directors are also expected to retain a material interest in Company shares for two years after they step down from the Board. Executives will normally be expected to hold 200% of salary (or actual relevant holding, if lower) on departure, with the guideline reducing to 100% of salary after 12 months. This guideline will apply to all share awards vesting after the adoption of this remuneration policy.
Operation	The Committee retains discretion to waive this guideline in certain cases (e.g. compassionate circumstances).

Notes to the policy table

Performance measures and targets

There is a strong emphasis on performance related executive pay demonstrating a substantial link between rewards and delivery of stretching performance objectives. The performance conditions for the annual bonus and LTIP are selected by the Committee each year to provide a rounded assessment of performance including metrics which drive financial resilience and key performance indicators for customers, communities and the environment. These metrics are used by the Board to oversee the operation of the businesses.

In recent years, LTIP grants have been subject to targets linked to Return on Regulated Equity, sustainable dividends and customer performance. For 2023, we are proposing some refinement to ensure ongoing alignment with our strategic priorities by assessing performance against measures that drive long-term sustainable performance. A significant portion of the award will remain based on return on regulated equity, in recognition that this is a key measure for our shareholders and the regulator. The 2023 LTIP award will also be assessed against measures relating to customer experience and water quality and the environment. These measures have objectives linked to customer, communities and the environment and have been set with reference to our long-term strategic ambitions.

The Committee may amend performance measures, weightings and targets, in the context of the Company's strategy, the impact of changes to the regulatory framework, accounting standards and any other relevant factors.

The measurement of performance against performance targets and determination of incentive outcomes is at the Committee's discretion. Adjustments may be made to reflect underlying financial or non-financial performance of the individual or the Group, consideration of overall performance in the round, and/or circumstances unforeseen or unexpected when the targets were set. When making this judgement, the Committee may take into account all factors deemed relevant.

Performance conditions may also be replaced or varied if an event occurs or circumstances arise which cause the Committee to determine that the performance conditions have ceased to be appropriate. If the performance conditions are varied or replaced, the amended conditions must, in the opinion of the Committee, be fair, reasonable and materially no less difficult than the original condition when set.

The Committee would clearly disclose any material changes to performance measures, and seek shareholder views as appropriate.

Malus and clawback

Malus and clawback provisions apply to all incentive awards. These provisions enable awards to either be forfeited prior to delivery, repaid or made subject to further conditions where the Committee considers it appropriate in the event of any significant adverse circumstances. For awards granted under the term of this policy, the circumstances in which malus and clawback may be applied include a financial misstatement, error in calculation, material failure of risk management, serious reputational damage, serious corporate failure or misconduct. In respect of the annual bonus, clawback may be applied for the period of three years following determination of the cash bonus. Under the LTIP, clawback may be applied until the end of the holding period.

Discretion

In line with the 2018 Corporate Governance Code, the Remuneration Committee has ensured that they will maintain the ability to override the formulaic outcomes for future awards under the annual bonus and LTIP where the outcomes are not considered by the Committee to be appropriate (e.g., unreflective of underlying performance).

The Committee will disclose the use of any such discretion.

Operation of executive share plans

The long-term incentive plan will be operated in accordance with the rules of the plan as approved by shareholders. The deferred bonus awards will be governed by the rules adopted by the Board from time to time. Awards under any of the Company's share plans referred to in this report may:

- Be granted as conditional share awards, nil-cost options or in such other form that the Committee determines has the same economic effect
- Have any performance conditions applicable to them amended or substituted by the Committee if an event occurs which causes the Committee to determine an amended or substituted performance condition would be more appropriate and not materially less difficult to satisfy
- Incorporate the right to receive an amount (in cash or additional shares) equal to the value of dividends which would have been paid on the shares under an award that vests. This amount may be calculated assuming that the dividends have been reinvested in the Company's shares on a cumulative basis
- Be settled in cash at the Committee's discretion (e.g. due to regulatory limitations).

On a change of control or voluntary wind up of the Company, LTIP awards may vest to the extent determined by the Committee having regard to the performance of the Company and, unless the Committee determines otherwise, the period of time that has elapsed since grant. Deferred bonus awards may vest in full. Alternatively, participants may have the opportunity, or be required, to exchange their awards for equivalent awards in another company, although the Committee may decide in these circumstances to amend the performance conditions.

The Committee also has the discretion to treat any variation of the Company's share capital or any demerger, special dividend or other transaction that may affect the current or future value of awards as an early vesting event on the same basis as a change of control.

Detailed provisions

The Committee reserves the right to make any remuneration payments and/or payments for loss of office (including exercising any discretion available in connection with such payments) outside the policy set out above where the terms of the payment were agreed (i) before the 2014 AGM (the date the Company's first shareholder-approved directors' remuneration policy came into effect); (ii) before the policy set out above came into effect, provided that the terms of the payment were consistent with the shareholder-approved directors' remuneration policy in force at the time they were agreed; or (iii) at a time when the relevant individual was not a director of the Company and, in the opinion of the Committee, the payment was not in consideration for the individual becoming a director of the Company. For these purposes 'payments' includes the Committee satisfying awards of variable remuneration and, in relation to an award over shares, the terms of the payment are 'agreed' at the time the award is granted.

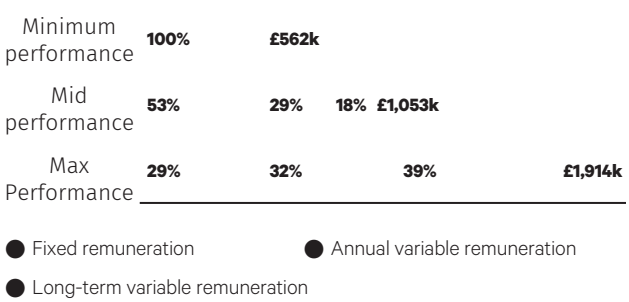
The Committee may make minor amendments to the policy (for example for regulatory, exchange control, tax or administrative purposes or to take account of a change in legislation) without obtaining shareholder approval for that amendment.

Differences in remuneration policy for all employees

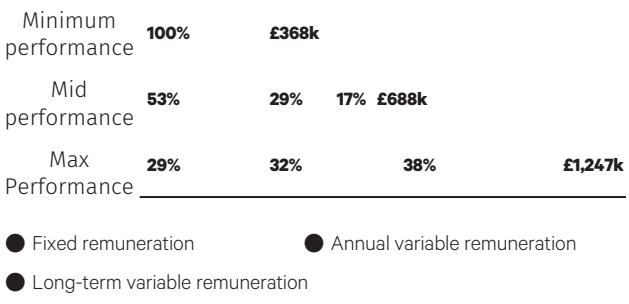
When setting remuneration for Executive Directors the Committee considers relevant information about pay and conditions in the Group. Senior executives and Executive Directors generally receive a higher proportion of their total pay in the form of variable remuneration and share awards. All employees of the Group are entitled to base salary and pension provision including life assurance. In addition, all colleagues are entitled to participate in annual bonus arrangements, the levels of which are based on the seniority and level of responsibility. Long-term incentive share awards are only available to senior executives and Executive Directors, and certain benefits are generally available only to more senior employees at management level and above.

Illustration of applications of remuneration policy

Susan Davy
Chief Executive Officer



Paul Boote
Chief Financial Officer



Minimum Performance	Fixed pay, which constitutes base salary, pension-related benefits and benefits in kind. These values are made up of the salaries for 2023/24 and the benefits values as shown for 2022/23. The pension value is 10% of salary.
Mid Performance	Fixed pay and 50% of the maximum annual bonus and 25% of the maximum long-term incentive award.
Maximum Performance	Fixed pay and 100% vesting of the annual bonus and of long-term incentive awards.

No adjustments have been made for potential payment of dividends. Benefits from all-employee schemes have also been excluded.

As long-term share awards are granted in shares and subject to stretching performance criteria, the value of the award can vary significantly depending on the extent to which targets are achieved and the movement in the share price. For example, if the share price increased by 50% over the relevant vesting and holding period, the maximum values shown in the charts above would increase to £2,282k for the CEO and £1,487k for the CFO. Conversely if the share price was to fall by 50%, the maximum values shown in the charts above would reduce to £1,545k for the CEO and £1,007k for the CFO.

Future policy table – Non-Executive Directors

Purpose and link to strategy	Set at a market level to attract Non-Executive Directors who have appropriate experience and skills to assist in determining the Group's strategy.
Fees	
Operation	Fees are set by the Board with the Non-Executive Chair's fees being set by the Committee. The relevant Directors are not present at the meetings when their fees are being determined. The Non-Executive Chair and Non-Executive Directors normally receive a basic fee and do not participate in any of the Company's incentive arrangements or receive pension-related benefits. Non-Executive Directors may receive an additional fee for any specific Board responsibility such as membership or chairmanship of a Committee or occupying the role of Senior Independent Director. In reviewing the fees, the Board, or Committee as appropriate, consider the level of fees payable to Non-Executive Directors in other companies of similar scale and complexity.
Maximum	Total fees paid to Non-Executive Directors will remain within the limits stated in the Articles of Association.
Benefits	
Operation	Where appropriate limited role-appropriate benefits may be provided. Expenses incurred in the performance of non-executive duties for the Company may be reimbursed or paid for directly by the Company (including any tax due on the expenses). The Chair's benefits include the provision of a driver and vehicle, when appropriate for the efficient carrying out of their duties.
Maximum	None.

Approach to recruitment remuneration

When considering the appointment of Executive Directors, the Committee seeks to balance the need to offer remuneration to attract candidates of sufficient calibre to deliver the Company's strategy whilst remaining mindful of the need to pay no more than is necessary.

The Committee will appoint new Executive Directors with a package that is in line with the remuneration policy that has been agreed by shareholders and is in place at the time.

Other elements of remuneration would be in line with the Company's policy set out in the in the future policy.

The maximum variable pay opportunity on recruitment (excluding 'buyouts') would be 275% of salary, which is in line with the future policy table. The Committee may determine for the first year of appointment that incentives may be subject to different weightings or objectives.

To facilitate recruitment, it may be necessary to recompense a new Executive Director for the expected value of remuneration or contractual arrangements forfeited on joining the Company ('buyout' awards). The Committee may make buyout awards in accordance with LR9.4.2 of the Listing Rules or utilising any other incentive plan operated by the Group from time-to-time. The Committee will ensure that any such award would at a maximum match the value of the awards granted by the previous employer and be made only where a Director is able to demonstrate that a loss has been incurred from leaving his or her previous employment. Any buyout would take into account the terms of the arrangement forfeited, including in particular any performance conditions and the time over which they vest. The award would normally have time horizons which are in line with or greater than the awards forfeited. Where appropriate the exact nature of the buyout may be tailored based on the commercial circumstances at the time, provided that the value of the buyout remains comparable to arrangements forfeited.

For interim positions a cash supplement may be paid rather than salary (for example a Non-Executive Director taking on an executive function on a short-term basis).

Where an employee is promoted to the position of Executive Director (including if an Executive Director is appointed following an acquisition or merger), pre-existing awards and contractual commitments would be honoured in accordance with their established terms.

Non-Executive Directors' fees would be in line with the policy set out in the future policy table on page 152.

Policy on termination of service agreements and payment for loss of office

The Company's policy is that Executive Directors' service agreements normally continue until the Director's agreed retirement date or such other date as the parties agree. Otherwise, they are terminable on one year's notice.

There are no liquidated damages provisions for compensation on termination within Executive Directors' service agreements. Taking into account the circumstances of any termination, the Committee may determine that a payment in lieu of notice should be made. Any such payments would be restricted to salary and benefits. In these circumstances, consideration would be given to phasing of payments and an individual's duty and opportunity to mitigate losses.

The Committee reserves the right to make any other payments in connection with a director's cessation of office or employment where the payments are made in good faith in discharge of an existing legal obligation (or by way of damages for breach of such an obligation) or by way of compromise or settlement of any claim arising in connection with the cessation of a director's office or employment. Any such payments may include but are not limited to paying any fees for outplacement assistance and/or the director's legal and/or professional advice fees in connection with his cessation of office or employment. The Company may meet ancillary costs, such as outplacement consultancy and/or reasonable legal costs.

Burrator Reservoir,
Devon

Any compensation payable will be determined by reference to the terms of the service contract between the Company and the employee, as well as the rules of the various incentive plans as set out in the table below.

Annual bonus	Normally no bonus is payable unless an Executive Director is employed on the date of payment. In certain good leaver circumstances (death, disability, redundancy, retirement and any other circumstance at the Committee's discretion) a bonus may be payable. Any such bonus would be based on performance and pro-rated to reflect the period of service with performance normally assessed at the same time as other employees. The Committee retains discretion to adjust the timing and pro-rating of any award to take account of any prevailing exceptional circumstances which they consider would be fair to the Company and to the employee. Share deferral would not normally apply.
Deferred shares	Unvested awards would normally lapse upon cessation. In certain good leaver circumstances, the participant may retain their awards. The restricted period is not automatically terminated on cessation of employment; rather, the restricted period continues to apply as if the leaver was still in employment. However, awards may be released to participants at an earlier date following cessation of employment at the discretion of the Committee. Good leaver circumstances are death, injury, ill-health, disability, redundancy, retirement (with agreement of the Company), the transfer of the employing company or business or any other circumstance at the Committee's discretion.
Long-term incentive plan	Any unvested awards would normally lapse upon cessation of the individual's employment within the Group. In certain good leaver circumstances, awards vest to the extent determined by the Committee taking into account the extent to which the performance conditions have been satisfied, the period of time elapsed between grant and the cessation of employment and such other factors as the Committee may deem relevant. Awards would normally vest on the original normal vesting date and be released at the end of the two-year holding period (unless the Committee determines awards should be subject to earlier vesting and release dates). If a participant dies, an award will, unless the Committee determines otherwise, vest and be released as soon as possible following the participant's death, taking into account the extent to which the performance conditions have been satisfied and the period of time elapsed since grant. Good leaver circumstances are death, ill health, injury, disability, redundancy, retirement, where the participant's employer is no longer a member of the Group, where the participant is employed in an undertaking which is transferred out of the Group, or for any other reason that the Committee determines. All awards would lapse if a participant was summarily dismissed.
All-employee awards	Leavers will be treated in accordance with the HMRC approved rules.
Other awards	Where a buyout award is made on recruitment, leaver provisions would be determined at the time of award.

Statement of consideration of employment conditions elsewhere in the Company

In setting executive remuneration the Committee takes account of employment market conditions and the pay and benefits differentials across the Group. The Committee considers annual summary reports of employee remuneration and the terms and conditions of employment within each operating company and has regard to these when considering remuneration for the Executive Directors and senior management. As part of this assessment the Committee considers various metrics including data on the ratio between CEO and all-employee pay, gender pay statistics and measures of employee engagement.

The Board engage on remuneration matters with the wider workforce, through many mechanisms including the employee RISE and the Partnership forum, the Big Chat and Open Door communications, on which more can be read on pages 31 to 39.

Statement of consideration of shareholder views

In developing this Remuneration Policy, the Committee took into account general good governance, best practice and evolving shareholder views. We regularly engage with major shareholders to understand their views on executive pay and their feedback informs our decision-making and the approach set out in this Policy.

As detailed on page 152 to the extent that a further review of the Policy is initiated later in the year the Committee would engage with our major stakeholders as appropriate.

Directors' Report

Introduction

The Directors present their Annual Report and Accounts for the year ending 31 March 2023. The Directors' Report comprises this report and the entire Governance section Including the Chair's Governance Statement. It has been prepared in accordance with the provisions of the Companies Act 2006 and regulations made under it. In accordance with the Financial Conduct Authority Listing's Rules, the information to be included in the 2023 Annual Report and Accounts, where applicable (under Listing Rule 9.8.4), is set out in this Directors Report. Other information relevant to this Report, and which is incorporated by reference, can be located as follows:

Information	Page Number
Particulars of important events affecting the Company and/or its subsidiaries which have occurred since the year end	2 and 3
Likely future developments of the Company	4 to 7
Risk management systems	52 to 62
Certain employee and employee engagement matters as well as the disclosures below	31 to 39, 100 to 101
Business relationships/engagement with suppliers, customers and others	8 to 9, 27, 28 to 39
Carbon and greenhouse gas emissions, energy consumption and energy efficiency action	67 to 69
Financial risk management	note 3 of the notes to the financial statements
Financial instruments	44 to 51, and notes 2(n) and 18 of the notes to the financial statements

This Directors' Report (including pages 98 to 101, which form part of this report) fulfils the requirements of the corporate governance statement for the purposes of the FCA's Disclosure Guidance and Transparency Rules.

Cautionary statement: This Annual Report has been prepared for, and only for the members of the Company, as a body, and no other persons. The Company, its directors, employees, agents or advisers do not accept or assume responsibility to any other person to whom this document is shown or into whose hands it may come and any such responsibility or liability is expressly disclaimed. By their nature, the statements concerning the risks and uncertainties facing the Group in this Annual Report involve uncertainty since future events and circumstances can cause results and developments to differ materially from those anticipated. The forward-looking statements reflect knowledge and information available at the date of preparation of this Annual Report and the Company undertakes no obligation to update these forward-looking statements. Nothing in this Annual Report should be construed as a profit forecast.

Corporate

Articles of Association: The Articles of Association may only be amended by special resolution of the shareholders. The current Articles were adopted as the Articles of Association of the Company at the conclusion of the 2022 AGM and are available on our website.

Auditors: The External Auditor for the 2022 financial year was Ernst & Young LLP. The Independent Auditors' Report starting on page 162 sets out the Information contained In the Annual Report which has been audited by the External Auditor. The Audit Committee considered the performance and audit fees of the External Auditors and the level of non-audit work undertaken. It is recommended to the Board that a resolution for the reappointment of Ernst & Your LLP for a further year as the Company's auditor be proposed to shareholders at the AGM on 20 July 2023.

Change of control: No person holds securities In the Company carrying special rights with regard to control of the Company. All of the Company's share schemes contain provisions relating to a change of control. Outstanding awards and options would normally vest and become exercisable on a change of control, subject to the satisfaction of any performance conditions pro-ration for time where appropriate.

There are a number of agreements that take effect, alter or terminate upon a change of control of the Company following a takeover bid, such as bank loan agreements, Eurobond documentation, hybrid capital securities documentation, private placement debt and employees' share plan. This may result in certain funding agreements being altered or repaid early. The impact of employees' share plans is not considered significant.

Other Agreements: There are no agreements between the Company and its Directors or employees providing for compensation for loss of office or employment that occurs because of a takeover bid.

Final dividend: The Board recommends a final dividend of 29.77 pence per ordinary share to be paid on 4 September 2023 to shareholders on the register on 21 July 2023, making a total dividend for the year of 42.73 pence per share. The aggregate cost of the final dividend will be £111.7million, resulting in a transfer from reserves of £111.3 million. The Strategic Report on pages 1 to 97 analyses the Group's financial results in more detail and sets out other financial information.

Political Contributions: The Company has authority, in accordance with Section 366 of the Companies Act 2006, to make political donations to political parties, political organisations and incur political expenditure subject to limits approved by shareholders. No political donations were made or political expenditure incurred and no contributions were made to a non-UK political party (2021/22: nil)

Other Contributions: During the year, the Group provided a total of £25,000 in charitable donations (2021/22: £91,000).

Directors

Appointments: A table showing Directors who served In the year and to the date of this Report can be found on page 99. Biographies for Directors currently In office can be found on pages 102 to 104 and on our website.

The appointment and replacement of Directors is governed by the Articles of Association, the UK Corporate Governance Code, the Companies Act 2006 and related legislation. The Directors may from time to time appoint one or more Directors. Any such Director shall hold office only until the next AGM and shall then be eligible for appointment by the Company's shareholders In accordance with the Corporate Governance Code. Subject to annual shareholder approval, Non-Executive Directors are appointed for an initial three-year period and annually thereafter. Each Director will retire and submit themselves for election at the forthcoming AGM.

Conflicts of Interest: The Board has adopted a Conflicts of Interest Policy. The Board has considered in detail the current external appointments of the Directors that may give rise situational conflicts and, where appropriate, has authorised potential conflicts. Such authorisation can be reviewed at any time but is always subject to annual review.

Purchase of own ordinary shares: Subject to applicable law and the Company's Articles of Association, the Directors may exercise all powers of the Company, including the power to authorise the Issue and/or market purchase of the Company's shares (subject to an appropriate authority being given in general meeting by the shareholders to the Directors). The Articles and a schedule of Matters Reserved for the Board can be found on our website.

At the 2022 AGM, the Directors were given the following authorities:

- To purchase up to a maximum number of 26,484,359 of the Company's ordinary shares at a minimum price of the nominal value of the share and a maximum price of not more than the higher of i) 105% of the average of the middle market quotations for such ordinary shares as derived from the London Stock Exchange Daily Official List for the five business days immediately preceding the day on which that ordinary share Is purchased; and ii) an amount equal to the higher of the price of the last independent trade of an ordinary share and the highest current independent bid for an ordinary share on the trading venue where the purchase is carried out (the Share Buy-Back Authority).

Following the value created from the sale of Viridor in 2020/21 and use of funds to repay debt, make a contribution to our principal pension scheme, invest in South West Water and acquire Bristol Water, the Board decided to return surplus funds totalling £1.9 billion to shareholders. In 2021/22 funds were returned to shareholders via a c.£1.5 billion special dividend and £0.2 billion through a up to £0.4 billion share buy-back programme in order to purchase Ordinary Shares from shareholders (a Share Buy-back). The Board considers the use of a Share Buy-Back as an appropriate means of returning capital to shareholders, whilst providing Pennon with ongoing financial flexibility. During 2022/23 a further £40 million was returned concluding the Share Buy Back programme, with the remaining £160 million being allocated to renewable energy investment opportunities.

The Share Buy-Back Authority was used during the year under review to buy back 3,910,503 shares with a nominal value of 61.05p at an average price of 10.22 pence per share and for total consideration of £40.0 million. This represents approximately 1.50% of the called up share capital of the Company as at 31 March 2023. In the period from 1 April 2023 until 30 May 2023, no further ordinary shares of 61.05pence each In Pennon were repurchased using the Share Buy-Back Authority. All shares purchased under the Share Buy-Back Authority have been cancelled. Information on transactions in own shares is also publicly available via the regulatory information service and on Pennon's website at **www.pennon-group.co.uk/ms-announcements.**

The Share Buy-Back Authority will expire at the 2023 AGM. No shares were made subject to a lien or charge during the year under review and up to the date of approval of this Annual Report and Accounts. As at 1 April 2023, 5,628 shares were held in treasury, representing 0.002% of the issued share capital. No treasury shares were re-issued during the year.

Directors' insurance and indemnities: The Company has maintained Directors' and officers' liability insurance for the benefit of the Company, the Directors and its officers throughout the year. The Company has entered into qualifying third-party indemnity arrangements for the benefit of all its Directors in a form and scope that complies with the requirements of the Companies Act 2006 and which were in force throughout the year and remain in force.

Disclosures

Listing Rule 9.8.4 disclosures: There is no information to be disclosed under Listing Rule (9.8.4R. The Company has no long-term incentive arrangements in place under LR 9.4.2R where the only participant is a director and the arrangement is established specifically to facilitate, in unusual circumstances, the recruitment or retention of the individual.

Financial Risk Management: The Directors have carried out a robust assessment of the principal and emerging risks facing the Group, including In relation to its business model, future performance, solvency and liquidity. Details of our principal risks and association mitigations are set out on pages 52 to 62. Note 3 to the Financial Statements gives details of the Group's financial risk management policies and related exposures. This note is incorporated by reference and deemed to form part of this Report.

Going Concern: The going concern basis has been adopted in preparing these financial statements. At 31 March 2023 the Group has access to undrawn committed funds and cash and cash deposits totalling £420 million, including cash and other short-term deposits of £165 million and £255 million of undrawn facilities. Cash and other short-term deposits include £22 million of restricted funds deposited with lessors which are available for access, subject to being replaced by an equivalent valued security.

In making their assessment, the Directors reviewed the principal risks and considered which risks might threaten the Group's going concern status, to do this the Group's business plan has been stress-tested. Whilst the Group's risk management processes seek to mitigate the impact of principal risks as set out on pages 52 to 62, individual sensitivities against these risks have been identified. These sensitivities, which are ascribed a value with reference to risk weighting, factoring in the likelihood of occurrence and financial impact, were applied to the baseline financial forecast which uses the Group's annual budget for FY 2023/24 and longer-term strategic business plan for the remainder of the going concern period to 30 June 2024. The forecast includes our new syndicated £300 million private placement. During the year we also agreed updated covenant terms on the majority of our facilities and the Directors are confident that the covenant update process for the remaining small number of lenders will be concluded satisfactorily in the very near term. For facilities where changes to covenant terms are not finalised at the date of approval of the financial statements, we have modelled the impact on the Group's solvency, using existing terms, under a stress-tested scenario, and concluded this does not compromise the going concern of the Group over the assessment period. The risks and sensitivities include consideration of; legislative impacts such as change in government policy and non-compliance with laws and regulations, macro-economic impacts such as inflation and interest rate increases, and operational impacts such as ensuring adequate water resources and failure of operational assets. A combined stress testing scenario has been performed to assess the overall impact of these individual scenarios impacting the Group collectively. The combined weighted impact of the risks occurring is c.£120m, this value is considered equivalent to an extreme one-off event that could occur within a year, the probability of such an event happening is deemed unlikely. Through this testing, it has been determined that none of the individual principal risks would in isolation, or in aggregate,

compromise the going concern of the Group over the going concern period, the assessment has been considered by reviewing the impact on the solvency position as well as debt and interest covenants. In the combined scenario to ensure that the Group was able to continue as a going concern, additional mitigations could be deployed to reduce gearing and increase covenant headroom. Examples of mitigations could include; reduction in discretionary operational expenditure, deferral of capital expenditure and / or cancellation of non-essential capital expenditure, reduction in the amount of dividend payable, and raising additional funding.

In addition, we have modelled a reverse engineered scenario that could possibly compromise the Group's solvency over the going concern assessment period. This scenario builds on the factors above and additionally assumes all the Group's principal risks are incurred within the going concern period, with no probability weightings attached. The Board considered the likelihood of this scenario on the Group's solvency over the going concern period, as remote, given this would require all of the principal risks to be incurred at maximum impact within the same time frame, without implementing controllable mitigations, as noted above, or raising additional funding.

Having considered the Group's funding position and financial projections, which take into account a range of possible impacts, as described in this report, the Directors have a reasonable expectation that the Group will meet the requirements of its covenants and has adequate resources to continue in operational existence for the period to at least the end of the going concern assessment period of 30 June 2024, and that there are no material uncertainties to disclose. For this reason, they continue to adopt the going concern basis in preparing the financial statements.

Data: As part of our business activity, the Group processes large amounts of personal data. The Group recognises that to enable this use of personal data it is critical that we continue to build on our approach to applying privacy in a lawful and ethical way. A programme of work to support this has been led by our data governance team. The work includes making improvements to our data governance framework and delivering our data privacy function. We have a number of policies, procedures and tools to support this. Compliance with these policies is mandatory. All colleagues undergo regular training to remind them of their responsibilities under these policies.

Employment policies and employee involvement

Continuous Improvement: The Group has a culture of continuous improvement through investment in people at all levels within the Group. The Group is committed to pursuing equality and diversity in all its employment activities including recruitment, training, career development and promotion and ensuring there is no bias or discrimination in the treatment of people. In particular, applications for employment are welcomed from persons with disabilities, and special arrangements and adjustments as necessary are made to ensure that applicants are treated fairly when attending for interview or for pre-employment aptitude tests. Wherever possible the opportunity is taken to retrain people who become disabled during their employment to maintain their employment within the Group.

Policies: The Group has policies in place covering health and safety, equal opportunities, diversity and inclusion, ethics and employee relations. Further detail of the contents of the diversity and inclusion policy are set out in the report of the Nomination Committee on page 128. Also, information regarding the employee diversity is provided on page 37. The Board's activities in relation to assessing and monitoring culture can be found in the Corporate Governance Statement on page 109. A summary of the Board's Diversity and Inclusion policy can be found in the Corporate Governance Statement on page 129.

Freedom of Association: Pennon respects the right to freedom of association and employees are consulted regularly about changes which may affect them either through their trade union appointed representatives or consultation groups or by means of their elected representatives at the Employee Engagement Forum. These forums, together with regular meetings with particular groups of employees, are used to ensure that employees are kept up to date with the business performance of their employer and the financial and economic factors affecting the performance of the Group. The Group also cascades information to all employees to provide them with important and up-to-date information about key events and to obtain feedback from them on a monthly basis. Further details of employee engagement and employment matters relating to the Group are set out on pages 31 to 39 of the Strategic Report.

Share Ownership: The Group encourages share ownership among its employees by operating an HMRC approved Sharesave Scheme and Share Incentive Plan. Following shareholder approval at the 2014 AGM, this scheme and plan were amended to provide for the increased savings limits approved by the Government. At 31 March 2023, approximately 43% (2022: 54%) of the Group's employees were participating in these plans.

Modern Slavery Act: Our people are fundamental to our business, and we remain committed and passionate about supporting our staff, customers and communities to thrive in creating an environment where everyone can feel safe and supported. We have a clear zero-tolerance approach to modern slavery and are committed to playing our part in helping eradicate it by having systems and processes to monitor, assess and reduce the risk of forced labour and human trafficking.

We remain focused on improving our risk assessment and the widening of our engagement. We have continued to engage and raise awareness, through internal training, and by continuing as a member of Slave Free Alliance. We are part of a utilities sector working group which shares best practice across our industry. We will continue to work hard to tackle this issue collaboratively with our partners, employees, suppliers, and peers, to evolve our approach to ensure it remains effective. Our latest Modern Slavery Statement can be found here: https://www.pennon-group.co.uk/sites/default/files/attachments/pdf/modern-slavery-statement-final-board-approved-2022.pdf

Greenhouse gas emissions: Details of our GHG emissions can be found in the Strategic Report on pages 67 to 69.

Energy usage: Details of our Energy usage can be found in the Strategic Report on page 69.

Research and development: Research and development within the Group involving water and wastewater treatment processes amounted to £0.8 million during the year (2021/22: £0.2 million).

Overseas branches: The Company has no overseas branches.

Shares

Issued Share Capital: Details of the Company's issued share capital, consisting of ordinary shares of nominal value 61.05 pence each are set out in note 33 to the financial statements. All of the Issued shares are fully paid up and quoted on the London Stock Exchange.

Rights: The rights attaching to the Company's ordinary shares are set out in the Articles of Association. There are no securities carrying special rights.

Restrictions: There are no restrictions on the transfer of issued ordinary shares of the Company or on the exercise of voting rights attached to them, except where the Company has exercised its right to suspend their voting rights or to prohibit their transfer following the omission of their holder or any person interested in them to provide the Company with information requested by it in accordance with Part 22 of the Companies Act 2006 or where their holder is precluded from exercising voting rights by the Financial Conduct Authority's Listing Rules or the City Code on Takeovers and Mergers. There are no persons with special rights regarding control of the Company. No shares issued under the employee share schemes have rights with regard to control of the Company that are not exercisable directly by the employee.

Substantial Shareholders: Details of significant direct or indirect holdings of securities of the Company are set out in the shareholder analysis on page 226. The Company is not aware of any agreements between shareholders which may result in restrictions on the transfer of securities or on voting rights.

Authority to Purchase Own Shares: The Directors also intend to renew the power to make purchases of the Company's own shares in issue as set out above up to an aggregate nominal value of:

i. £53,895,670 (such amount to be reduced by any shares allotted or rights granted under (ii) below in excess of £53,895,670); and
ii. £107,791,340 by way of a rights issue (such amount to be reduced by any shares allotted or rights granted from (i) above), similar to that approved by shareholders at the 2021 AGM. In addition, shareholders approved at the 2021 AGM, resolutions giving the Directors a limited authority to allot shares for cash other than pro rata to existing shareholders. These resolutions remain valid until the conclusion of this year's AGM. Similar resolutions will be proposed at the 2022 AGM. The Directors have no present intention to issue ordinary shares other than pursuant to the Company's employee share schemes.
iii. The Directors were also given the authority by shareholders at the 2019 AGM, to allot a single non-cumulative redeemable preference share of one penny nominal value (the WaterShare+ Share), the rights and restrictions in relation to which are set out in Article 5A of the Company's Articles of Association. The share was allotted on 20 October 2020.

Statement of Directors' responsibilities

The Directors are responsible for preparing the annual report and the Group 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 elected to prepare the Group and parent company financial statements in accordance with UK adopted international accounting standards (IFRSs) in conformity with the Companies Act 2006. 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 in accordance with IAS 8 Accounting Policies, Changes in Estimates and Errors and then apply them consistently;
- make judgments and accounting estimates that are reasonable and prudent;
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- provide additional disclosures when compliance with the specific requirements of IFRSs is insufficient to enable users to understand the impact of particular transactions, other events and conditions of the Group's financial position and financial performance;
- in respect of the Group financial statements, state whether UK adopted international accounting standards in conformity with the Companies Act 2006 have been followed, subject to any material departures disclosed and explained in the financial statements;
- in respect of the parent company financial statements, state whether UK adopted international accounting standards in conformity with the Companies Act 2006 have been followed; and
- prepare the financial statements on the going concern basis unless it is appropriate to presume that the Company and/or Group will not continue in business.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's and Group'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 Company and Group financial statements comply with the Companies Act 2006. 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. Under applicable law and regulations, the Directors are also responsible for preparing a Strategic Report, Directors' Report, Directors' Remuneration Report and Corporate Governance Statement that comply with the law and those regulations. The Directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website.

Each of the Directors, whose names and functions are listed on pages 102 to 104, confirms that, to the best of her or his knowledge:

The consolidated financial statements, prepared in accordance with UK adopted international accounting standards in conformity with the Companies Act 2006 give a true and fair view of the assets, liabilities, financial position and profit of the parent company and undertakings included in the consolidation taken as a whole.

The Annual Report, including the Strategic Report (pages 1 to 97), includes a fair review of the development and performance of the business during the year and the position of the Company and undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties they face.

They consider that the Annual Report, taken as a whole, is fair, balanced and understandable, and provides the information necessary for shareholders to assess the Company's position, performance, business model and strategy.

Statement as to disclosure of information to the auditor

i. So far as each of the Directors in office at the date of the signing of the report is aware, there is no relevant audit information of which the Company's auditor is unaware; and
ii. Each of the Directors has taken all the steps each Director ought to have taken individually as a Director in order to make herself or himself aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

The Directors' Report consisting of pages 158 to 161 was approved by the Board on 31 May 2023.

By order of the Board

Andrew Garard
Group General Counsel and Company Secretary

31 May 2023

Independent Auditors' report

Opinion

In our opinion:

- Pennon Group plc's group financial statements and parent company financial statements (the "financial statements") give a true and fair view of the state of the group's and of the parent company's affairs as at 31 March 2023 and of the group's profit for the year then ended;
- the group financial statements have been properly prepared in accordance with UK adopted international accounting standards;
- the parent company financial statements have been properly prepared in accordance with UK adopted international accounting standards as applied in accordance with section 408 of the Companies Act 2006; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006.

We have audited the financial statements of Pennon Group plc (the 'parent company') and its subsidiaries (the 'group') for the year ended 31 March 2023 which comprise:

Group	Parent company
Group balance sheet as at 31 March 2023	Balance sheet as at 31 March 2023
Consolidated income statement for the year then ended	Statement of changes in equity for the year then ended
Consolidated statement of comprehensive income for the year then ended	Cash flow statement for the year then ended
Group statement of changes in equity for the year then ended	Related notes 1 to 44 to the financial statements including a summary of significant accounting policies
Group cash flow statement for the year then ended	
Related notes 1 to 44 to the financial statements, including a summary of significant accounting policies	

The financial reporting framework that has been applied in their preparation is applicable law and UK adopted international accounting standards and as regards the parent company financial statements, as applied in accordance with section 408 of the Companies Act 2006.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the financial statements section of our report. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion

Independence

We are independent of the group and parent in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the FRC's Ethical Standard as applied to listed public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

The non-audit services prohibited by the FRC's Ethical Standard were not provided to the group or the parent company and we remain independent of the group and the parent company in conducting the audit.

Conclusions relating to going concern

In auditing the financial statements, we have concluded that the directors' use of the going concern basis of accounting in the preparation of the financial statements is appropriate. Our evaluation of the directors' assessment of the group and parent company's ability to continue to adopt the going concern basis of accounting included the following procedures:

- We obtained an understanding of the process undertaken by management to perform the going concern assessment.
- We have obtained management's going concern assessment, including the cash flow forecast, liquidity requirements and forecast covenant calculations for the going concern period which covers the period from approval of the 2023 financial statements through to 30 June 2024, and have tested this for arithmetical accuracy. Management has modelled a downside scenario in their cash flow forecast and covenant calculations in order to incorporate unexpected changes to the forecasted liquidity of the group.
- We have reviewed the forecasts used for the going concern assessment period for reasonableness, agreed the data to the Board approved plan and, where applicable, corroborated the data with audit information from other areas, including capital commitments. We have evaluated the appropriateness of the key assumptions in management's forecasts including revenue growth, by comparing these to year-to-date performance and through consideration of historical forecasting accuracy and the impact of regulatory price increases.
- The largest component of the group's operations relates to the regulated water business, undertaken by South West Water Limited, which has an agreed business plan with Ofwat for the five-year price period to 31 March 2025, setting out the basis of allowed tariff changes. We have compared the key assumptions in the group's regulated water business forecasts to the business plans and pricing determinations agreed with Ofwat, for consistency.
- We have evaluated management's stress test modelling including management's downside scenario and specific risk register probability-weighted scenarios, to understand the impact on the group's liquidity and covenant ratios. Management has also modelled a reverse engineered scenario (reverse stress test) assuming all the principal risks materialise within the going concern period with no probability weightings attached. We assessed the reasonableness of management's stress test scenarios by performing our own sensitivity analysis for severe but plausible scenarios.
- We have compared the risks identified and modelled in the cash flow forecasts of management's downside scenario to the group risk register and evaluated the quantification by management. We have considered whether there are other alternative risks that should be taken into consideration based on our knowledge of the business. Our procedures included evaluating management's assessment of the impact of climate change within the going concern period, including the principal risk of availability of sufficient water resources to meet current and future demand.
- We have compared facilities assumed in the forecasts to supporting loan documentation and to covenant terms. For facilities, where changes to terms are not finalised at the date of approval of the financial statements, we have evaluated the impact on covenants and liquidity headroom based on existing terms.
- We performed testing to consider the likelihood of a scenario causing a liquidity issue or breach of covenants, including the impact of controllable mitigating actions, where relevant.
- We have reviewed the group's going concern disclosures included in the annual report in order to assess whether the disclosures were appropriate and in conformity with the reporting standards.

We observed at 31 March 2023, the group had access to undrawn committed facilities of £254.8 million and cash and short-term and other deposits totalling £165.4 million (£143.3 million excluding restricted funds). The group generated positive net cash flows from operating activities of £152.6 million. Subsequent to the year end date, the group

has secured a £300m private placement and agreed amended covenant terms on the majority of its facilities. Management's forecasts indicate there is headroom in the base case and in the downside scenario after controllable mitigations. Management consider the reverse engineered scenario, that all the group's principal risks are incurred within the going concern period with no probability weightings attached, to be remote.

Based on the work we have performed, we have not identified any material uncertainties relating to events or conditions that, individually or collectively, may cast significant doubt on the group and parent company's ability to continue as a going concern for a period up to 30 June 2024.

In relation to the group and parent company's reporting on how they have applied the UK Corporate Governance Code, we have nothing material to add or draw attention to in relation to the directors' statement in the financial statements about whether the directors considered it appropriate to adopt the going concern basis of accounting.

Our responsibilities and the responsibilities of the directors with respect to going concern are described in the relevant sections of this report. However, because not all future events or conditions can be predicted, this statement is not a guarantee as to the group's ability to continue as a going concern.

Overview of our audit approach

Audit scope	We performed an audit of the complete financial information of four components. The components where we performed full audit procedures accounted for 100% of Earnings before interest, taxes and non-underlying items, 100% of Revenue and 94% of Total assets.
Key audit matters	• Revenue recognition across the group's operations in relation to accrued income relating to measured supplies • Valuation of the expected credit loss provision for customer balances across the group • Capitalisation of costs relating to the capital programme
Materiality	Overall group materiality of £7.2m which represents 5% of earnings before interest, taxes and non-underlying items.

An overview of the scope of the parent company and group audits

Tailoring the scope

Our assessment of audit risk, our evaluation of materiality and our allocation of performance materiality determine our audit scope for each company within the group. Taken together, this enables us to form an opinion on the consolidated financial statements. We take into account size, risk profile, the organisation of the group and effectiveness of group-wide controls, changes in the business environment, the potential impact of climate change and other factors such as recent internal audit results when assessing the level of work to be performed at each company.

In assessing the risk of material misstatement to the group financial statements, and to ensure we had adequate quantitative coverage of significant accounts in the financial statements, of the five reporting components of the Group, we selected four components covering entities Pennon Group plc, South West Water Limited, Pennon Water Services Limited and Bristol Water Holdings UK Limited, which represent the principal business units within the Group.

We performed an audit of the complete financial information of all four components ("full scope components") which were selected based on their size or risk characteristics.

The reporting full scope components where we performed audit procedures accounted for 100% of the group's earnings before interest, taxes and non-underlying items (2022: 100% of the group's profit before tax and non-underlying items), 100% (2022: 100%) of the group's Revenue and 94% (2022: 95%) of the group's Total assets.

The remaining component accounts for not more than 1% of the group's earnings before interest, taxes and non-underlying items. For this component, we performed other procedures, including analytical review procedures, testing of consolidation journals and intercompany eliminations to respond to any potential risks of material misstatement to the group financial statements.

Changes from the prior year

In the prior year, following the acquisition of Bristol Water Holdings UK Limited in June 2021, a non-EY firm audited this full scope component, operating under the instruction of the primary audit engagement team. In the current year, the Bristol Water audit team is led by the Senior Statutory Auditor.

Involvement with component teams

In establishing our overall approach to the Group audit, we determined the type of work that needed to be undertaken at each of the components by us, as the primary audit engagement team, or by component auditors. The audit teams for all full scope components are led by the Senior Statutory Auditor.

The primary team interacted regularly with the component teams where appropriate during various stages of the audit, reviewed key working papers and were responsible for the scope and direction of the audit process. We maintained continuous and open dialogue with all component audit teams in addition to holding formal meetings to ensure that we were fully aware of their progress and results of their procedures. The Senior Statutory Auditor discussed the planned audit approach with the component teams and any issues arising from their work, attended meetings with management and reviewed key audit working papers on risk areas. This, together with the additional procedures performed at group level, gave us appropriate evidence for our opinion on the group financial statements.

Climate change

Stakeholders are increasingly interested in how climate change will impact Pennon Group plc. The group has determined that the most significant future impacts from climate change on their operations will be from physical and transitional climate-related risks. These are explained on pages 74 to 95 in the required Task Force on Climate related Financial Disclosures and on pages 52 to 62 in the principal risks and uncertainties. They have also explained their climate commitments on pages 42 to 43. All of these disclosures form part of the "Other information," rather than the audited financial statements. Our procedures on these unaudited disclosures therefore consisted solely of considering whether they are materially inconsistent with the financial statements or our knowledge obtained in the course of the audit or otherwise appear to be materially misstated, in line with our responsibilities on "Other information".

In planning and performing our audit we assessed the potential impacts of climate change on the group's business and any consequential material impact on its financial statements.

The group has explained in their basis of preparation note to the financial statements how they have reflected the impact of climate change in their financial statements and how this aligns with their commitment to the aspirations of the Paris Agreement to achieve net zero emissions by 2050 which form part of their disclosures within the Task Force on Climate related Financial Disclosures which form part of the "Other information". Significant judgements and estimates relating to climate change are included in Note 2(a) Basis of preparation and Note 4 Critical accounting judgements and estimates. The disclosures within "Other information" also explain where governmental and societal responses to climate change risks are still developing, and where the degree of certainty of these changes means that they cannot be taken into account when determining asset and liability valuations under the requirements of UK adopted international accounting standards. In Note 4 to the financial statements supplementary narrative explanation of the impact of climate change on long life assets and the sensitivity of depreciation charge to amendments in the useful economic lives of these assets has been provided, concluding there is no specific impact on useful economic lives of long life assets as at 31 March 2023.

Our audit effort in considering the impact of climate change on the financial statements was focused on evaluating management's assessment, which was prepared with support from external consultants. We evaluated management's assessment of the impact of climate risk, physical and transition, their climate commitments, the effects of material climate risks disclosed on pages 74 to 95 and the significant judgements and estimates disclosed in Note 4, including whether these have been appropriately reflected in asset values where these are determined through modelling future cash flows and associated disclosures (see Notes 2(a) Basis of preparation), following the requirements of UK adopted international accounting standards. As part of this evaluation, we performed our own risk assessment, supported by our climate change internal specialists, to determine the risks of material misstatement in the financial statements from climate change which needed to be considered in our audit.

We also challenged the Directors' considerations of climate change risks in their assessment of going concern and viability and associated disclosures. We have described our considerations of climate change, relevant to our assessment of going concern in the 'Conclusions relating to going concern' section of our report.

Based on our work we have not identified the impact of climate change on the financial statements to be a key audit matter or to impact a key audit matter.

Key audit matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) that we identified. These matters included those which had the greatest effect on: the overall audit strategy, the allocation of resources in the audit; and directing the efforts of the engagement team. These matters were addressed in the context of our audit of the financial statements as a whole, and in our opinion thereon, and we do not provide a separate opinion on these matters.

Risk	Our response to the risk	Key observations communicated to the Audit Committee
Revenue recognition across the group's operations in relation to accrued income relating to measured supplies (2023: £132.8 million, 2022: £120.8 million) Refer to the Audit Committee Report (page 123); Accounting policies (page 177); and Note 5 of the Consolidated Financial Statements (page 185) The group's revenue streams relate to the provision of water and sewerage services by South West Water, Pennon Water Services and Bristol Water. ISAs (UK & Ireland) presume there is a risk of fraud relating to revenue recognition. For the group, given the targets associated with financial performance and potential pressures to meet market expectations, there is an incentive to overstate revenue. This risk over revenue recognition specifically arises in the following areas of estimation, where there is an opportunity to overstate revenue: Income from measured water services requires an estimation of the amount of unbilled charges at the period end. This is calculated using a combination of system generated information, based on previous customer volume usage, together with management adjustments for a number of different factors not included in the system-generated accrual, such as seasonality and operational data trends. The risk remained consistent in the current year.	Procedures to respond to this risk were performed by the component teams. We obtained an understanding of the process, by performing walkthroughs of the supply of measured services, meter reading and related billing in order to assess the completeness of adjustments to reflect the accrual or deferral of revenue at the year-end; We tested key controls linked to system generated information and around the estimation process for measured revenue; We obtained internal and external data on factors that influence demand from customers, weather patterns and leaks in infrastructure networks and formed an expectation of the impact of these matters on revenue to compare to assumptions used in management's estimate; We obtained a system report of invoices raised post year end based on actual meter readings taken since the year end. We selected a sample of items from the report to compare to supporting evidence. We compared this report to the year end assumptions used to accrue income for these customer accounts, to assess the reliability of the assumptions used to determine accrued income; We performed analytical procedures by comparing revenue balances for the year against expectations and obtained support for significant variances; We used data analytics to understand the journal entries posted as part of the revenue, trade receivables and accrued income to cash collection process to identify transactions that were outside of our expectation and agreed these to underlying supporting documentation and business rationale; In performing our journal testing, we paid increased attention to entries impacting revenue, focusing on non-system postings and those raised in the last two weeks of the year.	We concluded that the estimation process undertaken by management to calculate the measured income accrual reflected latest operational factors in the key assumptions and that the income accrual was appropriately determined.

Risk	Our response to the risk	Key observations communicated to the Audit Committee
Valuation of the expected credit loss provision for customer balances across the group (2023: £106.5 million, 2022: £100.4 million) Refer to the Audit Committee Report (page 123); Accounting policies (page 179); and Note 22 of the Consolidated Financial Statements (page 198) The expected credit loss provision is calculated using a combination of system generated information on historic debt recovery rates and management's judgement of the future likely recovery rates. There is a risk that the assumptions, used by management in calculating the expected credit loss provision, may not be appropriate and the valuation of the provision against customer balances may be misstated. Management's key assumptions include: • that the historic level of collections is indicative of the ability to collect at the same levels in the future; and • that the risk of non-recovery from customers varies, depending on factors such as whether the household customer no longer occupies a property in the area, has previously paid/not paid, is/is not on a payment plan etc., and for non-household customers depends on the general economic performance of the business sector they operate within. The risk has remained consistent in the current year.	Procedures to respond to this risk were performed by the component teams. We performed a walkthrough of the process for calculating the expected credit loss provision and assessed the design effectiveness of the key controls; For debt relating to household customers, we tested operating effectiveness of key controls over billing systems and integrity of data and the reports utilised to generate the ageing and categorisation of debt within the component's billing systems. For debt relating to non-household customers, we tested the accuracy of data and reports by obtaining underlying evidence to support the parameters relied upon by management in calculating the expected credit loss provision; We tested latest information on collection rates and evaluated how this data was used in the preparation of the expected credit loss provision; For the South West Water operations, we utilised collection trends to determine our own range of the likely ultimate collection of debts existing at the balance sheet date, including performing several scenario analyses and compared these to the provision recorded by management, including assessing assumptions for evidence of management bias; We assessed the assumptions used by management in determining amounts provided against different categories and age of debt, by comparing these assumptions to historic collection rates and by considering the impact of changes in the methods adopted operationally by management to collect debt, and in the external environment; We considered whether historic collection performance evidenced behaviour patterns assumed by management depending on categorisation of household and business sector for non-household customers; For debt relating to household customers, we utilised collection information over previous periods, with sensitivities to consider the impact of a deterioration which might arise from a downturn in the economy, to determine an acceptable range of the likely ultimate collection of debts existing at the balance sheet date and compared this to the provision recorded by management; For debt relating to non-household customers, we tested management's segmentation by business sector and risk factors considered for each sector, regarding non-recovery of debt. We compared this analysis with information on actual collections, by sector, in the current year and since the balance sheet date; and We tested the appropriateness of journal entries and adjustments impacting the expected credit loss provision, particularly those raised close to the balance sheet date.	We concluded that the expected credit loss provision of £106.5 million is within an acceptable range and reflects the recent history of collection of outstanding debts and considerations of the impact on future collections from the current macro-economic environment.

Risk	Our response to the risk	Key observations communicated to the Audit Committee
Capitalisation of costs relating to the capital programme (2023: £353.7 million, 2022: £273.3 million) Accounting policies (page 178); and Note 17 of the Consolidated Financial Statements (page 194) The group has a substantial capital programme which has been agreed with the Water Services Regulation Authority (Ofwat) and therefore incurs significant annual expenditure in relation to the development and maintenance of both infrastructure and non-infrastructure assets. There is judgement involved in allocating costs between operating and capital expenditure given the nature of certain projects which include both repairs and maintenance as well as asset enhancement. Therefore, there is a potential for misstatement between the income statement and the statement of financial position. In addition, internal expenditure including staff costs to support capital projects is capitalised only if it can be demonstrated that it is directly attributable to the asset, provides probable economic benefit to the company and can be measured reliably. There is a risk that costs capitalised do not meet these criteria. Due to the level of judgement involved, we have determined that there is a potential for fraud through possible manipulation of this balance. The risk is new in the current year due to the increased level of capital spend in the year.	Procedures to respond to this risk were performed by the component teams. We evaluated capital and operating or finance costs, and assessed whether these are appropriately classified and recalculated the amounts included as capital additions to ensure they agree with the underlying supporting documentation; For a sample of capitalised additions, we evaluated the appropriateness of the classification as capital by considering the nature of the expenditure with reference to invoice, certificate or timesheets relating to a specific project or asset. We also considered the judgements management applied in capitalising certain staff costs and overheads; We tested a sample of items allocated to expenditure in the income statement and verified whether they are correctly classified by considering the nature of projects i.e., repairs and maintenance or asset enhancement, to which the expenditure relates; We analysed assets commissioned during the year, on a sample basis, and obtained confirmation from project managers of their use in the business; We made inquiries of project managers to gain an understanding of the on-going capital projects of the Group and how costs are reviewed and determined as capital expenditures that meet the Group's capitalisation policy; We selected a sample of manual journal entries to record additions within fixed assets, which resulted from a credit posting to an operating expenditure account and checked whether the capitalisation of such expense was appropriately authorised and in accordance with the capitalisation policy.	We concluded that management has applied the capitalisation policy appropriately in determining the expenditure to be capitalised.

In the prior year, our auditor's report included a key audit matter in relation to the accounting for the acquisition of Bristol Water. The fair value exercise was completed in 2022 and there were no other acquisitions in the current year, therefore the accounting for the acquisition of Bristol Water is no longer considered a key audit matter.

In the current year, considering the increased level of capital spend and the judgements involved in allocating costs between capital and operating expenditure, we have determined that the capitalisation of costs relating to the capital programme is a key audit matter.

Our application of materiality

We apply the concept of materiality in planning and performing the audit, in evaluating the effect of identified misstatements on the audit and in forming our audit opinion.

Materiality

The magnitude of an omission or misstatement that, individually or in the aggregate, could reasonably be expected to influence the economic decisions of the users of the financial statements. Materiality provides a basis for determining the nature and extent of our audit procedures.

We determined materiality for the group to be £7.2 million (2022: £7.2 million), which is 5% of earnings before interest, taxes and non-underlying items. In the prior year, we used 5% of profit before taxation and non-underlying items as our materiality basis. In the current year, we have changed the basis to earnings before interest, taxes and non-underlying items which provides us with an appropriate measure of the underlying performance of the group, as this excludes the impact of higher interest costs on the group's index-linked debt, driven by the significantly higher levels of inflation and is a measure of focus for users of the financial statements.

We determined materiality for the Parent Company to be £11.0 million (2022: £12.4 million), which is 1% (2022: 1%) of equity.

- **Reported earnings before interest and taxes £109.4 million**
  (2022: reported profit before taxation £127.7 million)

- **Non-underlying items (refer to Note 6) increase basis by £43.7 million**
  (2022: £15.8 million increase)

- **Totals £153.1 million earnings before interest, taxes and non-underlying items**
  (2022: £143.5 million profit before taxation and non-underlying items)
- **Materiality of £7.2 million** (2022: £7.2 million)
  (5% of earnings before interest, taxes and non-underlying items (2022: 5% of profit before taxation and non-underlying items)**)**

We are also required to consider if changing the basis of materiality results in a substantially different materiality level to that used in prior period and if it is appropriate to do so. Given there have been no significant changes in the underlying performance and operations of the business, compared to the prior year, we have determined our planning materiality as no higher than the final materiality for the prior year, namely £7.2m.

Performance materiality

The application of materiality at the individual account or balance level. It is set at an amount to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements exceeds materiality.

On the basis of our risk assessments, together with our assessment of the group's overall control environment, our judgement was that performance materiality was 75% (2022: 75%) of our planning materiality, namely £5.4 million (2022: £5.4 million). We have set performance materiality at this percentage based on our assessment of the group's internal control environment and the extent and nature of audit findings identified in the prior period. This basis is consistent with the prior year.

Audit work at component locations for the purpose of obtaining audit coverage over significant financial statement accounts is undertaken based on a percentage of total performance materiality. The performance materiality set for each component is based on the relative scale and risk of the component to the group as a whole and our assessment of the risk of misstatement at that component. In the current year, the range of performance materiality allocated to components was £1.6 million to £4.8 million (2022: £1.1 million to £5.1 million).

Reporting threshold

An amount below which identified misstatements are considered as being clearly trivial.

We agreed with the Audit Committee that we would report to them all uncorrected audit differences in excess of £0.4 million (2022: £0.4 million), which is set at 5% of planning materiality, as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds.

We evaluate any uncorrected misstatements against both the quantitative measures of materiality discussed above and in light of other relevant qualitative considerations in forming our opinion.

Other information

The other information comprises the information included in the annual report set out on pages 1 to 161 and 220 to 228 other than the financial statements and our auditor's report thereon. The directors are responsible for the other information contained within the annual report.

Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in this report, we do not express any form of assurance conclusion thereon.

Our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the course of the audit, or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether this gives rise to a material misstatement in the financial statements themselves. If, based on the work we have performed, we conclude that there is a material misstatement of the other information, we are required to report that fact.

We have nothing to report in this regard.

Opinions on other matters prescribed by the Companies Act 2006

In our opinion, the part of the directors' remuneration report to be audited has been properly prepared in accordance with the Companies Act 2006.

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the strategic report and the directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the strategic report and the directors' report have been prepared in accordance with applicable legal requirements.

Matters on which we are required to report by exception

In the light of the knowledge and understanding of the group and the parent company and its environment obtained in the course of the audit, we have not identified material misstatements in the strategic report or the directors' report.

We have nothing to report in respect of the following matters in relation to which the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent company financial statements and the part of the Directors' Remuneration Report to be audited are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit

Corporate Governance Statement

We have reviewed the directors' statement in relation to going concern, longer-term viability and that part of the Corporate Governance Statement relating to the group and company's compliance with the provisions of the UK Corporate Governance Code specified for our review by the Listing Rules.

Based on the work undertaken as part of our audit, we have concluded that each of the following elements of the Corporate Governance Statement is materially consistent with the financial statements or our knowledge obtained during the audit:

- Directors' statement with regards to the appropriateness of adopting the going concern basis of accounting and any material uncertainties identified set out on page 159;
- Directors' explanation as to its assessment of the company's prospects, the period this assessment covers and why the period is appropriate set out on page 63;
- Director's statement on whether it has a reasonable expectation that the group will be able to continue in operation and meets its liabilities set out on page 159;
- Directors' statement on fair, balanced and understandable set out on page 161;
- Board's confirmation that it has carried out a robust assessment of the emerging and principal risks set out on page 52;
- The section of the annual report that describes the review of effectiveness of risk management and internal control systems set out on page 53; and;
- The section describing the work of the audit committee set out on page 120.

Responsibilities of directors

As explained more fully in the directors' responsibilities statement set out on page 161, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the group and parent company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the group or the parent company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

Explanation as to what extent the audit was considered capable of detecting irregularities, including fraud

Irregularities, including fraud, are instances of non-compliance with laws and regulations. We design procedures in line with our responsibilities, outlined above, to detect irregularities, including fraud. The risk of not detecting a material misstatement due to fraud is higher than the risk of not detecting one resulting from error, as fraud may involve deliberate concealment by, for example, forgery or intentional misrepresentations, or through collusion. The extent to which our procedures are capable of detecting irregularities, including fraud is detailed below.

However, the primary responsibility for the prevention and detection of fraud rests with both those charged with governance of the company and management.

We obtained an understanding of the legal and regulatory frameworks that are applicable to the group and determined that the most significant are:

- Companies Act 2006
- Financial Reporting Council (FRC) and the UK Corporate Governance Code
- Tax legislation (governed by HM Revenue & Customs)
- Health and Safety legislation
- Environment Agency environmental permits
- Ofwat regulations
- UK listing rules

- We understood how Pennon Group plc is complying with those frameworks by reading internal policies and codes of conduct and assessing the entity level control environment, including the level of oversight of those charged with governance. We made enquiries of the group's legal counsel, regulatory team and internal audit of known instances of non-compliance or suspected non-compliance with laws and regulations. We corroborated our enquiries through review of correspondence with regulatory bodies. We designed our audit procedures to identify non-compliance with such laws and regulations identified in the paragraph above. As well as enquiry and attendance at meetings, our procedures involved a review of the reporting to the above committees and a review of board meetings and other committee minutes to identify any non-compliance with laws and regulations. Our procedures also involved journal entry testing, with a focus on journals meeting our defined risk criteria based on our understanding of the business.
- We assessed the susceptibility of the group's financial statements to material misstatement, including how fraud might occur by making enquiries of senior management, including the Chief Executive Officer, Chief Financial Officer, Head of Internal Audit and Audit Committee Chair. We planned our audit to identify risks of management override, tested higher risk journal entries and performed audit procedures to address the potential for management bias, particularly over areas involving significant estimation and judgement. Further discussion of our approach to address the identified risks of management override are set out in the key audit matters section of our report.
- Based on this understanding we designed our audit procedures to identify non-compliance with such laws and regulations. Our procedures involved making enquiries of key management, those charged with governance and legal counsel, reviewing key policies, inspecting legal registers and correspondence with regulators and reading key management meeting minutes. We involved our internal specialists where appropriate. We also completed procedures to conclude on the compliance of significant disclosures in the Annual Report and Accounts with the requirements of the relevant accounting standards, UK legislation and the UK Corporate Governance Code.
- We communicated regularly with the component teams and attended key meetings with the component teams, management and legal counsel in order to identify and communicate any instances of non-compliance with laws and regulations.
- The group operates in the water sector which is highly regulated. As such the Senior Statutory Auditor reviewed the experience and expertise of the engagement team to ensure that the team had the appropriate competence and capabilities, which included the use of specialists where appropriate.

A further description of our responsibilities for the audit of the financial statements is located on the Financial Reporting Council's website at https://www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditor's report.

Other matters we are required to address

- Following the recommendation from the audit committee, we were appointed by the company on 31 March 2014 to audit the financial statements for the year ending 31 March 2015 and subsequent financial periods.
- The period of total uninterrupted engagement including previous renewals and reappointments is 9 years, covering the years ending 31 March 2015 to 31 March 2023.
- The audit opinion is consistent with the additional report to the audit committee.

Use of our report

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Christabel Cowling (Senior statutory auditor)
for and on behalf of Ernst & Young LLP, Statutory Auditor
London

31 May 2023

Consolidated income statement

For the year ended 31 March 2023

	Notes	Before non-underlying items 2023 £m	Non-underlying items (note 6) 2023 £m	Total 2023 £m	Before non-underlying items 2022 £m	Non-underlying items (note 6) 2022 £m	Total 2022 £m
Revenue	5	**825.0**	**(27.8)**	**797.2**	792.3	–	792.3
Operating costs	7						
Employment costs		**(102.2)**	**–**	**(102.2)**	(90.4)	(1.7)	(92.1)
Raw materials and consumables used		**(33.6)**	**–**	**(33.6)**	(22.9)	–	(22.9)
Other operating expenses		**(373.6)**	**(15.9)**	**(389.5)**	(289.5)	(14.1)	(303.6)
Trade receivables impairment		**(7.8)**	**–**	**(7.8)**	(5.6)	–	(5.6)
Earnings before interest, tax, depreciation and amortisation	5	**307.8**	**(43.7)**	**264.1**	383.9	(15.8)	368.1
Depreciation and amortisation	7	**(154.7)**	**–**	**(154.7)**	(146.7)	–	(146.7)
Operating profit/(loss)	5	**153.1**	**(43.7)**	**109.4**	237.2	(15.8)	221.4
Finance income	8	**9.2**	**18.4**	**27.6**	2.6	–	2.6
Finance costs	8	**(145.8)**	**–**	**(145.8)**	(96.3)	–	(96.3)
Net finance costs	8	**(136.6)**	**18.4**	**(118.2)**	(93.7)	–	(93.7)
Share of post-tax profit from associated companies	20	**0.3**	**–**	**0.3**	–	–	–
Profit/(loss) before tax	5	**16.8**	**(25.3)**	**(8.5)**	143.5	(15.8)	127.7
Taxation credit/(charge)	9	**3.6**	**5.3**	**8.9**	(13.9)	(98.2)	(112.1)
Profit/(loss) for the year		**20.4**	**(20.0)**	**0.4**	129.6	(114.0)	15.6
Attributable to:							
Ordinary shareholders of the parent				**0.1**			15.4
Non-controlling interests				**0.3**			0.2
Earnings per ordinary share (pence per share)	11						
Basic				**–**			4.9
Diluted				**–**			4.9

The above results were derived from continuing operations.

The notes on pages 176 to 219 form part of these financial statements.

Consolidated statement of comprehensive income

For the year ended 31 March 2023

	Notes	**Before non-underlying items 2023 £m**	**Non-underlying items (note 6) 2023 £m**	**Total 2023 £m**	Before non-underlying items 2022 £m	Non-underlying items (note 6) 2022 £m	Total 2022 £m
Profit/(loss) for the year		**20.4**	**(20.0)**	**0.4**	129.6	(114.0)	15.6
Other comprehensive income/(loss)							
Items that will not be reclassified to profit or loss							
Remeasurement of defined benefit obligations	30	**(39.0)**	**–**	**(39.0)**	24.9	–	24.9
Income tax on items that will not be reclassified	9	**9.8**	**–**	**9.8**	2.4	–	2.4
Total items that will not be reclassified to profit or loss		**(29.2)**	**–**	**(29.2)**	27.3	–	27.3
Items that may be reclassified subsequently to profit or loss							
Cash flow hedges		**29.1**	**–**	**29.1**	40.6	–	40.6
Income tax on items that may be reclassified	9	**(7.3)**	**–**	**(7.3)**	(6.5)	–	(6.5)
Total items that may be reclassified subsequently to profit or loss		**21.8**	**–**	**21.8**	34.1	–	34.1
Other comprehensive (loss)/income for the year net of tax	36	**(7.4)**	**–**	**(7.4)**	61.4	–	61.4
Total comprehensive income/(loss) for the year		**13.0**	**(20.0)**	**(7.0)**	191.0	(114.0)	77.0
Total comprehensive income/(loss) attributable to:							
Ordinary shareholders of the parent				**(7.3)**			76.8
Non-controlling interests				**0.3**			0.2

The notes on pages 176 to 219 form part of these financial statements.

Balance sheets

At 31 March 2023

	Notes	Group 2023 £m	Group 2022* £m	Company 2023 £m	Company 2022 £m
Assets					
Non-current assets					
Goodwill	15	**163.9**	163.9	**–**	–
Other intangible assets	16	**14.9**	13.9	**–**	–
Property, plant and equipment	17	**4,476.9**	4,264.0	**0.1**	0.1
Other non-current assets	19	**23.2**	9.6	**26.1**	31.5
Financial assets at fair value through profit	24	**1.3**	–	**1.3**	–
Deferred tax assets	31	**–**	–	**18.6**	13.1
Derivative financial instruments	23	**33.2**	14.8	**0.5**	1.0
Investments in subsidiary undertakings	20	**–**	–	**1,316.6**	1,310.8
Investments in associated companies	20	**0.3**	–	**–**	–
Retirement benefit obligations	30	**29.3**	66.3	**4.7**	12.4
		4,743.0	4,532.5	**1,367.9**	1,368.9
Current assets					
Inventories	21	**10.0**	7.7	**–**	–
Trade and other receivables	22	**238.0**	270.9	**80.4**	49.8
Current tax receivable	27	**8.4**	1.5	**–**	–
Derivative financial instruments	23	**20.7**	5.6	**0.6**	0.6
Cash and cash deposits	25	**165.4**	519.0	**104.1**	306.7
		442.5	804.7	**185.1**	357.1
Liabilities					
Current liabilities					
Borrowings	28	**(124.7)**	(240.2)	**(279.1)**	(312.8)
Financial liabilities at fair value through profit	24	**(2.6)**	(2.5)	**(0.1)**	(0.1)
Derivative financial instruments	23	**(2.4)**	–	**–**	–
Trade and other payables	26	**(225.4)**	(171.5)	**(6.3)**	(5.6)
Current tax liabilities	27	**–**	–	**(3.4)**	(3.4)
Provisions	32	**(0.4)**	(1.0)	**–**	–
		(355.5)	(415.2)	**(288.9)**	(321.9)
Net current assets/(liabilities)		**87.0**	389.5	**(103.8)**	35.2
Non-current liabilities					
Borrowings	28	**(3,006.1)**	(2,961.7)	**(155.7)**	(154.5)
Other non-current liabilities	29	**(155.3)**	(137.2)	**(8.5)**	(8.6)
Financial liabilities at fair value through profit	24	**(34.0)**	(36.1)	**–**	–
Derivative financial instruments	23	**(2.4)**	–	**–**	–
Deferred tax liabilities	31	**(507.0)**	(512.4)	**–**	–
		(3,704.8)	(3,647.4)	**(164.2)**	(163.1)
Net assets		**1,125.2**	1,274.6	**1,099.9**	1,241.0
Shareholders' equity					
Share capital	33	**159.5**	161.7	**159.5**	161.7
Share premium account	34	**237.6**	235.5	**237.6**	235.5
Capital redemption reserve	35	**157.1**	154.7	**157.1**	154.7
Retained earnings and other reserves	36	**570.6**	722.6	**545.7**	689.1
Total shareholders' equity		**1,124.8**	1,274.5	**1,099.9**	1,241.0
Non-controlling interests		**0.4**	0.1	**–**	–
Total equity		**1,125.2**	1,274.6	**1,099.9**	1,241.0

* An adjustment to the preliminary accounting for the Bristol Water acquisition has been made within the measurement period ending 2 June 2022. This adjustment is presented retrospectively and the 31 March 2022 balance sheet figures have been adjusted accordingly (see note 4).

The profit for the year attributable to ordinary shareholders' equity dealt with in the accounts of the Parent Company is £8.4 million (2022 £74.5 million). The notes on pages 176 to 219 form part of these financial statements.

The financial statements on pages 170 to 219 were approved by the Board of Directors and authorised for issue on 31 May 2023 and were signed on its behalf by:

Susan Davy
Chief Executive Officer
Pennon Group plc
Registered Office: Peninsula House, Rydon Lane, Exeter, Devon, England EX2 7HR. Registered in England Number 2366640.

Statements of changes in equity

At 31 March 2023

	Share capital (note 33) £m	Share premium account (note 34) £m	Capital redemption reserve (note 35) £m	Retained earnings and other reserves (note 36) £m	Non-controlling interests £m	Total equity £m
Group						
At 31 March 2021	171.8	232.1	144.2	2,436.8	(0.1)	2,984.8
Profit for the year	–	–	–	15.4	0.2	15.6
Other comprehensive profit for the year	–	–	–	61.4	–	61.4
Total comprehensive income for the year	–	–	–	76.8	0.2	77.0
Transactions with equity shareholders:						
Dividends paid	–	–	–	(1,590.3)	–	(1,590.3)
Shares purchased for cancellation (including related expenses)	–	–	–	(201.7)	–	(201.7)
Shares cancelled (note 33)	(10.5)	–	10.5	–	–	–
Adjustment in respect of share-based payments (net of tax)	–	–	–	2.2	–	2.2
Own shares acquired by the Pennon Employee Share Trust in respect of share options granted	–	–	–	(1.2)	–	(1.2)
Proceeds from shares issued under the Sharesave Scheme	0.4	3.4	–	–	–	3.8
Total transactions with equity shareholders	(10.1)	3.4	10.5	(1,791.0)	–	(1,787.2)
At 31 March 2022	161.7	235.5	154.7	722.6	0.1	1,274.6
Profit for the year	–	–	–	0.1	0.3	0.4
Other comprehensive loss for the year	–	–	–	(7.4)	–	(7.4)
Total comprehensive (loss)/income for the year	–	–	–	(7.3)	0.3	(7.0)
Transactions with equity shareholders:						
Dividends paid	–	–	–	(101.6)	–	(101.6)
Shares purchased for cancellation (including related expenses)	–	–	–	(40.0)		(40.0)
Shares cancelled (note 33)	(2.4)	–	2.4	–	–	–
Adjustment in respect of share-based payments (net of tax)	–	–	–	1.9	–	1.9
Own shares acquired by the Pennon Employee Share Trust in respect of share options granted	–	–	–	(5.0)	–	(5.0)
Proceeds from shares issued under the Sharesave Scheme	0.2	2.1	–	–	–	2.3
Total transactions with equity shareholders	(2.2)	2.1	2.4	(144.7)	–	(142.4)
At 31 March 2023	**159.5**	**237.6**	**157.1**	**570.6**	**0.4**	**1,125.2**

The notes on pages 176 to 219 form part of these financial statements.

Statements of changes in equity (continued)

For the year ended 31 March 2023

	Share capital (note 33) £m	Share premium account (note 34) £m	Capital redemption reserve (note 35) £m	Retained earnings and other reserves (note 36) £m	Total equity £m
Company					
At 31 March 2021	171.8	232.1	144.2	2,410.8	2,958.9
Profit for the year (note 10)	–	–	–	74.5	74.5
Other comprehensive loss for the year	–	–	–	(2.5)	(2.5)
Total comprehensive income for the year	–	–	–	72.0	72.0
Transactions with equity shareholders:					
Dividends paid	–	–	–	(1,590.3)	(1,590.3)
Shares purchased for cancellation (including related expenses)	–	–	–	(201.7)	(201.7)
Shares cancelled (note 33)	(10.5)	–	10.5	–	–
Adjustment in respect of share-based payments (net of tax)	–	–	–	0.9	0.9
Charge in respect of share options vesting	–	–	–	(2.6)	(2.6)
Proceeds from shares issued under the Sharesave Scheme	0.4	3.4	–	–	3.8
Total transactions with equity shareholders	(10.1)	3.4	10.5	(1,793.7)	(1,789.9)
At 31 March 2022	161.7	235.5	154.7	689.1	1,241.0
Profit for the year (note 10)	–	–	–	8.4	8.4
Other comprehensive loss for the year	–	–	–	(6.1)	(6.1)
Total comprehensive income for the year	–	–	–	2.3	2.3
Transactions with equity shareholders:					
Dividends paid	–	–	–	(101.6)	(101.6)
Shares purchased for cancellation (including related expenses)	–	–	–	(40.0)	(40.0)
Shares cancelled (note 33)	(2.4)	–	2.4	–	–
Adjustment in respect of share-based payments (net of tax)	–	–	–	1.3	1.3
Charge in respect of share options vesting	–	–	–	(5.4)	(5.4)
Proceeds from shares issued under the Sharesave Scheme	0.2	2.1	–	–	2.3
Total transactions with equity shareholders	(2.2)	2.1	2.4	(145.7)	(143.4)
At 31 March 2023	**159.5**	**237.6**	**157.1**	**545.7**	**1,099.9**

The notes on pages 176 to 219 form part of these financial statements.

Cash flow statements

For the year ended 31 March 2023

	Notes	Group 2023 £m	Group 2022 £m	Company 2023 £m	Company 2022 £m
Cash flows from operating activities					
Cash generated/(outflow) from operations	37	**313.7**	334.2	**(38.9)**	(29.9)
Interest paid	37	**(159.7)**	(74.6)	**(7.7)**	(6.0)
Tax (paid)/received		**(1.4)**	(7.3)	**0.6**	(6.2)
Net cash generated/(outflow) from operating activities		**152.6**	252.3	**(46.0)**	(42.1)
Cash flows from investing activities					
Interest received		**4.9**	2.6	**6.1**	2.2
Dividends received		**–**	–	**15.7**	109.6
Movement of restricted deposits		**146.1**	89.1	**–**	–
Purchase of property, plant and equipment		**(326.6)**	(225.6)	**–**	–
Acquisition of subsidiaries including acquisition costs, net of cash acquired	20, 43	**–**	(421.2)	**–**	(434.0)
Proceeds on disposal of subsidiaries, net of cash disposed at Group level and transaction costs		**–**	9.2	**–**	9.2
Purchase of intangible assets		**(4.6)**	(3.4)	**–**	–
Proceeds from sale of property, plant and equipment		**0.7**	1.4	**–**	–
Investment in subsidiary undertakings	20	**–**	–	**–**	(45.0)
Net cash (used in)/received from investing activities		**(179.5)**	(547.9)	**21.8**	(358.0)
Cash flows from financing activities					
Proceeds from issuance of ordinary shares		**2.3**	3.8	**2.3**	3.7
Purchase of ordinary shares by the Pennon Employee Share Trust		**(5.0)**	(1.2)	**(5.4)**	–
Proceeds from new borrowing		**233.0**	61.0	**–**	–
Repayment of borrowings		**(210.3)**	(49.4)	**(33.7)**	(0.5)
Cash inflows from lease financing arrangements		**40.2**	15.0	**–**	–
Lease principal repayments (including net recoverable VAT paid / recovered)		**(99.2)**	(258.9)	**–**	–
Dividends paid		**(101.6)**	(1,590.3)	**(101.6)**	(1,590.3)
Repurchase of own shares and associated fees		**(40.0)**	(201.7)	**(40.0)**	(201.7)
Net cash used in financing activities		**(180.6)**	(2,021.7)	**(178.4)**	(1,788.8)
Net (decrease)/ increase in cash and cash equivalents		**(207.5)**	(2,317.3)	**(202.6)**	(2,188.9)
Cash and cash equivalents at beginning of the year	25	**351.2**	2,668.5	**306.7**	2,495.6
Cash and cash equivalents at end of the year	25	**143.7**	351.2	**104.1**	306.7

The notes on pages 176 to 219 form part of these financial statements.

Notes to the Financial Statements

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 227. Pennon Group's business is operated through two principal subsidiaries. South West Water Limited, providing water and wastewater services in Devon, Cornwall and parts of Dorset and Somerset and water only services in parts of Dorset, Hampshire, Wiltshire and Bristol. Following the statutory licence transfer from Bristol Water plc to South West Water Limited on 1 February 2023 the regulated water business of Bristol Water plc transferred to South West Water Limited. Pennon Group is the majority shareholder of Pennon Water Services Limited, a company providing water and wastewater retail services to non-household customer accounts across Great Britain. Bristol Water Holdings UK Limited owns a 30% share in Water 2 Business Limited, a joint venture with Wessex Water, operating in the same sector as Pennon Water Services Limited.

2. Principal accounting policies

The principal accounting policies adopted in the preparation of these financial statements are set out below. These policies have been consistently applied to the years presented.

(a) Basis of preparation

These financial statements have been prepared on the historical cost accounting basis (except for fair value items, principally acquisitions, transfers of assets from customers and certain financial instruments as described in accounting policy notes (b), (u) and (n) respectively) and in accordance with UK-adopted international accounting standards and, as regards the parent company financial statements, as applied in accordance with the provisions of the Companies Act 2006. The Company has taken advantage of section 408 of the Companies Act 2006 not to present the parent company profit and loss account. These financial statements are presented in pounds sterling and all values rounded to the nearest one-hundred thousand pounds, except when otherwise indicated.

A summary of the principal accounting policies is set out below, together with an explanation where changes have been made to previous policies on the adoption of new accounting standards and interpretations in the year.

The going concern basis has been adopted in preparing these financial statements. At 31 March 2023 the Group has access to undrawn committed funds and cash and cash deposits totalling £420 million, including cash and other short-term deposits of £165 million and £255 million of undrawn facilities. Cash and other short-term deposits include £22 million of restricted funds deposited with lessors which are available for access, subject to being replaced by an equivalent valued security.

In making their assessment, the Directors reviewed the principal risks and considered which risks might threaten the Group's going concern status, to do this the Group's business plan has been stress-tested. Whilst the Group's risk management processes seek to mitigate the impact of principal risks as set out on pages 52 to 62, individual sensitivities against these risks have been identified. These sensitivities, which are ascribed a value with reference to risk weighting, factoring in the likelihood of occurrence and financial impact, were applied to the baseline financial forecast which uses the Group's annual budget for FY 2023/24 and longer-term strategic business plan for the remainder of the going concern period to 30 June 2024. The forecast includes our new syndicated £300 million private placement. During the year we also agreed updated covenant terms on the majority of our facilities and the Directors are confident that the covenant update process for the remaining small number of lenders will be concluded satisfactorily in the very near term. For facilities where changes to covenant terms are not finalised at the date of approval of the financial statements, we have modelled the impact on the Group's solvency, using existing terms, under a stress-tested scenario, and concluded this does not compromise the going concern of the Group over the assessment period. The risks and sensitivities include consideration of; legislative impacts such as change in government policy and non-compliance with laws and regulations, macro-economic impacts such as inflation and interest rate increases, and operational impacts such as ensuring adequate water resources and failure of operational assets. A combined stress testing scenario has been performed to assess the overall impact of these individual scenarios impacting the Group collectively. The combined weighted impact of the risks occurring is c.£120m, this value is considered equivalent to an extreme one-off event that could occur within a year, the probability of such an event happening is deemed unlikely. Through this testing, it has been determined that none of the individual principal risks would in isolation, or in aggregate, compromise the going concern of the Group over the going concern period, the assessment has been considered by reviewing the impact on the solvency position as well as debt and interest covenants. In the combined scenario to ensure that the Group was able to continue as a going concern, additional mitigations could be deployed to reduce gearing and increase covenant headroom. Examples of mitigations could include; reduction in discretionary operational expenditure, deferral of capital expenditure and / or cancellation of non-essential capital expenditure, reduction in the amount of dividend payable, and raising additional funding.

In addition, we have modelled a reverse engineered scenario that could possibly compromise the Group's solvency over the going concern assessment period. This scenario builds on the factors above and additionally assumes all the Group's principal risks are incurred within the going concern period, with no probability weightings attached. The Board considered the likelihood of this scenario on the Group's solvency over the going concern period, as remote, given this would require all of the principal risks to be incurred at maximum impact within the same time frame, without implementing controllable mitigations, as noted above, or raising additional funding.

Having considered the Group's funding position and financial projections, which take into account a range of possible impacts, as described in this report, the Directors have a reasonable expectation that that the Group will meet the requirements of its covenants and has adequate resources to continue in operational existence for the period to at least the end of the going concern assessment period of 30 June 2024, and that there are no material uncertainties to disclose. For this reason, they continue to adopt the going concern basis in preparing the financial statements.

In preparing the financial statements management has considered the impact of climate change, taking into account the relevant disclosures in the Strategic Report, including those made in accordance with the recommendations of the Taskforce on Climate-related Financial Disclosure. The expected environmental impact of climate change on the water business has been modelled noting that the physical risks are increasing. It is likely that the Group will need to invest to protect certain assets such as sewage works and pumping stations against sea level inundation and these considerations form part of the planning process for new capital expenditure. Longer term investment, outlined in the strategic plans, will be needed to manage future risks. To achieve this, combined regulatory and government support within their policy frameworks will be essential. Whilst it is estimated additional spend will be required to manage future risks, the current available information and assessment did not identify any risks that would require the useful economic lives of assets to be reduced in the year or identify the need for impairment that would impact the carrying values of such assets or have any other impact on the financial statements. The impact assessments will be continuously updated to reflect the latest available information on the impact of climate change.

New standards or interpretations which were mandatory for the first time in the year beginning 1 April 2022 did not have a material impact on the net assets or results of the Group and the parent company.

New standards or interpretations due to be adopted from 1 April 2023 are not expected to have a material impact on the Group's and the parent company's net assets or results. Existing borrowing covenants are not impacted by changes in accounting standards.

2. Principal accounting policies *continued*

(b) Basis of consolidation

The Group financial statements include the results of Pennon Group plc and its subsidiaries and joint ventures.

The results of subsidiaries and joint ventures are included from the date of acquisition or incorporation and excluded from the date of disposal. The results of subsidiaries are consolidated where the Group is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. The results of joint ventures are accounted for on an equity basis.

Intra-group trading, loan balances and transactions are eliminated on consolidation.

The acquisition method of accounting is used to account for the purchase of subsidiaries. The excess of the value transferred to the seller in return for control of the acquired business, together with the fair value of any previously held equity interest in that business over the Group's share of the fair value of the identifiable net assets, is recorded as goodwill.

(c) Revenue recognition

Group revenue is recognised following delivery of performance obligations and an assessment of when control over the product or service is transferred to the customer. Revenue is only recognised when collection of consideration is highly probable.

Revenue is recognised either when the performance obligation in the contract has been performed (point in time recognition) or 'over time' as the performance obligations to the customer are satisfied. For each obligation satisfied over time, the Group applies a revenue recognition method that accurately reflects performance in transferring control of the services to the customer.

Where a contract with a customer includes more than one performance obligation, revenue is allocated to each obligation in proportion to a fair value assessment of the total contract sales value split across the services provided.

At the inception of a contract the total transaction price is estimated, being the fair value to which the Group expects to be entitled under the contract, including any variable consideration. Variable consideration is based on the most likely outcome of the performance obligations. Revenue excludes value added tax, trade discounts and revenue arising from transactions between Group companies.

Water (domestic and non-household retail)

For most of the services provided to domestic customers, contract terms are implied through statute and regulation in the absence of formal, written contracts. South West Water and Bristol Water have a duty under legislation to provide domestic customers with services regardless of payment and is not permitted to disconnect domestic customers for non-payment of bills. Charges are set via the periodic review price-setting process, regulated by Ofwat.

In respect of ongoing, continuous services to customers, such as the provision of drinking water and wastewater services, revenue is recognised over time.

Customers with an unmeasured supply are billed at the start of the year for the full amount of the annual charge but typically take advantage of a choice of payment arrangements to pay by regular instalments. The performance obligation has been assessed as standing ready to provide water and sewerage services when required by our customers, and accordingly revenue is recognised under IFRS 15 as the stand-ready obligation is fulfilled over time.

Customers with a metered supply are sent up to four bills per year, based either on actual meter readings or estimated usage. For these customers, revenue includes an estimation of the amount of unbilled usage at the period end. Payment options for domestic customers include an annual meter payment plan where customers agree to pay a fixed amount per month which is adjusted to reflect actual consumption at the end of the year. Revenue is recognised as water is supplied, based on estimate usage for unbilled elements.

A range of regulated services is offered to property developers and owners who require connection to the water and sewerage networks or need the networks to be extended or altered. Typically, these customers pay an estimate of the charges in advance as a deposit, which is treated as a contract liability and are billed or refunded the difference between the estimate and actual costs on completion of the work.

The principle components of these contributions are as follows:

i) Where the performance obligation relates solely to a connection to the network, revenue is recognised at the point of connection when the customer is deemed to obtain control.

ii) Where assets are constructed or provided by the Group or assets transferred to the Group, it is considered that there is an explicit or implied performance obligation to provide an ongoing water and/or wastewater service, with the result that revenue is recognised over a time no longer than the economic life of assets provided by or transferred to the Group.

Pennon Water Services provides specialist retail water and wastewater services to business customers. It raises bills and recognises revenue in accordance with its contracts with customers and in line with the limits established for the non-household periodic price-setting process where applicable.

Contract assets and liabilities

A trade receivable is recognised when the Group has an unconditional right to receive consideration in exchange for performance obligations already fulfilled. A contract asset is recognised when the Group has fulfilled some of its performance obligations but has not yet obtained an unconditional right to receive consideration. The amounts for contract assets, when applicable, are disclosed within note 19 (Other non-current assets) and note 22 (Trade and other receivables) as appropriate. A contract liability is recognised when consideration is received in advance of the Group performing its performance obligations to customers, including, when appropriate, transfers of assets from customers (per paragraph (u) below). The value of contract liabilities is disclosed within note 26 (Trade and other payables) and note 29 (Other non-current liabilities) as appropriate.

(d) Segmental reporting

Each of the Group's business segments provides services which are subject to risks and returns which are different from those of the other business segments. The Group's internal organisation and management structure and its system of internal financial reporting are based primarily on business segments.

The Group is organised into two operating segments. The water segment comprises the regulated water and wastewater services undertaken by South West Water. The non-household retail business reflects the services provided by Pennon Water Services. Other segments, including Pennon Group plc, are not reportable segments as they are not reported to Chief Decision makers. Segmental revenue and results include transactions between businesses. Inter-segmental transactions are eliminated on consolidation.

(e) Goodwill

Goodwill arising on consolidation from the acquisition of subsidiary undertakings represents the excess of the purchase consideration over the fair value of net assets acquired, less any subsequent impairment charges.

Goodwill is recognised as an asset and reviewed for impairment at least annually. Any impairment is recognised immediately in the income statement and is not subsequently reversed. For the purpose of impairment testing, goodwill acquired in a business combination is allocated to each of the cash generating units (CGUs) or group of CGUs, that is expected to benefit from the synergies of the combination. Each unit or group of units to which goodwill is allocated represents the lowest level within the entity at which the goodwill is monitored for internal reporting purposes. Goodwill is allocated and monitored at the reportable operating segment level. Further details are contained in accounting policy (i).

When a subsidiary undertaking is sold, the profit or loss on disposal is determined after including the attributable amount of goodwill.

2. Principal accounting policies *continued*

(f) Other intangible assets

Other intangible assets include assets acquired in business combination and are capitalised at fair value at the date of acquisition. Following initial recognition, finite life intangible assets are amortised on a straight-line basis over their estimated useful lives, with the expense charged to the income statement through operating costs.

(g) Property, plant and equipment

i) Infrastructure assets (being water mains and sewers, impounding and pumped raw water storage reservoirs, dams, pipelines and sea outfalls)

Infrastructure assets were included at fair value on transition to IFRS, and subsequent additions are recorded at cost less accumulated depreciation and impairment charges. Expenditure to increase capacity or enhance infrastructure assets is capitalised where it can be reliably measured, and it is probable that incremental future economic benefits will flow to the Group. The cost of day to day servicing of infrastructure components is recognised in the income statement as it arises.

Infrastructure assets are depreciated evenly over their useful economic lives, and are principally:

Dams and impounding reservoirs	100 to 200 years
Water mains	60 to 180 years
Sewers	75 to 150 years

Assets in the course of construction are not depreciated until commissioned.

ii) Other assets (being property, overground plant and equipment)

Other assets are included at cost less accumulated depreciation.

Freehold land is not depreciated. Other assets are depreciated evenly to their residual value over their estimated economic lives, and are principally:

Land and buildings – freehold buildings	10 to 80 years
Land and buildings – leasehold buildings	Over the estimated economic lives or the lease period, whichever is the shorter
Operational properties	15 to 100 years
Fixed plant	10 to 30 years
Vehicles, mobile plant and computers	4 to 20 years

Assets in the course of construction are not depreciated until commissioned.

The cost of assets includes directly attributable labour and overhead costs which are incremental to the Group. Borrowing costs directly attributable to the construction of a qualifying asset (an asset necessarily taking a substantial period of time to be prepared for its intended use) are capitalised as part of the asset. Assets transferred from customers are recognised at fair value as set out in accounting policy (u).

The assets' residual values and useful lives are reviewed annually.

Gains and losses on disposal are determined by comparing sale proceeds with carrying amounts. These are included in the income statement.

(h) Leased assets

All are accounted for by recognising a right-of-use asset and a lease liability except for:

- Low value assets; and
- Leases with a duration of 12 months or less.

Contracts are initially measured at the present value of contractual payments due to the lessor over the lease term, with the discount rate determined by reference to the rate inherent in the lease unless this is not readily determinable, in which case the Group's incremental borrowing rate on commencement of the lease is used. After initial measurement, lease payments are allocated between the liability and finance cost. The finance cost is charged to profit and loss over the lease period to produce a constant periodic rate of interest on the remaining balance of the liability for each period. The interest element of cash payments in respect of these leases is included within interest payments in determining net cash generated from operating activities. The capital element of the cash payment is included within cash flows from financing activities. Right-of-use assets are amortised on a straight-line basis over the remaining term of the lease or the remaining economic life of the asset if shorter. When the Group revisits its estimate of lease term (because, for example, it reassesses an extension option), it adjusts the carrying amount of the lease liability to reflect the payments to make over the revised term, which is discounted at the same discount rate that applied on lease commencement. In these circumstances an equivalent adjustment is made to the carrying value of the right-of-use asset, with the revised carrying amount being amortised over the remaining (revised) lease term.

Assets are included as property, plant and equipment as right-of-use assets at the present value of the minimum lease payments and are depreciated over their estimated economic lives or the finance lease period, whichever is the shorter. The corresponding liability is recorded as borrowings. The interest element of the rental costs is charged against profits using the actuarial method over the period of the lease.

The Group regularly uses sale and leaseback transactions to finance its capital programme. A sale and leaseback transaction is where the Group sells an asset and immediately reacquires the use of the asset by entering into a lease with the buyer. Each transaction is assessed as to whether it meets the criteria within IFRS 15 'Revenue from contracts with customers' for a sale to have occurred. If the sale criteria are met a lease liability is recognised, the associated property, plant and equipment asset is derecognised, and a right-of-use asset is recognised at the proportion of the carrying value relating to the right retained. Any gain or loss arising relates to the rights transferred to the buyer. If the criteria for a sale under IFRS 15 have not been met the asset is not derecognised and no sale is recorded.

(i) Impairment of non-financial assets

Assets with an indefinite useful life are not subject to amortisation and are tested annually for impairment, or whenever events or changes in circumstance indicate that the carrying amount may not be recoverable.

Assets subject to amortisation or depreciation are tested for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

An impairment loss is recognised for the amount by which an asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value, less costs to sell, and value-in-use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (CGUs). Value-in-use represents the present value of projected future cash flows expected to be derived from a CGU, discounted using a pre-tax discount rate which reflects an assessment of the market cost of capital of the CGU. Impairments are charged to the income statement in the year in which they arise.

Non-financial assets other than goodwill that have been impaired are reviewed for possible reversal of the impairment at each reporting date.

Where a previously impaired asset or CGU's recoverable amount is in excess of its carrying amount, previous impairments are reversed to the carrying value that would have expected to be recognised had the original impairment not occurred.

2. Principal accounting policies *continued*

(j) Parent company: Investment in subsidiary undertakings

Investments in subsidiary undertakings are initially recorded at cost, being the fair value of the consideration paid. Subsequently investments are reviewed for impairment on an individual basis annually or if events or changes in circumstances indicate that the carrying value may not be fully recoverable.

(k) Investment in associated companies

Associated companies are entities over which the Group exercises joint control. Investments in associated companies are accounted for using the equity method of accounting. Any excess of the cost of acquisition over the Group's share of the fair values of the identifiable net assets of the associated company at the date of acquisition is recognised as goodwill and is included in the carrying value of the investment in the associated company.

The carrying value of the Group's investment is adjusted for the Group's share of post-acquisition profits or losses recognised in the income statement and statement of comprehensive income. Losses of an associated company in excess of the Group's interest are not recognised unless the Group has a legal or constructive obligation to fund those losses.

(l) Inventories

Inventories are stated at the lower of cost and net realisable value. The cost of finished goods and work in progress includes raw materials and the cost of bringing stocks to their present location and condition. It excludes borrowing costs. Net realisable value is the estimated selling price less cost to sell. The costs of items of inventory are determined using weighted average costs.

(m) Cash and cash deposits

Cash and cash deposits comprise cash in hand and short-term deposits held at banks. Bank overdrafts are offset against cash balances where there is a legally enforceable right to offset and there is an intention to settle the balances on a net basis. Otherwise, overdrafts are included within current borrowings.

(n) Financial instruments

Financial instruments are recognised and measured in accordance with IFRS 9. The Group classifies its financial instruments in the following categories:

i) Debt instruments at amortised cost

All loans and borrowings are initially recognised at fair value, net of transaction costs incurred. Following initial recognition, interest-bearing loans and borrowings are subsequently stated at amortised cost using the effective interest method. Gains and losses are recognised in the income statement when instruments are derecognised or impaired. Premia, discounts and other costs and fees are recognised in the income statement through amortisation.

Borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date.

ii) Trade receivables

Trade receivables do not carry any interest receivable and are recognised initially at fair value and subsequently at amortised cost using the effective interest method, less provision for expected credit losses (ECLs). In accordance with IFRS 9, each Group entity performs an impairment analysis at each reporting date to measure the ECLs. Each entity does not track changes in credit risk but instead recognises a loss allowance based on lifetime ECLs at each reporting date. Each subsidiary has established a provision matrix that is based on its historical credit loss experience, adjusted for forward-looking factors specific to the receivables and the economic environment.

iii) Trade payables

Trade payables are not interest-bearing and are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method.

iv) Derivative financial instruments and hedging activities

The Group uses derivative financial instruments, principally interest rate swaps, cross-currency interest rate swaps and inflation swaps to hedge risks associated with interest rate and exchange rate fluctuations. Derivative instruments are initially recognised at fair value on the date the derivative contract is entered into and subsequently remeasured at fair value for the reported balance sheet.

The Group designates certain hedging derivatives as either:

- A hedge of a highly probable forecast transaction or change in the cash flows of a recognised asset or liability (a cash flow hedge); or
- A hedge of the exposure to change in the fair value of a recognised asset or liability (a fair value hedge).

The gain or loss on remeasurement is recognised in the income statement except for cash flow hedges which meet the conditions for hedge accounting, when the portion of the gain or loss on the hedging instrument which is determined to be an effective hedge is recognised directly in equity, and the ineffective portion in the income statement. The gains or losses deferred in equity in this way are subsequently recognised in the income statement in the same period in which the hedged underlying transaction or firm commitment is recognised in the income statement.

In order to qualify for hedge accounting, the Group is required to document in advance the relationship between the item being hedged and the hedging instrument. The Group is also required to document and demonstrate an assessment of the relationship between the hedged item and the hedging instrument which shows that the hedge will be highly effective on an ongoing basis. This effectiveness testing is reperformed at the end of each reporting period to ensure that the hedge remains highly effective.

The full fair value of a hedging derivative is apportioned on a straight-line basis between non-current and current assets and liabilities based on the remaining maturity of the hedging derivative.

Derivative financial instruments deemed held for trading, which are not subject to hedge accounting, are classified as a current asset or liability with any change in fair value recognised immediately in the income statement.

The Group uses cross-currency swaps for some of its foreign currency denominated private placement borrowings. The swaps either have the effect of (i) converting variable rate foreign currency borrowings into fixed rate sterling borrowings, (ii) converting fixed rate foreign currency borrowings into fixed rate sterling borrowings, or (iii) converting fixed rate foreign currency borrowings into floating rate sterling borrowings.

v) Financial instruments at fair value through profit

Financial instruments at fair value through profit reflect the fair value movement of the hedged risk on a hedged item through a fair value hedging relationship. The fair values of these financial instruments are initially recognised on the date the hedging relationship is entered into and thereafter remeasured at each subsequent balance sheet date. The gain or loss on remeasurement for the period is recognised in the income statement.

vi) Receivables due from subsidiary undertakings

Amounts owed by subsidiaries are classified and recorded at amortised cost and reduced by allowances for ECLs. Estimated future credit losses are first recorded on initial recognition of a receivable and are based on estimated probability of default. Individual balances are written off when management deems them not to be collectible.

2. Principal accounting policies *continued*

(o) Taxation including deferred tax

The tax charge for the year comprises current and deferred tax. Tax is recognised in the income statement, except to the extent that it relates to items recognised in the statement of comprehensive income or directly in equity. In this case the tax is also recognised in the statement of comprehensive income or directly in equity as appropriate.

Current tax is calculated on the basis of tax laws enacted or substantively enacted at the balance sheet date. Management periodically evaluates tax items subject to interpretation and establishes provisions on individual tax items, where in the judgement of management, the position is uncertain. The Group includes a number of companies, including the parent company, which are part of a tax group for certain aspects of the tax legislation. One of these aspects relates to group relief whereby current tax liabilities can be offset by current tax losses arising in other companies within the same tax group. Payments for group relief are included within the current tax disclosures.

Deferred tax is provided in full on temporary differences between the carrying amount of assets and liabilities in the financial statements and the tax base, except where they arise from initial recognition of an asset or liability in a transaction, other than a business combination, that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred tax assets are recognised only to the extent that it is probable that future taxable profits will be available against which the assets can be realised. Deferred tax is determined using the tax rates enacted or substantively enacted at the balance sheet date, and expected to apply when the deferred tax liability is settled or the deferred tax asset is realised.

(p) Provisions

Provisions are made where there is a present legal or constructive obligation as a result of a past event and it is probable that there will be an outflow of economic benefits to settle this obligation and a reliable estimate of this amount can be made. Where the effect of the time value of money is material the current amount of a provision is the present value of the expenditures expected to be required to settle obligations. The unwinding of the discount to present value is included as notional interest within finance costs.

(q) Share capital and treasury shares

Ordinary shares are classified as equity.

Where the Company purchases the Company's equity share capital (treasury shares) the consideration paid, including any directly attributable costs, is deducted from equity until the shares are cancelled or reissued. Where such shares are subsequently reissued, any consideration received, net of any directly attributable transaction costs, is included in equity.

The Group balance sheet includes the shares held by the Pennon Group plc Employee Benefit Trust, relating to employee share-based payments, which have not vested at the balance sheet date. These are shown as a deduction from shareholders' equity until such time as they vest.

Share buy-back scheme and tender offer

Shares purchased for cancellation are deducted from retained earnings at the total consideration paid or payable, including any related expenses. Where the Group has an irrevocable commitment to purchase shares for cancellation at the balance sheet date, a liability is recognised in other creditors based on the share price at the balance sheet date and retained earnings reduced by the amount of the liability.

Shares purchased and held by the Group (treasury shares) are deducted from the treasury reserve at the total consideration paid or payable. On cancellation of treasury shares, the cost is transferred from the treasury reserve to retained earnings.

When treasury shares are issued at below cost, an amount representing the difference between the cost of those shares and issue proceeds is transferred to retained earnings. No gain or loss is recognised in the consolidated income statement on the purchase, sale, issue or cancellation of the Group's own equity instruments.

(r) Dividend distributions

Dividend distributions are recognised as a liability in the financial statements in the period in which the dividends are approved by the Company's shareholders. Interim dividends are recognised when paid, final dividends when approved by shareholders at the Annual General Meeting.

(s) Employee benefits

i) Retirement benefit obligations

The Group operates defined benefit and defined contribution pension schemes.

Defined benefit pension schemes

The liability recognised in the balance sheet in respect of defined benefit pension plans is the present value of the defined benefit obligation at the end of the year less the fair value of plan assets. If the value of a plan's assets exceeds the present value of its obligations, the resulting surplus is only recognised if the Group has an unconditional right to that surplus.

The defined benefit obligation is calculated by independent actuaries who advise on the selection of Directors' best estimates of assumptions, using the projected unit credit method. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows using interest rates of high-quality corporate bonds, and that have terms to maturity approximating to the terms of the related pension obligation. The increase in liabilities of the Group's defined benefit pension schemes, expected to arise from employee service in the year, is charged against operating profit.

Changes in benefits granted by the employer are recognised immediately as a past service cost in the income statement.

Actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions are charged or credited to equity in the statement of comprehensive income in the period in which they arise.

Defined contribution scheme

Costs of the defined contribution pension scheme are charged to the income statement in the year in which they arise. The Group has no further payment obligations once the contributions have been paid.

ii) Share-based payment

The Group operates a number of equity-settled, share-based payment plans for employees. The fair value of the employee services required in exchange for the grant is recognised as an expense over the vesting period of the grant.

Fair values are calculated using an appropriate pricing model. Non-market-based vesting conditions are adjusted for assumptions as to the number of shares which are expected to vest.

(t) Fair values

The fair value of interest rate, inflation and cross currency swaps is based on the market price to transfer the asset or liability at the balance sheet date in an ordinary transaction between market participants. The fair values of short-term deposits, loans and overdrafts with a maturity of less than one year are assumed to approximate to their book values. In the case of non-current bank loans and other loans, the fair value of financial liabilities for disclosure purposes is estimated by discounting the future contractual cash flows at the current market interest rate available to the Group for similar financial instruments.

2. Principal accounting policies *continued*

(u) Transfers of assets from customers

Where an item of property, plant and equipment that must be used to connect customers to the network is received from a customer, or where cash is received from a customer for the acquisition or construction of such an item, that asset is recorded and measured on initial recognition at its fair value. The credit created by the recognition of the asset is recognised as a contract liability on the balance sheet. The contract liability reduces, and revenue is recognised in the income statement, as performance obligations are satisfied. The period over which the credit is recognised depends upon the nature of the service provided, as determined by the agreement with the customer. Where the service provided is solely a connection to the network, the credit is recognised at the point of connection. If the agreement does not specify a period, revenue is recognised over a period no longer than the economic life of the transferred asset used to provide the ongoing service.

The fair value of assets on transfer from customers is determined using a cost valuation approach allowing for depreciation.

(v) Foreign exchange

Transactions denominated in foreign currencies are translated at the exchange rate at the date of the transaction. Monetary assets and liabilities denominated in a foreign currency are translated at the closing balance sheet rate. The resulting gain or loss is recognised in the income statement.

(w) Non-underlying items

Non-underlying items are those that in the Directors' view should be separately disclosed by virtue of their size, nature or incidence to enable a full understanding of the Group's financial performance.

(x) Grants and contributions

Grants and contributions receivable in respect of property, plant and equipment which provide the customer with ongoing access to the water and sewerage networks, are treated as contract liabilities and released to revenue over the economic life of those elements of property, plant and equipment. Grants and contributions receivable in respect of expenses charged against profits in the year have been included in the income statement.

Government grants are recognised where there is reasonable certainty that the grant will be received and all attached conditions will be complied with. When the grant relates to an expense item, it is recognised on a systematic basis over the periods that the related costs, for which it is intended to compensate, are expensed. The income from such grants is presented in the financial statements as a deduction from the expense to which it relates.

3. Financial risk management

(a) Financial risk factors

The Group's activities expose it to a variety of financial risks: liquidity risk; market risk (interest rate and foreign currency risk); credit risk and inflation risk.

The Group's treasury function seeks to ensure that sufficient funding is available to meet foreseeable needs and to maintain reasonable headroom for contingencies and manages inflation and interest rate risk.

The principal financial risks faced by the Group relate to liquidity, interest rate and credit counterparty risk.

These risks and treasury operations are managed by the Group Chief Financial Officer in accordance with policies established by the Board. Major transactions are individually approved by the Board. Treasury activities are reported to the Board and are subject to review by internal audit.

Financial instruments are used to raise finance, manage risk, optimise the use of surplus funds and manage overall interest rate performance. The Group does not engage in speculative activity.

i) Liquidity risk

The Group actively maintains a mixture of long-term and short-term committed facilities which are designed to ensure the Group has sufficient available funds for operations and planned expansions equivalent to at least one year's forecast requirements at all times. Details of undrawn committed facilities and short-term facilities are provided in note 28.

Refinancing risk is managed under a Group policy that requires that no more than 20% of Group net borrowings should mature in any financial year.

The Group and water business have entered into covenants with lenders. While terms vary, these typically provide for limits on gearing (primarily based on the water business's regulatory capital value and unregulated EBITDA) and interest cover. Existing covenants are not impacted by subsequent changes to accounting standards.

3. Financial risk management *continued*

(a) Financial risk factors *continued*

Contractual undiscounted cash flows, including interest payments, at the balance sheet date were:

	Due within 1 year £m	Due between 1 and 2 years £m	Due between 2 and 5 years £m	Due over 5 years £m	Total £m
Group					
31 March 2023					
Non-derivative financial liabilities					
Borrowings excluding lease liabilities	**92.7**	**64.4**	**364.3**	**1,544.7**	**2,066.1**
Interest payments on borrowings	**86.7**	**83.0**	**208.3**	**768.7**	**1,146.7**
Lease liabilities including interest	**70.9**	**88.5**	**282.1**	**1,243.7**	**1,685.2**
Trade and other payables	**174.0**	**–**	**–**	**–**	**174.0**
Derivative contracts					
Derivative contracts – net payments/(receipts)	**(0.8)**	**(4.6)**	**(0.6)**	**0.3**	**(5.7)**
31 March 2022					
Non-derivative financial liabilities					
Borrowings excluding lease liabilities	70.0	101.4	221.0	1,596.9	1,989.3
Interest payments on borrowings	56.8	57.1	89.4	492.4	695.7
Lease liabilities including interest	189.4	46.4	227.7	1,157.7	1,621.2
Trade and other payables	134.4	–	–	–	134.4
Derivative contracts					
Derivative contracts – net payments/(receipts)	(3.6)	(6.5)	(7.9)	(2.2)	(20.2)
Company					
31 March 2023					
Non-derivative financial liabilities					
Borrowings (including intercompany borrowings)	**279.1**	**8.8**	**146.9**	**–**	**434.8**
Interest payments on borrowings	**9.6**	**9.3**	**6.7**	**6.0**	**31.6**
Trade and other payables	**3.6**	**–**	**–**	**–**	**3.6**
31 March 2022					
Non-derivative financial liabilities					
Borrowings (including intercompany borrowings)	312.8	–	75.1	79.4	467.3
Interest payments on borrowings	6.5	6.6	13.8	2.5	29.4
Trade and other payables	5.7	–	–	–	5.7

ii) Market risk

The treasury policy states at least 60% of the Group's debt should be fixed, this is managed through fixed rate debt and the use of derivatives to ensure these levels are met. Of the Group's net borrowings a proportion is RPI index-linked. The interest rate for index-linked debt is based mainly upon an RPI measure; due to current Ofwat methodology the Group has considered other index linked indices which are also used in determining the amount of revenue from customers of South West Water. The Group uses a combination of fixed rate, index-linked borrowings and fixed rate interest swaps as cash flow hedges of future variable interest payments to achieve this policy. The notional principal amounts of the interest rate swaps are used to determine settlement under those swaps and are not therefore an exposure for the Group. These instruments are analysed in note 23.

The Group has no significant interest-bearing assets upon which the net return fluctuates from market risk. Deposit interest receivable is expected to fluctuate in line with interest payable on floating rate borrowings. Consequently, the Group's income and cash generated from operations (note 37) are independent of changes in market interest rates.

For 2023 if interest rates on variable net borrowings had been on average 1% higher/lower with all other variables held constant, post-tax profit for the year and equity would have increased/decreased by £6.4 million (2022 post tax profit for the year and equity would have increased/decreased by £4.3 million), for the equity sensitivity fair value, with derivative impacts excluded. This provides an indication of the changes which could be expected and can be multiplied to support sensitivity analysis, the expected volatility is within the range of 0%-2%.

For 2023 if the indices on index-linked borrowings had been on average 1% higher/lower with all other variables held constant, post-tax profit for the year and equity would have decreased/increased by £3.8 million (2022 post tax profit for the year and equity would have increased/decreased by £6.5 million). This provides an indication of the changes which could be expected and can be multiplied to support sensitivity analysis, the expected volatility is within the range of 3%-7%.

Foreign currency risk occurs at transactional and translation level from borrowings and transactions in foreign currencies. These risks are managed through forward contracts, which provide certainty over foreign currency risk.

iii) Credit risk

Credit counterparty risk arises from cash and cash deposits, derivative financial instruments and exposure to customers, including outstanding receivables. Further information on the credit risk relating to trade and other receivables is given in note 22.

Counterparty risk arises from the investment of surplus funds and from the use of derivative financial instruments. The Board has agreed a policy for managing such risk which is controlled through credit limits, counterparty approvals, and rigorous monitoring procedures.

The Group has no other significant concentration of credit risk. The Group's surplus funds are managed by the Group's treasury function and are usually placed in short-term fixed interest deposits or the overnight money markets. Deposit counterparties must meet Board approved minimum criteria based on their short-term credit ratings and therefore be of good credit quality.

3. Financial risk management *continued*

(a) Financial risk factors *continued*

iv) Inflation risk

Market inflation has caused inflationary pressures across the Group, the Group has index linked facilities which are predominantly Retail Price Index (RPI) linked.

Inflation risk arises if the indexes increase meaning the Group will either be paying or accreting the inflation, this could put pressure on the gearing or interest cover ratios.

Inflation risk is mitigated through the index linked nature of our revenues and RCV calculations.

(b) Capital risk management

The Group's objectives when managing capital are to safeguard the Group's ability to continue as a going concern in order to provide returns for shareholders and benefits for other stakeholders and to maintain an optimal capital structure to minimise the cost of capital.

The Group's policy is to have a minimum of 12 months pre-funding of projected capital expenditure. At 31 March 2023 the Group had cash and facilities, including restricted funds, of £420 million (2022 £816 million), meeting this objective.

In order to maintain or adjust the capital structure, the Group seeks to maintain a balance of returns to shareholders through dividends and an appropriate capital structure of debt and equity for each business segment and the Group.

The Group monitors capital on the basis of the gearing ratio. This ratio is calculated as net borrowings divided by total capital. Net borrowings are analysed in note 38 and calculated as total borrowings less cash and cash deposits. Total capital is calculated as total shareholders' equity plus net borrowings. The Group currently manages a net borrowings position of £2,965.4 million (2022 £2,682.9 million).

The gearing ratios at the balance sheet date were:

	2023 £m	2022 £m
Net borrowings (note 38)	**2,965.4**	2,682.9
Total equity	**1,125.2**	1,276.6
Total capital	**4,090.6**	3,959.5
Gearing ratio	**72.6%**	67.8%

The water segment is also monitored on the basis of the ratio of its net borrowings to regulatory capital value. Ofwat's notional gearing target for the K7 (2020-25) regulatory period is set at 60%.

	South West Water*	
	2023 £m	2022 £m
Shadow Regulatory Capital Value	**4,715.9**	4,236.0
Net borrowings	**2,865.3**	2,639.1
Net borrowings/Regulatory Capital Value	**60.8%**	62.3%

*Net borrowing reflects South West Water Limited's group of companies, with 2022 reanalysed to exclude the impact of intra-group loans, to provide comparative performance.

The Group has entered into covenants with lenders and, while terms vary, these typically provide for limits on gearing and interest cover. The Group has been in compliance with its covenants during the year.

(c) Determination of fair values

The Group uses the following hierarchy for determining the fair value of financial instruments by valuation technique:

- Quoted prices (unadjusted) in active markets for identical assets or liabilities (level 1)
- Inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices) (level 2)
- Inputs for the asset or liability that are not based on observable market data (that is, unobservable inputs) (level 3).

The Group's financial instruments are valued principally using level 2 measures as analysed in note 23.

The fair value of financial instruments not traded in an active market (for example over-the-counter derivatives) is determined by using valuation techniques. A variety of methods and assumptions are used based on market conditions existing at each balance sheet date. Quoted market prices or dealer quotes for similar instruments are used for long-term debt. Other techniques, such as estimated discounted cash flows, are used to determine fair value for the remaining financial instruments. The fair value of interest rate swaps is calculated as the present value of the estimated future cash flows.

The carrying values, less expected credit losses, of trade receivables and payables are assumed to approximate to their fair values.

4. Critical accounting judgements and estimates

The Group's principal accounting policies are set out in note 2. Management is required to exercise significant judgement and make use of estimates and assumptions in the application of these policies. Estimates are based on factors including historical experience and expectations of future events that management believe to be reasonable. However, given the judgemental nature of such estimates, actual results could be different from the assumptions used.

Estimates

Provision for doubtful debts

The Group has a material level of exposure to collection of trade receivables. Provisions in respect of these balances are calculated with reference to historical credit loss experience, adjusted for forward-looking factors which by their nature are subject to uncertainty. Analysis of actual recovery compared with provisioning levels have not, to date, resulted in material variances.

Under its regular review procedures at the balance sheet date, the Group applies a simplified approach in calculating ECLs for trade receivables and contract assets. Therefore, the Group does not track changes in credit risk but instead recognises a loss allowance based on lifetime ECLs at each reporting date. Each subsidiary has established a provision matrix that is informed by its historical credit loss experience, adjusted for forward-looking factors specific to the receivables and the economic environment. The Group's policy is to write-off trade receivables where the expectation of recovery is considered highly unlikely.

The actual level of debt collected may differ from the estimated levels of recovery. As at 31 March 2023 the Group's current trade receivables were £280.3 million (2022 £296.2 million), against which £106.5 million (2022 £100.4 million) had been provided for ECLs (note 22). Whilst the provisions are considered to be appropriate, changes in estimation basis or in economic conditions could lead to a change in the level of provisions recorded and consequently the charge or credit to the Income Statement.

Retirement benefit obligations

The Group operates defined benefit pension schemes for which actuarial valuations are carried out as determined by the trustees at intervals of not more than three years. The most recent triennial valuation of the main scheme was as at 31 March 2022, the outcome of which is summarised in note 30.

The pension cost and liabilities under IAS 19 are assessed in accordance with Directors' best estimates using the advice of an independent qualified actuary and assumptions in the latest actuarial valuation. The assumptions are based on member data supplied to the actuary and market observations for interest rates and inflation, supplemented by discussions between the actuary and management. The mortality assumption uses a scheme-specific calculation based on CMI 2019 actuarial tables with an allowance for future longevity improvement. The principal assumptions used to measure schemes' liabilities, sensitivities to changes in those assumptions and future funding obligations are set out in note 30.

Judgements

Non-underlying items

In establishing which items are disclosed separately as non-underlying, to enable a full understanding of the Group's financial performance, the Directors exercise their judgement in assessing the size, nature or incidence of specific items. See note 6 for further details.

Goodwill allocation

Goodwill arising on the acquisition of Bristol Water is allocated to the group of cash-generating units that are expected to benefit from the synergies of the combination, the 'Water CGU'. The Water CGU comprises the regions of South West Water, Bournemouth Water and Bristol Water. The Water CGU operates under one management structure with functional integration across the operating segment generating the synergies of the combination. The recoverable amount is the higher of fair value, less costs to sell, and value-in-use. Value-in-use represents the present value of projected future cash flows expected to be derived from a CGU, discounted using a pre-tax discount rate which reflects an assessment of the market cost of capital of the CGU. Impairments are charged to the income statement in the year in which they arise.

Other estimates

Management assessed and resolved that the level of estimation for revenue recognition of accrued revenue relating to water and wastewater should not be considered critical as the estimates are largely calculated on a systematic basis and have not, to date, resulted in a material adjustment within the following 12-month period. However, management consider the total level of estimation of accrued revenue relating to water and wastewater to be material and highlight this as a material other estimate.

The acquisition of Bristol Water in June 2021 has been accounted for using the acquisition method under IFRS 3. The identifiable assets, liabilities and contingent liabilities are recognised at their fair value at date of acquisition. The fair value of the net assets identified were determined with assistance from independent experts using professional valuation techniques appropriate to the individual category of asset or liability. Calculating the fair values of net assets, notably the fair values of property, plant and equipment given the nature of the infrastructure assets acquired, involves estimation and consequently the fair value exercise is recorded as an other accounting estimate. The depreciation charge is sensitive to the value of property, plant and equipment, a higher or lower fair value calculation would lead to a change in the depreciation charge in the period following acquisition. The operations of Bristol Water are now part of South West Water with all activities operating in the same industry, therefore identical or similar transactions within South West Water do not require new significant judgements or estimates to be made by the Group. In early June 2022 the final review of tax balances was completed, with the identification of capital assets non-qualifying for tax purposes, this has led to an increase in the deferred tax liability with an offsetting increase in the total value of goodwill recognised on acquisition of £5.5 million (see note 43), consequently the balance sheet has been restated retroactively to the acquisition date.

The property, plant and equipment of the Group relates primarily to infrastructure assets (being water mains and sewers, impounding and pumped raw water storage reservoirs, dams, pipelines and sea outfalls) as well as other assets which include fixed plant and operational properties. The useful economic lives of these types of asset vary from 10 to 200 years. Asset lives are reviewed annually and amended where changes are made to assumptions relating to the expected life of the asset from judgement around usage and performance experience, technological advancement and other relevant factors. Overall assessments on the impact of climate change on long life assets have been completed and will be continuously updated for the latest available information. The most recent assessment of the impact on climate change, which includes the potential to mitigate adverse impacts, has not identified any specific impact on the useful economic lives of long life assets. Environmental factors and climate change form part of the planning process for new capital expenditure. The depreciation charge is sensitive to amendments of the useful economic lives of these assets, a significant change in the estimated life of these assets could have a material impact on depreciation, this is therefore noted as a material other estimate.

5. Segmental information

Operating segments are reported in a manner consistent with internal reporting provided to the Chief Operating Decision-Maker (CODM), which has been identified as the Pennon Group plc Board. The earnings measures below are used by the Board in making decisions.

The Group is organised into two operating segments. The water segment comprises the regulated water and wastewater services undertaken by South West Water. The non-household retail business reflects the services provided by Pennon Water Services.

Segment assets include goodwill and other intangible assets, property, plant and equipment, inventories, trade and other receivables and cash and cash deposits. Segment liabilities comprise operating liabilities and borrowings and exclude taxation. The other segment liabilities include the Company's financing arrangements and Group taxation liabilities. Capital expenditure comprises additions to property, plant and equipment.

	2023 £m	2022 £m
Revenue		
Water	**701.3**	687.8
Non-household retail	**218.0**	195.3
Other	**8.6**	8.5
Less intra-segment trading [1]	**(102.9)**	(99.3)
Total underlying revenue	**825.0**	792.3
Water non-underlying revenue (note 6)	**(27.8)**	–
	797.2	792.3
Operating profit/(loss) before depreciation, amortisation and non-underlying items (Underlying EBITDA)		
Water	**308.4**	385.0
Non-household retail	**4.3**	3.4
Other	**(4.9)**	(4.5)
	307.8	383.9
Operating profit/(loss) before non-underlying items		
Water	**159.4**	244.0
Non-household retail	**3.6**	2.6
Other	**(9.9)**	(9.4)
	153.1	237.2
Profit/(loss) before tax and non-underlying items		
Water	**14.1**	146.0
Non-household retail	**1.8**	1.0
Other	**0.9**	(3.5)
	16.8	143.5
(Loss)/profit before tax		
Water	**(29.6)**	144.0
Non-household retail	**1.8**	1.0
Other	**19.3**	(17.3)
	(8.5)	127.7

1. Intra-segment transactions between and to different segments are under normal market-based commercial terms and conditions. Intra-segment revenue of the other segment is at cost.

	Water £m	**Non-household retail £m**	**Other £m**	**Eliminations £m**	**Group £m**
Balance sheet					
31 March 2023					
Assets (excluding carrying value in associated companies)	**4,925.3**	**59.3**	**594.6**	**(403.3)**	**5,175.9**
Carrying value in associated companies	**–**	**–**	**9.6**	**–**	**9.6**
Total assets	**4,925.3**	**59.3**	**604.2**	**(403.3)**	**5,185.5**
Liabilities	**(3,925.2)**	**(55.4)**	**(483.0)**	**403.3**	**(4,060.3)**
Net assets	**1,000.1**	**3.9**	**121.2**	**–**	**1,125.2**
31 March 2022					
Assets (excluding carrying value in associated companies)	4,872.8	57.1	776.3	(384.1)	5,322.1
Carrying value in associated companies	9.6	–	–	–	9.6
Total assets	4,882.4	57.1	776.3	(384.1)	5,331.7
Liabilities	(3,810.4)	(54.8)	(576.0)	384.1	(4,057.1)
Net assets	1,072.0	2.3	200.3	–	1,274.6

5. Segmental information *continued*

Segment liabilities of the water segment comprise of operating liabilities and borrowings. The other segment includes Company only assets and liabilities as well as Group taxation liabilities and should be considered in conjunction with the eliminations column.

	Notes	Water £m	Non-household retail £m	Other and eliminations £m	Group £m
Other information					
31 March 2023					
Intangible asset additions	16	**4.5**	**0.1**	**–**	**4.6**
Amortisation of other intangible assets	7	**3.4**	**0.2**	**–**	**3.6**
Capital expenditure (Property, plant and equipment)	17	**353.6**	**–**	**0.1**	**353.7**
Depreciation	7	**145.6**	**0.5**	**5.0**	**151.1**
Finance income	8	**6.2**	**0.1**	**21.3**	**27.6**
Finance costs	8	**151.5**	**1.9**	**(7.6)**	**145.8**
31 March 2022					
Intangible asset additions	16	3.4	0.2	–	3.6
Amortisation of other intangible assets	7	3.2	0.2	–	3.4
Capital expenditure (Property, plant and equipment)	17	237.3	–	–	237.3
Depreciation	7	137.8	0.7	4.8	143.3
Finance income	8	3.9	–	(1.3)	2.6
Finance costs	8	101.8	1.6	(7.1)	96.3

Finance income and costs above reflect the segment in which the amounts arise and exclude intercompany transactions.

All revenue is generated in the United Kingdom. The grouping of revenue streams by how they are affected by economic factors, as required by IFRS 15, is as follows:

Year ended 31 March 2023	Water £m	Non-household retail £m	Other £m	Total £m
Segment revenue – underlying	**701.3**	**218.0**	**8.6**	**927.9**
Segment revenue – non-underlying (note 6)	**(27.8)**	**–**	**–**	**(27.8)**
Inter-segment revenue	**(94.7)**	**–**	**(8.2)**	**(102.9)**
Revenue from external customers	**578.8**	**218.0**	**0.4**	**797.2**
Significant service lines				
Water	**578.8**	**–**	**–**	**578.8**
Non-household retail	**–**	**218.0**	**–**	**218.0**
Other	**–**	**–**	**0.4**	**0.4**
	578.8	**218.0**	**0.4**	**797.2**

Year ended 31 March 2022	Water £m	Non-household retail £m	Other £m	Total £m
Segment revenue – underlying	687.8	195.3	8.5	891.6
Inter-segment revenue	(90.9)	(0.2)	(8.2)	(99.3)
Revenue from external customers	596.9	195.1	0.3	792.3
Significant service lines				
Water	596.9	–	–	596.9
Non-household retail	–	195.1	–	195.1
Other	–	–	0.3	0.3
	596.9	195.1	0.3	792.3

The Group's country of domicile is the United Kingdom and this is the country in which it generates the majority of its revenue. The Group's non-current assets are all located in the United Kingdom.

6. Non-underlying items

Non-underlying items are those that in the Directors' view should be separately disclosed by virtue of their size, nature or incidence to enable a full understanding of the Group's financial performance in the year and business trends over time. The presentation of results is consistent with internal performance monitoring.

Revenue	Notes	2023 £m	2022 £m
WaterShare+[1]		**(20.2)**	–
Drought incentive[2]		**(7.6)**	–
Operating costs			
Drought costs[2]		**(9.4)**	–
WaterShare+[1]		**(2.2)**	–
Integration and CMA merger review costs[3]		**(4.3)**	(6.9)
Bristol Water acquisition costs[3]		**–**	(8.9)
Earnings before interest, tax, depreciation and amortisation		**(43.7)**	(15.8)
Bond redemption[4]		**18.4**	–
Net tax credit arising on non-underlying items above[5]	9	**4.7**	1.3
Deferred tax change in rate[6]	9	**0.6**	(99.5)
Net non-underlying charge		**(20.0)**	(114.0)

1. In September 2020, the Group offered its WaterShare+ scheme to its customers whereby customers could choose to accept a credit on their bill or take shares in Pennon Group plc. The scheme has operated again in the year ended 31 March 2023. The value of the rebate equated to £13 per customer and the total value of £20.2 million was recognised in full as a non-underlying reduction to revenue in the year ended 31 March 2023. £19.9 million of the WaterShare+ credits were taken as credits on customers' bills, with the balance of £0.3 million being taken as shares in Pennon Group Plc. This item was non-underlying in nature given its individual size and its non-recurring nature. Additional costs of £2.2 million were incurred in relation to the offering.
2. 2022 was one of the driest and hottest years on record. Elevated demand on the South West Water region from increased tourism and the hot, dry weather led to an approximate 15% increase in distribution input in the year against the expected level from 2017 included in the drought plan. The combination of these individually extreme factors led to extremely low water storage levels in the Colliford Water Resource Zone, with the main supply of Colliford reservoir falling to around 14% capacity in October. A drought was declared by the Environment Agency in Devon and Cornwall in August 2022. In order to react to the drought and water shortage, South West Water invoked a series of emergency measures and one-off expenditure to ensure the region could be supplied with water over the summer and continuing into 2023. Due to the exceptional combination of these events and the significance of the emergency actions, certain costs have been classified as non-underlying given their size, nature and non-recurring incidence. The costs directly addressing these exceptional circumstances include charges for drought permits, water tankering and other water saving measures. In November 2022, South West Water asked households in Cornwall to reduce water usage as part of the 'Stop The Drop' campaign to increase reservoir levels. Household customers were offered a £30 bill credit if Colliford reservoir reached 30% storage capacity by 31 December 2022 from a low of around 14%. In December 2022 the company announced the water level in Colliford reservoir reached 30% and as a result all household customers in Cornwall received a £30 credit on their bill. This one-off incentive was provided as part of the response to the drought conditions in the Cornwall area in order to further prompt customers to reduce water usage. The total value of the bill credits amounted to £7.6 million.
3. The Group incurred expenses of £4.3 million in the year ended 31 March 2023. These related to the integration and statutory transfer of Bristol Water into South West Water. These costs are classified as non-underlying due to their non-recurring nature. In the year ended 31 March 2022, the Group incurred expenses of £8.9 million in relation to the acquisition of Bristol Water and £6.9 million on the resulting merger review by the Competition and Markets Authority and other integration costs.
4. On 17 October 2022 Bristol Water plc gave notice of redemption of the £40 million bonds due to be repaid in March 2041. The bonds were redeemed as part of the statutory transfer of the business of Bristol Water to South West Water. The Group carrying value of the bonds at redemption was £91.3 million. The bonds were redeemed on 17 November 2022 for £72.3 million, and the difference arising on early settlement was credited to finance costs in the year. Associated legal costs of c.£1 million have been incurred in relation to the bond redemption. The redemption of the bonds is non-recurring and of a material value, hence the credit has been treated as non-underlying.
5. The tax credit arising on non-underlying items reflects a £2.8 million current tax credit in respect of losses which will be carried back against prior year taxable profits. A deferred tax credit of £1.9 million relates to tax losses carried forwards and the deferred tax unwind of the fair value adjustment in relation to the Bristol Water bond terminated in the year. The prior year credit of £1.3 million related to a current tax credit on Group strategic review costs.
6. Following the Chancellor's Budget on 4 March 2021 and subsequent substantial enactment of the Finance Act on 24 May 2021, the UK's main rate of corporation tax increased to 25% from 1 April 2023. All deferred tax assets and liabilities were therefore reviewed and where they will crystallise after 1 April 2023 recalculated to crystallise at 25%, hence giving a non-underlying deferred tax charge in the year ended 31 March 2022 of £99.5 million. This charge is considered non-underlying due to it arising from a material legislative change and its treatment is consistent with that applied in relation to previous changes in corporation tax rates. A £0.6 million deferred tax credit in respect of rate change arises on losses carried forwards which will be relieved at 25%.

7. Operating costs

	Notes	2023 £m	2022 £m
Employment costs before non-underlying items	13	**102.2**	90.4
Raw materials and consumables		**33.6**	22.9
Other operating expenses before non-underlying items include:			
Profit on disposal of property, plant and equipment		**(0.4)**	(1.0)
Short-term/low value asset lease expense		**5.3**	1.7
Government grant receivable		**(18.6)**	–
Trade receivables impairment	22	**7.8**	5.6
Depreciation of property, plant and equipment:			
• Owned assets	17	**118.3**	105.5
• Under leases	17	**32.8**	37.8
Amortisation of other intangible assets	16	**3.6**	3.4

During the year the group received financial support from the UK Government's Energy Relief Bill Scheme totalling £18.6 million (2022 nil). Operating costs include a charge of £15.9 million (2022 £15.8 million) relating to non-underlying items, as detailed in note 6.

Fees payable to the Company's auditor in the year were:

	2023 £000	2022 £000
Fees payable to the Company's auditor and its associates for the audit of parent company and consolidated financial statements	**384**	360
Fees payable to the Company's auditor and its associates for other services:		
The audit of Company's subsidiaries	**932**	474
Audit-related assurance services	**120**	108
Other non-audit services	**43**	28
Total fees	**1,479**	970
Fees payable to the Company's auditor in respect of Pennon Group pension schemes:		
Audit	**55**	55

Expenses reimbursed to the auditor in relation to the audit of the Group were £79,000 (2022 £50,000).

A description of the work of the Audit Committee is set out in its report on pages 120 to 125 which includes an explanation of how the auditor's objectivity and independence are safeguarded when non-audit services are provided by the auditor's firm.

8. Net finance costs

		2023			2022		
	Notes	Finance cost £m	Finance income £m	Total £m	Finance cost £m	Finance income £m	Total £m
Cost of servicing debt							
Bank borrowings and overdrafts		**(111.3)**	**–**	**(111.3)**	(73.9)	–	(73.9)
Interest element of lease payments		**(30.8)**	**–**	**(30.8)**	(20.3)	–	(20.3)
Other finance costs		**(3.7)**	**–**	**(3.7)**	(2.1)	–	(2.1)
Interest received		**–**	**4.9**	**4.9**	–	2.0	2.0
Net gains on derivative financial instruments		**–**	**2.3**	**2.3**	–	–	–
		(145.8)	**7.2**	**(138.6)**	(96.3)	2.0	(94.3)
Notional interest							
Retirement benefit obligations	30	**–**	**2.0**	**2.0**	–	0.6	0.6
Net finance costs (underlying)		**(145.8)**	**9.2**	**(136.6)**	(96.3)	2.6	(93.7)
Finance income (non-underlying)	6	**–**	**18.4**	**18.4**	–	–	–
Net finance costs (including non-underlying)		**(145.8)**	**27.6**	**(118.2)**	(96.3)	2.6	(93.7)

In addition to the above, finance costs of £5.0 million (2022 £1.3 million) have been capitalised on qualifying assets included in property, plant and equipment, at an average borrowing rate of 5.7% (2022 4.1%).

Other finance costs include £1.1 million (2022 £0.9 million) of dividends payable on listed preference shares issued by Bristol Water, which are classified as debt (see note 28).

9. Taxation

	Before non-underlying items 2023 £m	Non-underlying items (note 6) 2023 £m	Total 2023 £m	Before non-underlying items 2022 £m	Non-underlying items (note 6) 2022 £m	Total 2022 £m
Analysis of charge in year						
Current tax (credit)/charge	**(2.7)**	**(2.8)**	**(5.5)**	5.0	(1.3)	3.7
Deferred tax – other	**(0.6)**	**(1.9)**	**(2.5)**	8.9	–	8.9
Deferred tax arising on change of rate of corporation tax	**(0.3)**	**(0.6)**	**(0.9)**	–	99.5	99.5
Total deferred tax charge/(credit)	**(0.9)**	**(2.5)**	**(3.4)**	8.9	99.5	108.4
Tax (credit)/charge for year	**(3.6)**	**(5.3)**	**(8.9)**	13.9	98.2	112.1

UK corporation tax is calculated at 19% (2022 19%) of the estimated assessable profit for the year.

UK corporation tax for the Group is stated after a credit relating to prior year current tax of £2.7 million (2022 £1.7 million credit) and a prior year deferred tax charge of £1.0 million (2022 £10.2 million credit). These items arise following the recording of the routine return to provision adjustments following the submission of the tax computations for the year ended 31 March 2022 to HMRC ahead of the 31 March 2023 filing deadline.

The tax for the year differs from the theoretical amount which would arise using the standard rate of corporation tax in the UK of 19% (2022 19%) as follows:

	2023 £m	2022 £m
Reconciliation of total tax charge		
(Loss)/profit before tax	**(8.5)**	127.7
(Loss)/profit multiplied by the standard rate of UK corporation tax of 19% (2022 19%)	**(1.6)**	24.3
Effects of:		
(Income)/expenses not deductible for tax purposes	**(0.4)**	1.8
Joint venture profits not taxable	**(0.1)**	–
Adjustments to tax charge in respect of prior years	**(1.7)**	(11.9)
Change in UK tax rates	**(1.0)**	99.5
Depreciation charged on non-qualifying assets	**0.7**	0.7
Other	**(4.8)**	(2.3)
Tax (credit)/charge for year	**(8.9)**	112.1

	2023 £m	2022 £m
Reconciliation of current tax charge		
(Loss)/profit before tax	**(8.5)**	127.7
(Loss)/profit multiplied by the standard rate of UK corporation tax of 19% (2021 19%)	**(1.6)**	24.3
Effects of:		
Relief for capital allowances in place of depreciation	**(37.6)**	(36.3)
Disallowance of depreciation charged in the accounts	**24.4**	22.4
Other timing differences	**(11.1)**	(7.2)
(Income)/expenses not deductible for tax purposes	**(0.4)**	1.8
Joint venture profits not taxable	**(0.1)**	–
Accounting policy alignment adjustment on acquisition of Bristol Water	**5.0**	–
Adjustments to tax charge in respect of prior years	**(2.7)**	(1.7)
Depreciation charged on non-qualifying assets	**0.7**	0.6
Tax losses carried forward	**18.6**	–
Relief for capitalised interest and foreign exchange gains/losses	**(0.7)**	(0.2)
Current tax (credit)/charge for year	**(5.5)**	3.7

The Group's current tax credit is higher than the UK headline rate of 19%, primarily due to capital allowances. Capital allowances provide tax relief when a business incurs expenditure on qualifying capital items such as plant and machinery used by the business. As an infrastructure business, these allowances help the Group to plan major investment and consequentially to maintain lower customer bills, as corporation tax relief is given against the investments made.

The Group benefits from the 130% super-deductions and 50% enhanced allowances in respect of qualifying spend relating to contracts entered into after 3 March 2021.The Group incurs significant capital expenditure each year as it maintains and enhances it assets for the benefit of its customers, communities and the environment. These enhanced allowances have increased capital allowance claims for the year and contributed significantly to the current tax credit for the year. There is also a consequently higher deferred tax liability and charge due to the additional capital allowance deductions together with the increase in the rate of corporation tax to 25% from April 2023.

9. Taxation *continued*

Other differences relate to the timing of relief for items including pensions, fair value items and financial derivatives. The increase in the year relates mainly to the unwind of the fair value adjustment on the Bristol Water bond which was terminated in the year and additional pension contributions relief as a result of spreading in accordance with tax legislation.

Profits from joint ventures are included in the consolidated accounts on an after tax basis, as such these profits are not taxable in the Group accounts.

The accounting policy alignment relates to Bristol Water plc aligning their accounting policy in relation to deferred income to that of South West Water on acquisition. Despite the accounting adjustments reflecting the restated 2022 figures, for tax purposes the adjustment will be subject to corporation tax during the year ended 31 March 2023, hence the adjustment in the year.

Adjustments to the tax charge in respect of prior year arise from the return to provision adjustments booked having completed and submitted the corporation tax returns for the year ended 31 March 2022 in March 2023. This is a routine item with any adjustments reflected in the following years tax charge.

Depreciation charge on non-qualifying assets generates a permanent adjustment which increases the tax charge. Non-qualifying assets are those which do not qualify for writing down tax allowances, including certain fixed assets typically in relation to older buildings and premises where tax relief is not available.

Tax losses generated in the year and carried forward generate a deferred tax rather than current tax credit, hence the adjustment to current tax. When utilised, the adjustment will be reflected through a movement from deferred to current tax.

Immediate tax relief is available in respect of capitalised interest and foreign exchange gains/losses.

In addition to the amounts recognised in the income statement, the following tax charges / (credits) (which include the effect of the change in tax rate) were recognised:

	2023 £m	2022 £m
Amounts recognised directly in other comprehensive income		
Deferred tax credit on defined benefit pension schemes	**(9.8)**	(2.4)
Deferred tax charge on cash flow hedges	**7.3**	6.5
Amounts recognised directly in equity		
Deferred tax charge on share-based payments	**0.5**	–

Factors affecting future tax charges

The UK main rate of corporation tax will increase to 25% from 1 April 2023. This change was substantively enacted on 24 May 2021, as such deferred tax liabilities and assets were recalculated and recorded at the rate they are expected to unwind. This increased the tax charge in the income statement during the year ended 31 March 2022 by £99.5m, with a credit of £8.7m taken through the SOCI/Equity in respect of retirement obligations, derivatives and share based payments.

The Chancellor announced in the March 2023 Budget that super deductions will be replaced by full expensing for the next three years in respect of plant and machinery assets. The 50% first year allowance in relation to special rate assets will also continue until 31 March 2026. The Group therefore anticipates generating current tax losses for the next few years.

10. Profit of the parent company

	2023 £m	2022 £m
Profit attributable to ordinary shareholders' equity dealt within the accounts of the parent company	**8.4**	74.5

As permitted by Section 408 of the Companies Act 2006, no income statement or statement of comprehensive income is presented for the Company.

11. 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 (note 36), which are treated as cancelled.

For diluted earnings per share, the weighted average number of ordinary shares in issue is adjusted to include all dilutive potential ordinary shares. The Group has two types of dilutive potential ordinary shares – those share options granted to employees where the exercise price is less than the average market price of the Company's ordinary shares during the year; and the contingently issuable shares under the Group's Performance and Co-investment Plan, the long-term incentive plan and the deferred shares element of the Annual Incentive Bonus Plan, based on performance criteria for the vesting of the awards.

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

	2023	2022
Number of shares (millions)		
For basic earnings per share	**261.9**	312.1
Effect of dilutive potential ordinary shares from share options	**0.9**	1.7
For diluted earnings per share	**262.8**	313.8

11. Earnings per share *continued*

Basic and diluted earnings per ordinary share

Earnings per ordinary share before non-underlying items and deferred tax are presented as the Directors believe that this measure provides a more useful year on year comparison of business trends and performance. Deferred tax is excluded as the Directors believe it reflects a distortive effect of changes in corporation tax rates and the level of long-term capital investment. Earnings per share have been calculated as follows:

	2023			2022		
	(Loss)/profit after tax £m	**Earnings per share**		Profit after tax £m	Earnings per share	
		Basic p	**Diluted p**		Basic p	Diluted p
Statutory earnings attributable to ordinary shareholders of the parent	**0.1**	**–**	**–**	15.4	4.9	4.9
Deferred tax (credit)/charge before non-underlying items	**(0.9)**	**(0.3)**	**(0.3)**	8.9	2.9	2.8
Non-underlying items (net of tax)	**20.0**	**7.6**	**7.6**	114.0	36.5	36.4
Adjusted earnings	**19.2**	**7.3**	**7.3**	138.3	44.3	44.1

12. Dividends

	2023 £m	2022 £m
Amounts recognised as distributions to ordinary equity holders in the year		
Interim dividend paid for the year ended 31 March 2022 11.70p (2021 6.77p) per share	**31.6**	28.6
Final dividend paid for the year ended 31 March 2022 26.83p (2021 14.97p) per share	**70.0**	63.2
Special dividend paid for the year ended 31 March 2022 nil (2021 355.0p) per share	**–**	1,498.5
	101.6	1,590.3
Proposed dividends		
Proposed interim dividend for the year ended 31 March 2023: 12.96p (2022 11.70p) per share	**33.9**	32.4
Proposed final dividend for the year ended 31 March 2023: 29.77p (2022 26.83p) per share	**77.8**	69.6
	111.7	102.0

The proposed interim and final dividends have not been included as liabilities in these financial statements.

The proposed interim dividend for 2023 was paid on 5 April 2023 and the proposed final dividend is subject to approval by shareholders at the AGM.

13. Employment costs

	Notes	**2023 £m**	2022 £m
Wages and salaries		**110.0**	96.3
Social security costs		**12.1**	9.7
Pension costs	30	**11.0**	11.1
Share-based payments	33	**2.4**	2.2
Total employment costs		**135.5**	119.3
Charged:			
• Employment costs (excluding non-underlying items) – consolidated income statement		**102.2**	90.4
• Employment costs (non-underlying items) – consolidated income statement		**–**	1.7
• Capital schemes – property, plant and equipment		**32.7**	27.2
• Research and development		**0.6**	–
Total employment costs		**135.5**	119.3

Details of Directors' emoluments are set out in note 14. There are no personnel, other than Directors, who as key management exercise authority and responsibility for planning, directing and controlling the activities of the Group. Members of other executive committees assist the Directors in their duties but do not hold authority to control the activities of the Group.

	2023	2022
Employees (average full-time equivalent number)		
The average monthly number of employees (including Executive Directors) was:		
Water	**2,639**	2,394
Non-household retail	**158**	177
Other	**67**	65
Total	**2,864**	2,636

14. Directors' emoluments

	2023 £000	2022 £000
Executive Directors:		
• Salary	**784**	775
• Performance-related bonus paid or payable	**51**	149
• Share-based payments	**786**	707
• Other emoluments, including payments in lieu of pension provision	**111**	116
Non-Executive Directors	**583**	523
	2,315	2,270

The cost of share-based payments represents the amount charged to the income statement, as described in note 33. The aggregate gains on vesting of Directors' share-based awards amounted to a total of £142,000 (2022 £180,000).

Total emoluments include nil (2022 nil) payable to Directors for services as directors of subsidiary undertakings.

At 31 March 2023 no Directors (2022 none) are accruing retirement benefits under defined benefit pension schemes in respect of which the Group contributed. In the previous year ending 31 March 2022, the defined benefit pension scheme closed to future accrual, on 30 June 2021, and during the prior period up to the date of closure to future accrual the company contributed £12,000 in respect of one Director.

At 31 March 2023 two Directors (2022 two) are members of the Group's defined contribution pension scheme in respect of which the Group contributed £4,000 (2022 £3,000).

At 31 March 2023 two Directors received payments in lieu of pension provision (2022 two).

More detailed information concerning Directors' emoluments (including pensions and the highest paid Director) and share interests is shown in the Directors' remuneration report on pages 136 to 157.

15. Goodwill

	£m
Cost:	
At 1 April 2021	42.3
Acquisition of Bristol Water Group (note 43)	121.6
At 31 March 2022	163.9
At 31 March 2023	163.9
Carrying amount:	
At 1 April 2021	42.3
At 31 March 2022 (restated)	163.9
At 31 March 2023	**163.9**

Goodwill acquired in a business combination is allocated at acquisition to the CGU expected to benefit from that business combination. During the year ended 31 March 2022, the Group acquired the Bristol Water Group, adding £121.6 million to goodwill (see note 43).

All goodwill represents the water business, therefore this is the lowest level at which goodwill is monitored and tested.

An adjustment to the preliminary accounting for the Bristol Water acquisition has been made within the measurement period ending 2 June 2022, this adjustment is presented retrospectively and the 31 March 2022 balance sheet figures have been adjusted accordingly (see note 4).

Impairment testing of goodwill

The Group tests goodwill for impairment annually, or more frequently if there are any indications that impairment may have arisen.

The recoverable amount of the water business segment is assessed using level 2 fair value hierarchy techniques, with reference to the market value of the water business, using a market-based observable premium, based on historical water industry merger and acquisition activity, to regulated capital value as defined by ofwat.

The results of tests performed during the year demonstrate significant headroom in the water CGU, and it is judged that no reasonable change in the key assumptions would cause the carrying amount of the CGUs to exceed the recoverable amount.

16. Other intangible assets

	Patents £m	Other £m	Total £m
Cost:			
At 1 April 2021	0.2	4.0	4.2
Additions	–	3.6	3.6
Acquisition of Bristol Water Group	–	12.8	12.8
Disposals	(0.2)	(0.8)	(1.0)
At 31 March 2022	–	19.6	19.6
Additions	–	4.6	4.6
Disposals	–	(1.9)	(1.9)
At 31 March 2023	–	22.3	22.3
Accumulated amortisation:			
At 1 April 2021	0.2	2.8	3.0
Charge for year	–	3.4	3.4
Disposals	(0.2)	(0.5)	(0.7)
At 31 March 2022	–	5.7	5.7
Charge for year	–	3.6	3.6
Disposals	–	(1.9)	(1.9)
At 31 March 2023	–	7.4	7.4
Carrying amount:			
At 1 April 2021	–	1.2	1.2
At 31 March 2022	–	13.9	13.9
At 31 March 2023	**–**	**14.9**	**14.9**

Other, including computer software, is amortised over the useful life of the assets which at acquisition was ten years. The average remaining life is one year (2022 two years).

The carrying values of other intangible assets are reviewed annually or when events or changes in circumstance indicate that the carrying amounts may not be fully recoverable.

17. Property, plant and equipment

	Land and buildings £m	Infrastructure assets £m	Operational properties £m	Fixed and mobile plant, vehicles and computers £m	Construction in progress £m	Total £m
Group						
Cost:						
At 31 March 2021	126.4	2,042.4	777.6	2,078.9	117.8	5,143.1
Additions	1.3	40.5	7.5	67.3	120.7	237.3
Acquisition of Bristol Water Group	56.4	644.0	161.3	60.2	22.9	944.8
Assets adopted at fair value	–	11.0	–	–	–	11.0
Grants and contributions	–	–	–	–	(3.2)	(3.2)
Disposals	(0.2)	(1.2)	(1.3)	(2.4)	–	(5.1)
Transfers/reclassifications	2.8	17.7	7.2	46.3	(74.0)	–
At 31 March 2022	186.7	2,754.4	952.3	2,250.3	184.2	6,327.9
Additions	0.7	52.3	11.4	85.3	204.0	353.7
Assets adopted at fair value	–	14.3	–	–	–	14.3
Disposals	(0.3)	(1.5)	(0.6)	(2.4)	–	(4.8)
Transfers/reclassifications	1.7	43.8	8.5	43.8	(97.8)	–
At 31 March 2023	188.8	2,863.3	971.6	2,377.0	290.4	6,691.1
Accumulated depreciation:						
At 31 March 2021	18.9	335.6	294.0	1,273.6	–	1,922.1
Charge for year	4.2	33.7	19.2	89.5	–	146.6
Disposals	–	(1.2)	(1.3)	(2.3)	–	(4.8)
At 31 March 2022	23.1	368.1	311.9	1,360.8	–	2,063.9
Charge for year	4.5	36.3	20.6	93.4	–	154.8
Disposals	(0.3)	(1.5)	(0.4)	(2.3)	–	(4.5)
At 31 March 2023	27.3	402.9	332.1	1,451.9	–	2,214.2
Net book value:						
At 31 March 2021	107.5	1,706.8	483.6	805.3	117.8	3,221.0
At 31 March 2022	163.6	2,386.3	640.4	889.5	184.2	4,264.0
At 31 March 2023	**161.5**	**2,460.4**	**639.5**	**925.1**	**290.4**	**4,476.9**

Of the total depreciation charge of £154.8 million (2022 £146.6 million), £1.5 million (2022 £1.3 million) has been charged to capital projects, £2.2 million (2022 £2.0 million) has been offset by deferred income and £151.1 million (2022 £143.3 million) has been charged against profits. Asset lives and residual values are reviewed annually. During the year borrowing costs of £5.0 million (2022 £1.3 million) have been capitalised on qualifying assets, at an average borrowing rate of 5.7% (2022 4.1%).

Groups of assets forming cash generating units are reviewed for indicators of impairment. No indicators of impairment were identified during the year.

Asset lives are reviewed annually. No significant changes were required in 2022/23.

17. Property, plant and equipment *continued*

The Group leases many assets as a lessee, across several categories of asset. Right-of-use assets held under leases included in property, plant and equipment above were:

	Land and buildings £m	Infrastructure assets £m	Operational properties £m	Fixed and mobile plant, vehicles and computers £m	Construction in progress £m	Total £m
Group						
Cost:						
At 1 April 2021	35.3	413.7	482.2	524.7	–	1,455.9
Additions	–	–	7.7	7.9	–	15.6
Acquisition of Bristol Water Group	0.5	0.1	–	1.7	–	2.3
Disposals	–	(14.1)	(114.3)	(152.6)	–	(281.0)
At 31 March 2022	35.8	399.7	375.6	381.7	–	1,192.8
Additions	0.1	19.3	0.5	20.9	–	40.8
Disposals	(0.5)	(35.1)	(41.0)	(13.6)	–	(90.2)
At 31 March 2023	35.4	383.9	335.1	389.0	–	1,143.4
Accumulated depreciation:						
At 31 March 2021	2.8	78.0	142.8	304.3	–	527.9
Charge / (credit) for year	1.3	5.1	8.0	23.4	–	37.8
Disposals	–	(3.5)	(48.1)	(143.2)	–	(194.8)
At 31 March 2022	4.1	79.6	102.7	184.5	–	370.9
Charge for year	1.2	4.9	6.0	20.7	–	32.8
Disposals	(0.2)	(14.7)	(18.1)	(13.4)	–	(46.4)
At 31 March 2023	5.1	69.8	90.6	191.8	–	357.3
Net book amount:						
At 31 March 2021	32.5	335.7	339.4	220.4	–	928.0
At 31 March 2022	31.7	320.1	272.9	197.2	–	821.9
At 31 March 2023	**30.3**	**314.1**	**244.5**	**197.2**	**–**	**786.1**

When the group enters into sale and leaseback arrangements, the accounting for the arrangement depends on whether the transaction meets the criteria within IFRS 15 for a sale to have occurred. If the sale criteria are met, the associated property, plant and equipment asset is derecognised, and a right-of-use asset is recognised at the proportion of the carrying value relating to the right retained. If the criteria for a sale under IFRS 15 have not been met the asset is not derecognised, but is reclassified to right-of-use assets (within property, plant and equipment). Right of use assets includes assets held under sale and leaseback arrangements with a carrying value of £785.2 million (2022 £793.7 million).

	Fixed and mobile plant, vehicles and computers £m
Company	
Cost:	
At 31 March 2021	0.3
At 31 March 2022	0.3
At 31 March 2023	0.3
Accumulated depreciation:	
At 31 March 2021	0.2
At 31 March 2022	0.2
At 31 March 2023	0.2
Net book value:	
At 31 March 2021	0.1
At 31 March 2022	0.1
At 31 March 2023	**0.1**

Asset lives and residual values are reviewed annually.

18. Financial instruments by category

The accounting policies for financial instruments that have been applied to line items are:

		Fair value		Amortised cost		
	Notes	Derivatives used for fair value hedging £m	Derivatives used for cash flow hedging £m	Debt instruments at amortised cost £m	Trade receivables and trade payables £m	Total £m
Group						
31 March 2023						
Financial assets						
Amounts owed by joint ventures	19	**–**	**–**	**9.3**	**–**	**9.3**
Trade receivables	22	**–**	**–**	**–**	**173.8**	**173.8**
Derivative financial instruments	23	**0.4**	**53.5**	**–**	**–**	**53.9**
Cash and cash deposits	25	**–**	**–**	**165.4**	**–**	**165.4**
Total		**0.4**	**53.5**	**174.7**	**173.8**	**402.4**
Financial liabilities						
Borrowings	28	**–**	**–**	**(3,130.8)**	**–**	**(3,130.8)**
Derivative financial instruments	23	**–**	**(4.8)**	**–**	**–**	**(4.8)**
Trade payables	26	**–**	**–**	**–**	**(150.7)**	**(150.7)**
Total		**–**	**(4.8)**	**(3,130.8)**	**(150.7)**	**(3,286.3)**
31 March 2022						
Financial assets						
Amounts owed by joint ventures	19	–	–	9.6	–	9.6
Trade receivables	22	–	–	–	180.9	180.9
Derivative financial instruments	23	1.2	19.2	–	–	20.4
Cash and cash deposits	25	–	–	519.0	–	519.0
Total		1.2	19.2	528.6	180.9	729.9
Financial liabilities						
Borrowings	28	–	–	(3,201.9)	–	(3,201.9)
Amounts owed by joint ventures	26	–	–	–	(1.8)	(1.8)
Trade payables	26	–	–	–	(107.5)	(107.5)
Total		–	–	(3,201.9)	(109.3)	(3,311.2)
Company						
31 March 2023						
Financial assets						
Amounts owed by subsidiaries	19,22	**–**	**–**	**101.8**	**–**	**101.8**
Other receivables	22	**–**	**–**	**3.4**	**–**	**3.4**
Derivative financial instruments	23	**0.4**	**0.7**	**–**	**–**	**1.1**
Cash and cash deposits	25	**–**	**–**	**104.1**	**–**	**104.1**
Total		**0.4**	**0.7**	**209.3**	**–**	**210.4**
Financial liabilities						
Borrowings	28	**–**	**–**	**(434.8)**	**–**	**(434.8)**
Trade payables	26	**–**	**–**	**–**	**(2.0)**	**(2.0)**
Total		**–**	**–**	**(434.8)**	**(2.0)**	**(436.8)**
31 March 2022						
Financial assets						
Amounts owed by subsidiaries	19, 22	–	–	79.7	–	79.7
Other receivables	22	–	–	0.7	–	0.7
Derivative financial instruments	23	1.2	0.4	–	–	1.6
Cash and cash deposits	25	–	–	306.7	–	306.7
Total		1.2	0.4	387.1	–	388.7
Financial liabilities						
Borrowings	28	–	–	(467.3)	–	(467.3)
Trade payables	26	–	–	–	(0.7)	(0.7)
Total		–	–	(467.3)	(0.7)	(468.0)

19. Other non-current assets

Non-current receivables

	Group		Company	
	2023 £m	2022 £m	**2023 £m**	2022 £m
Amounts owed by subsidiary undertakings	**–**	–	**26.1**	31.5
Amounts owed by related parties (note 42)	**9.3**	9.6	**–**	–
Interest receivable	**13.9**	–	**–**	–
	23.2	9.6	**26.1**	31.5

Non-current receivables were due:

	Group		Company	
	2023 £m	2022 £m	**2023 £m**	2022 £m
Between 1 and 2 years	**13.9**	9.6	**5.2**	5.2
Over 2 years and less than 5 years	**9.3**	–	**15.7**	15.6
Over 5 years	**–**	–	**5.2**	10.7
	23.2	9.6	**26.1**	31.5

The fair values of non-current receivables were:

	Group		Company	
	2023 £m	2022 £m	**2023 £m**	2022 £m
Amounts owed by subsidiary undertakings	**–**	–	**26.1**	31.5
Amounts owed by joint ventures	**9.3**	9.6	**–**	–
Interest receivable	**13.0**	–	**–**	–
	22.3	9.6	**26.1**	31.5

20. Investments

Subsidiary undertakings

	£m
Company	
At 31 March 2021	846.4
Investment in subsidiary undertakings:	
Bristol Water acquisition	419.6
South West Water share acquisition	45.0
Impairment of investment in subsidiary	(0.2)
At 31 March 2022	1,310.8
Investment in subsidiary undertakings:	
Bristol Water disposal	(407.5)
South West Water share acquisition	413.3
At 31 March 2023	**1,316.6**

The recoverable amount of investments is determined based on value-in-use calculations, which are set out in note 15.

During the year, as part of the statutory licence transfer of Bristol Water to South West Water, the Company transferred its shareholding in Bristol Water plc to South West Water Limited for £413 million. The consideration was satisfied through the Company subscribing for an additional £1 of share capital of South West Water Limited at a premium of £413 million.

In the year ended 31 March 2022, the Company subscribed to 45 million £1 ordinary shares in South West Water Limited at a cost £45 million.

Investment in associates and joint ventures

Name of entity	Principal activity	Place of business/country of incorporation	% of ownership	Measurement method
Water 2 Business Limited ("W2B")	National retailer in the non-household market and provides retail water services to non-household customers	England	30%	Equity
Bristol Wessex Billing Services Limited ("BWBSL")	Meter reading, billing, debt recovery and customer contact management services	England	50%	Equity
Searchlight Collection Limited	Debt collection services	England	50%	Equity

The carrying value of the Group's share of these investments in associates and joint ventures at 31 March 2022 and at 31 March 2023 is £0.3 million. The Group's share of the profits and other comprehensive income of these investments in associates and joint ventures for the year ended 31 March 2023 is £0.3 million (year ended 31 March 2022 nil).

20. Investments *continued*

The Group's joint ventures and associates are all private companies and there are no quoted market prices available for the shares. Summarised financial information for the joint ventures and investments in associates is set out below:

Summarised balance sheets

	2023 £m			2022 £m		
	W2B	**BWBSL**	**Searchlight**	W2B	BWBSL	Searchlight
Current						
Cash and cash equivalents	**1.5**	**1.3**	**–**	–	1.1	–
Other current assets	**60.1**	**2.2**	**0.1**	53.6	2.0	0.1
Total current assets	**61.6**	**3.5**	**0.1**	53.6	3.1	0.1
Non-current assets	**5.5**	**–**	**–**	6.5	–	–
Financial liabilities (excluding trade payables)	**–**	**–**	**–**	(1.1)	–	–
Current liabilities (including trade payables)	**(35.0)**	**(3.5)**	**–**	(28.0)	(3.1)	–
Total current liabilities	**(35.0)**	**(3.5)**	**–**	(29.1)	(3.1)	–
Non-current liabilities	**(31.1)**	**–**	**–**	(32.2)	–	–
Net assets	**1.0**	**–**	**0.1**	(1.2)	–	0.1

Summarised statement of comprehensive income

	2023 £m			2022 £m		
	W2B	**BWBSL**	**Searchlight**	W2B	BWBSL	Searchlight
Revenue	**232.9**	**17.5**	**0.3**	193.5	15.8	0.3
Cost of sales and other operating expenses	**(228.7)**	**(17.5)**	**(0.3)**	(190.9)	(15.8)	(0.3)
Interest	**(1.3)**	**–**	**–**	(0.7)	–	–
Pre-tax profit	**2.9**	**–**	**–**	1.9	–	–
Taxation charge	**(0.7)**	**–**	**–**	(0.6)	–	–
Total comprehensive income	**2.2**	**–**	**–**	1.3	–	–

The information above reflects the amounts presented in the financial statements of the associates (and not the Group's share of these amounts) adjusted for differences in accounting policies between the Group and associates. W2B's year-end date is 30 June. BWBSL's and Searchlight's year ends are 31 March. The Group's carrying amount of the investments held is £0.3m (2022 nil) which comprises 30% of the Group's share of equity of W2B. For BWBSL and Searchlight, the net equity is £nil (2022 £nil). The Group's share of profit from associated companies is £0.3m (2022 £nil) which comprises 30% of the Group's share of W2B, restricted by brought forward losses.

21. Inventories

	Group		Company	
	2023 £m	2022 £m	**2023 £m**	2022 £m
Raw materials and consumables	**10.0**	7.7	**–**	–

22. Trade and other receivables – current

	Group		Company	
	2023 £m	2022 £m	**2023 £m**	2022 £m
Trade receivables	**280.3**	296.2	**–**	–
Less: allowance for expected credit losses in respect of trade receivables	**(106.5)**	(100.4)	**–**	–
Net trade receivables	**173.8**	195.8	**–**	–
Amounts owed by parent undertaking	**–**	–	**–**	–
Amounts owed by subsidiary undertakings	**–**	–	**75.7**	48.2
Amounts owed by associated companies	**0.1**	–	**–**	–
Other receivables	**20.8**	41.1	**3.4**	0.7
Accrued income	**34.1**	26.4	**–**	0.1
Prepayments	**9.2**	7.6	**1.3**	0.8
	238.0	270.9	**80.4**	49.8

Trade receivables include accrued income relating to customers with water budget payment plans. Trade receivables have decreased year on year, largely due to the one-off bill reductions in the final quarter of the year in relation to Watershare+ and the drought incentive (see note 6) along with tariff reductions in the South West Water region.

Accrued income includes £25.7 million (2022 £22.0 million) in respect of metered accrual revenue in the retail water business. Metered accrual revenue relates to performance obligations that have been fully extinguished in providing services to customers prior to the reporting date. Payment in respect of these services is a matter of time following issuance of invoices.

The Directors consider that the carrying amounts of trade and other receivables approximate to their fair value.

22. Trade and other receivables – current *continued*

There is no concentration of credit risk in trade receivables. The Group has a large number of customers who are dispersed and there is no significant loss on trade receivables expected that has not been provided for.

The Group applies the simplified approach in calculating the expected credit losses for trade receivables allowing a provision matrix to be used which is based on the expected life of trade receivables, default rates for different customer categories within the collection process and forward-looking information.

As at 31 March, an analysis of the ageing of trade receivables is as follows:

	2023 £m	2022 £m
Group		
Not due	**57.5**	68.9
Past due 1 – 30 days	**14.7**	17.4
Past due 31 – 120 days	**17.1**	20.2
More than 120 days	**191.0**	189.7
	280.3	296.2

The aged trade receivables above are taken directly from aged sales ledger records.

The Group's operating businesses specifically review separate categories of debt to identify an appropriate allowance for expected credit losses as outlined in note 2 (n) ii). South West Water Limited has a duty under legislation to continue to provide domestic customers with services regardless of payment. Given the different nature of customer demographics within South West Water's operating area and the non-household retail business of Pennon Water Services, different provision matrices are adopted by each business. The provision matrix adopted for household customers in the most significant operating region of Devon and Cornwall is outlined in the table below, showing the range of provision rates dependent on phase of collection. The table also includes the gross debt and provision rates for other customer areas:

	Trade receivables 2023 £m	**Allowance for expected credit losses 2023 £m**
Devon and Cornwall (household customers)		
• Current occupier < 12 months: 1% - 30%	**35.3**	0.2
• Current occupier 12 – 24 months: 10% – 60%	**14.6**	2.8
• Current occupier 24 – 36 months: 15% – 80%	**10.8**	3.4
• Current occupier > 36 months: 20% – 100%	**90.4**	49.5
• Previous occupier: 55% – 100%	**51.9**	31.3
Bristol	**31.0**	5.4
Pennon Water Services	**38.3**	13.5
Other	**8.0**	0.4
	280.3	106.5

No material expected credit loss provision has been recognised in respect of amounts owed by subsidiary undertakings.

The movement in the allowance for expected credit losses in respect of trade receivables was:

	2023 £m	2022 £m
At 1 April	**100.4**	102.3
Provision for expected credit losses	**7.8**	5.5
Receivables written off during the year as uncollectable	**(1.7)**	(7.4)
At 31 March	**106.5**	100.4

23. Derivative financial instruments

	Group		Company	
	2023 £m	2022 £m	**2023 £m**	2022 £m
Derivatives used for cash flow hedging				
Non-current assets	**32.9**	14.1	**0.2**	0.3
Current assets	**20.6**	5.1	**0.5**	0.1
Current liabilities	**(2.4)**	–	**–**	–
Non-current liabilities	**(2.4)**	–	**–**	–
Derivatives used for fair value hedging				
Non-current assets	**0.3**	0.7	**0.3**	0.7
Current assets	**0.1**	0.5	**0.1**	0.5

The Group's financial risks and risk management policies are set out in note 3. The fair value of derivatives is split between current and non-current assets or liabilities based on the maturity of the cash flows. The ineffective portion recognised in the income statement arising from hedging relationships was £nil (2022 £nil).

23. Derivative financial instruments *continued*

During the year a £5.0 million charge (2022 £5.8 million charge) was recognised in profit and loss relating to cash flow hedges previously recognised through other comprehensive income and recorded in the hedging reserve. A £29.1 million credit (2022 £40.6 million credit) was recognised in other comprehensive income for cash flow hedges that may be classified subsequently to profit and loss.

Interest rate swaps, primarily cash flow hedges, and fixed rate borrowings are used to manage the mix of fixed and floating rates to ensure at least 60% of Group net borrowings are at fixed rate.

At 31 March 2023 the Group had interest rate swaps to swap from floating to fixed rate and hedged financial liabilities with a notional value of £853 million and a weighted average maturity of 3.4 years (2022 £718 million, with 3.5 years). The weighted average interest rate of the swaps for their nominal amount was 1.54% (2022 1.14%).

The Group has established a hedge ratio of 1:1 for the hedging relationships as the underlying risks of the swaps are identical to the hedged risk components. To test the hedge effectiveness, the Group uses the hypothetical derivative method and compares the changes in the fair value of the hedging instrument against the changes in fair value of the hedged item attributable to the hedged risk.

The hedge ineffectiveness can arise from:

- Different interest rate curve applied to discount the hedged item and hedging instrument
- Differences in timing of cash flows of the hedged item and hedging instrument
- The counterparties' credit risk differently impacting the fair value movements of the hedging instrument and hedged item

The impact of the hedging instrument on the statement of financial position is as follows:

Group	Notional amount £m	Carrying amount £m	Line item in the statement of financial position	Change in fair value used for measuring ineffectiveness in the period £m
As at 31 March 2023				
Interest rate swaps	853.4	52.4	Derivative financial instruments	33.6
RPI swaps	300.0	(4.4)	Derivative financial instruments	(4.4)
Cross currency swaps	24.0	1.1	Derivative financial instruments	(0.5)
As at 31 March 2022				
Interest rate swaps	717.9	18.8	Derivative financial instruments	40.6
Cross currency swaps	24.0	1.6	Derivative financial instruments	1.5

Company	Notional amount £m	Carrying amount £m	Line item in the statement of financial position	Change in fair value used for measuring ineffectiveness in the period £m
As at 31 March 2023				
Cross currency swaps	24.0	1.1	Derivative financial instruments	(0.5)
As at 31 March 2022				
Cross currency swaps	24.0	1.6	Derivative financial instruments	1.5

The periods for which the cash flow hedges are expected to affect future profit or loss are as follows:

	Due within 1 year £m	**Due between 1 and 2 years £m**	**Due between 2 and 5 years £m**	**Due over 5 years £m**	**Total £m**
Group					
31 March 2023					
Assets	**20.8**	**19.0**	**8.8**	**5.3**	**53.9**
Liabilities	**(2.4)**	**(2.0)**	**(0.2)**	**(0.2)**	**(4.8)**
31 March 2022					
Assets	5.1	5.0	7.0	2.1	19.2
Company					
31 March 2023					
Assets	**0.5**	**0.2**	**–**	**–**	**0.7**
Liabilities	**–**	**–**	**–**	**–**	**–**
31 March 2022					
Assets	0.1	0.2	0.1	–	0.4

Valuation hierarchy

The Group uses the following hierarchy for determining the fair value of financial instruments by valuation technique:

- Quoted prices (unadjusted) in active markets for identical assets or liabilities (level 1)
- Inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices) (level 2)
- Inputs for the asset or liability that are not based on observable market data (that is, unobservable inputs) (level 3).

23. Derivative financial instruments *continued*

The fair value of financial instruments not traded in an active market (level 2, for example over-the-counter derivatives) is determined by using valuation techniques. A variety of methods and assumptions are used based on market conditions existing at each balance sheet date. Quoted market prices or dealer quotes for similar instruments are used for long-term debt. Other techniques, such as estimated discounted cash flows, are used to determine fair value for the remaining financial instruments. The fair value of interest rate swaps is calculated as the present value of the estimated future cash flows.

The Group's financial derivatives are valued using level 2 measures:

	Group		Company	
	2023 £m	2022 £m	**2023 £m**	2022 £m
Assets				
Derivatives used for cash flow hedging	**53.5**	19.2	**0.7**	0.4
Derivatives used for fair value hedging	**0.4**	1.2	**0.4**	1.2
Total assets	**53.9**	20.4	**1.1**	1.6
Liabilities				
Derivatives used for cash flow hedging	**(4.8)**	–	**–**	–
Total liabilities	**(4.8)**	–	**–**	–

24. Financial instruments at fair value through profit

	Group		Company	
	2023 £m	2022 £m	**2023 £m**	2022 £m
Current liabilities	**2.6**	2.5	**0.1**	0.1
Non-current liabilities	**34.0**	36.1	**–**	–
Non-current assets	**1.3**	–	**1.3**	–

Financial instruments at fair value through profit reflect the fair value movement of the hedged risk on the hedged item which had been designated in a fair value hedging relationship.

The hedged item was the £150 million bond issued by South West Water Finance Plc in 2010 which matures in July 2040 (see note 28). The hedging relationship was de-designated in previous periods at which point the fair value amount recognised at that point ceased to be revalued. The fixed financial liability at the point of de-designation is released to the income statement over the remaining life of the debt.

25. Cash and cash deposits

	Group		Company	
	2023 £m	2022 £m	**2023 £m**	2022 £m
Cash at bank and in hand	**69.7**	57.3	**34.0**	6.7
Short-term bank deposits	**25.0**	50.0	**25.0**	50.0
Other deposits	**70.7**	411.7	**45.1**	250.0
Total cash and cash deposits	**165.4**	519.0	**104.1**	306.7

Group short-term deposits have an average maturity of one working day (2022 one working day).

Group other deposits have an average maturity of 45 days (2022 78 days).

Group other deposits include restricted funds of £21.7 million (2022 £161.7 million) to settle long-term lease liabilities (note 28) and £nil (2022 £6.1 million) held in an instant access account under the terms of other loan agreements. Restricted funds are available for access, subject to being replaced by an equivalent valued security.

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

	Group		Company	
	2023 £m	2022 £m	**2023 £m**	2022 £m
Cash and cash deposits as above	**165.4**	519.0	**104.1**	306.7
Less: deposits with a maturity of three months or more (restricted funds)	**(21.7)**	(167.8)	**–**	–
	143.7	351.2	**104.1**	306.7

26. Trade and other payables – current

	Group		Company	
	2023 £m	2022 £m	**2023 £m**	2022 £m
Trade payables	**150.7**	107.5	**2.0**	0.7
Contract liabilities	**3.7**	3.3	**–**	–
Other tax and social security	**3.4**	4.3	**0.4**	0.8
Accruals	**44.3**	29.5	**2.3**	2.1
Other payables	**23.3**	25.1	**1.6**	2.0
Amounts owed to joint venture	**–**	1.8	**–**	–
	225.4	171.5	**6.3**	5.6

The Directors consider that the carrying amount of trade and other payables approximates to their fair value.

26. Trade and other payables – current *continued*

The movement in the contract liabilities was:

Contract liabilities	Group 2023 £m	Group 2022 £m
At 1 April	**140.5**	130.3
Revenue recognised in the year	**(6.4)**	(2.0)
Consideration received in advance of completion of performance obligations	**24.9**	12.2
At 31 March	**159.0**	140.5

The analysis of contract liabilities between current and non-current is:

	Group 2023 £m	Group 2022 £m
Current	**3.7**	3.3
Non-current (note 29)	**155.3**	137.2
	159.0	140.5

Performance obligations related to the current contract liabilities balance above are expected to be satisfied, and revenue will be recognised, within the financial year ended 31 March 2024.

27. Current tax assets/(liabilities)

	Group 2023 £m	Group 2022 £m	Company 2023 £m	Company 2022 £m
Current year debtor / (creditor)	**3.1**	2.8	**(0.2)**	(0.2)
Prior year tax items	**5.3**	(1.3)	**(3.2)**	(3.2)
	8.4	1.5	**(3.4)**	(3.4)

28. Borrowings

	Group 2023 £m	Group 2022 £m	Company 2023 £m	Company 2022 £m
Current				
Bank and other loans	**92.7**	40.0	**–**	–
Private placements	**–**	30.0	**–**	30.0
Amounts owed to subsidiary undertakings	**–**	–	**279.1**	282.8
	92.7	70.0	**279.1**	312.8
Leases	**32.0**	170.2	**–**	–
Total current borrowings	**124.7**	240.2	**279.1**	312.8
Non-current				
Bank and other loans	**697.0**	641.9	**49.8**	49.9
Private placements	**305.3**	279.3	**105.9**	104.6
Fixed rate bonds	**214.6**	213.2	**–**	–
RPI index-linked bonds	**744.0**	773.0	**–**	–
Listed preference shares	**12.5**	12.5	**–**	–
	1,973.4	1,919.9	**155.7**	154.5
Leases	**1,032.7**	1,041.8	**–**	–
Total non-current borrowings	**3,006.1**	2,961.7	**155.7**	154.5
Total borrowings	**3,130.8**	3,201.9	**434.8**	467.3

South West Water Finance Plc issued a £150 million fixed rate bond in July 2010 maturing in 2040 with a cash coupon of 5.875%.

South West Water Finance Plc issued a £200 million RPI index-linked bond in July 2008 maturing in 2057 with a cash coupon of 1.99%. Bournemouth Water Limited issued a £65 million RPI index-linked bond in April 2005 maturing in 2033 with a cash coupon of 3.084%. This instrument was transferred to South West Water Limited in April 2017. Prior to acquisition by Pennon, Bristol Water Plc issued RPI index-linked bonds totalling £91 million maturing in 2032 with a cash coupon of 3.635%.

In November 2022 Bristol Water plc redeemed £40m of bonds due to be repaid in March 2041 at a value of £72.3 million. The Group carrying value of the bonds at redemption was £91.7 million and costs were incurred of £1.0m, resulting in a net gain on settlement of £18.4 million.

Fair value adjustments of £124 million (2022 £169 million) in relation to the acquisition of Bournemouth Water Limited and Bristol Water Plc have been allocated to the instruments to which they relate.

28. Borrowings *continued*

The listed preference shares were issued by Bristol Water Plc at £1 in 1992. They are held by external shareholders and are listed on the London Stock Exchange. Shareholders are entitled to receive dividends at 8.75% per annum on the par value of the shares on a cumulative basis; these dividends are payable half yearly on 1 April and 1 October. On winding up, the preference shareholders rank ahead of Bristol Water ordinary shareholders and are entitled to receive £1 per share and any dividends accrued but unpaid in respect of their shares. In the event that dividends on the preference shares are in arrears for six months or more, holders of the preference shares become entitled to vote at general meetings of members. The authorised preference share capital consists of 14,000,000 8.75% irredeemable cumulative preference shares of £1 each. The preference shares are classified as liabilities in the consolidated balance sheet of the Group and the related dividends are classified as finance costs.

The fair values of borrowings, are valued using level 2 measures, unless otherwise stated below, (as set out in note 23) were:

	2023		2022	
	Book value £m	**Fair value £m**	Book value £m	Fair value £m
Group				
Bank and other loans	**92.7**	**92.7**	40.0	40.0
Private placement	**–**	**–**	30.0	30.0
	92.7	**92.7**	70.0	70.0
Leases	**32.0**	**–**	170.2	–
Total current borrowings	**124.7**	**92.7**	240.2	70.0
Group				
Bank and other loans	**697.0**	**684.1**	641.9	650.5
Private placements	**305.3**	**288.2**	279.3	272.0
Fixed rate bonds (level 1)	**135.8**	**137.8**	135.3	181.5
Fixed rate bonds	**78.8**	**66.8**	77.9	75.2
RPI index-linked bond	**744.0**	**614.5**	773.0	885.9
Listed preference shares	**12.5**	**21.5**	12.5	24.9
	1,973.4	**1,812.9**	1,919.9	2,090.0
Leases	**1,032.7**	**–**	1,041.8	–
Total non-current borrowings	**3,006.1**	**1,812.9**	2,961.7	2,090.0
Total borrowings	**3,130.8**	**1,905.6**	3,201.9	2,160.0
Company				
Private placements	**–**	**–**	30.0	30.0
Amounts owed to subsidiary undertakings	**279.1**	**279.1**	282.8	282.8
Total current borrowings	**279.1**	**279.1**	312.8	312.8
Bank and other loans	**49.8**	**50.4**	49.9	51.8
Private placements	**105.9**	**105.7**	104.6	105.1
Total non-current borrowings	**155.7**	**156.1**	154.5	156.9
Total borrowings	**434.8**	**435.2**	467.3	469.7

Under IFRS 16 the disclosure of the fair value of leases is not required.

Where market values are not available, fair values of borrowings have been calculated by discounting expected future cash flows at prevailing interest rates.

During the year, as part of its ongoing programme to renew and raise new financing, the Group entered into £200 million of new terms loans and leasing facility arrangements, with an average maturity of 9 years, a £25 million private placement and £195 million of new and renewed revolving credit facilities.

The maturity of non-current borrowings, excluding leases, was:

	Group		Company	
	2023 £m	2022 £m	**2023 £m**	2022 £m
Between 1 and 2 years	**64.4**	101.4	**8.7**	–
Over 2 years and less than 5 years	**364.2**	221.0	**147.0**	75.1
Over 5 years	**1,544.8**	1,597.5	**–**	79.4
	1,973.4	1,919.9	**155.7**	154.5

The weighted average maturity of non-current borrowings, excluding leases, was 13.2 years (2022 14.2 years).

Undrawn committed borrowing facilities at the balance sheet date were:

	Group		Company	
	2023 £m	2022 £m	**2023 £m**	2022 £m
Floating rate:				
Expiring within 1 year	**119.8**	50.0	**80.0**	25.0
Expiring after 1 year	**135.0**	247.0	**25.0**	80.0
	254.8	297.0	**105.0**	105.0

28. Borrowings *continued*

Information on leases

The Group has leases for various assets as shown in note 17.

The maturity of lease liabilities was:

	Group		Company	
	2023 £m	2022 £m	**2023 £m**	2022 £m
Within 1 year	**32.0**	170.1	**–**	–
Over 1 year and less than 5 years	**181.7**	180.6	**–**	–
Over 5 years	**851.0**	861.2	**–**	–
	1,064.7	1,211.9	**–**	–

Analysed as:

	Group		Company	
	2023 £m	2022 £m	**2023 £m**	2022 £m
Current	**32.0**	170.1	**–**	–
Non-current	**1,032.7**	1,041.8	**–**	–
	1,064.7	1,211.9	**–**	–

For the purposes of calculating debt or borrowings under the Group's financing agreements, all of which were negotiated under IFRS prior to the implementation of IFRS 16, borrowings that were previously categorised as operating leases under IAS 17 are excluded from the definition of debt. As at 31 March 2023 the carrying value of leases previously categorised as IAS 17 operating leases was £37.3 million (2022 £36.9 million).

The Group does not face a significant liquidity risk with regard to its lease liabilities. Lease liabilities are monitored within the Group's treasury function.

The discount rate used to calculate the lease liabilities above involves estimation. Where the Group cannot readily determine the rate implicit in the lease the Group uses an estimated incremental borrowing rate (IBR). At 31 March 2023 the range of IBRs used was between 2.6% and 3.9% (2022 between 2.6% and 3.9%) and the weighted average IBR across all leases was 3.3% (2021 3.8%). If the weighted average rate used increased or decreased by 10bps, this would result in a c.1.1% increase or reduction in the present value of lease liabilities recognised at 31 March 2023 (2022 c.1.1%).

The period for repayment of certain leases includes an agreement to deposit with the lessor group amounts equal to the difference between the original and revised payments due. The accumulated deposits, £21.6 million at 31 March 2023 (2022 £161.7 million), are currently being held to settle the lease liability subject to rights to release by negotiation with the lessor. The deposits are subject to a registered charge given as security to the lessor for the balance outstanding.

Cash outflows in respect of leasing relate to principal repayments of £120.3 million (2022 £231.4 million) and interest repayments of £100.5 million (2022 £17.2 million), in addition to inflows from lease financing arrangements of £40.2 million (2022 £15.0 million).

Other information required to be disclosed under IFRS 16 is included in note 17.

29. Other non-current liabilities

	Group		Company	
	2023 £m	2022 £m	**2023 £m**	2022 £m
Amounts owed to subsidiary undertakings	**–**	–	**8.5**	8.6
Contract liabilities	**155.3**	137.2	**–**	–
	155.3	137.2	**8.5**	8.6

Non-current contract liabilities relate to consideration received in advance of the Group performing its performance obligations to customers where performance obligations will not be completed within 12 months of the balance sheet date. The overall movement in total contract liabilities is disclosed in note 26. Contract liabilities reflect the fair value of assets transferred from customers in the water segment. The majority of the contract liabilities included above are expected to unwind after five years.

30. Retirement benefit obligations

During the year the Group operated a number of defined benefit pension schemes and also defined contribution schemes. The principal plan within the Group is the Pennon Group Pension Scheme (PGPS), which is a funded defined benefit, final salary pension scheme in the UK. Following the acquisition of Bristol Water, the Group also assumed defined benefit obligations through Bristol Water's membership of Water Companies Pension Scheme ('WCPS').

The Group's pension schemes are established under trust law and comply with all relevant UK legislation. The assets of the Group's pension schemes are held in separate trustee administered funds. The trustees of the funds are required to act in the best interest of the funds' beneficiaries. The appointment of schemes' trustees is determined by the schemes' trust documentation. The Group has a policy for the PGPS that one-half of all trustees, other than the Chair, are nominated by members of the schemes, including pensioners.

Bristol Water's membership of WCPS is through a separate section of that scheme. The assets of the section are held separately from those of the Group and are invested by discretionary fund managers appointed by the trustees of the scheme. The employees in the section ceased to earn additional defined benefit pensions on 31 March 2016. There were no employer contributions to the scheme from that date and from 30 June 2016, with the agreement of the trustees, deficit contributions also ceased. All eligible employees were offered membership of a stakeholder pension scheme.

In 2018 the trustees of the Bristol Water section of the WCPS purchased a bulk annuity policy to insure the benefits for members of the section. Following this the method for valuing the liabilities of the pension scheme has remained the same. However, the scheme assets, in the form of the insurance policy, now materially match the value of the liabilities. The process to buy up and wind up the scheme is continuing, including discussions regarding the release of the surplus on completion of this process.

PGPS is closed to future accrual.

30. Retirement benefit obligations *continued*

Defined contribution schemes

Pension costs for defined contribution schemes were £9.4 million (2022 £7.6 million).

Defined benefit schemes

Assumptions

The principal actuarial assumptions at 31 March were:

	2023 %	2022 %
Rate of increase in pensionable pay	**2.7**	3.0
Rate of increase for current and future pensions	**2.8**	3.1
Rate used to discount schemes' liabilities and expected return on schemes' assets	**4.7**	2.8
Inflation	**3.3**	3.6

Mortality

Assumptions regarding future mortality experience are set based on actuarial advice in accordance with published statistics and experience. The mortality assumption uses a scheme-specific calculation based on CMI 2019 actuarial tables with an allowance for future longevity improvement.

The average life expectancy in years of a member having retired at age 62 on the balance sheet date is projected as:

	2023	2022
Male	**24.2**	24.9
Female	**26.7**	27.2

The average life expectancy in years of a future pensioner retiring at age 62, 20 years after the balance sheet date, is projected as:

	2023	2022
Male	**25.6**	26.0
Female	**28.2**	28.3

The sensitivities regarding the principal assumptions used to measure the schemes' liabilities are:

	Change in assumption	Impact on schemes' liabilities
Rate of increase in current and future pensions	+/– 0.5%	+/– 4.3%
Rate used to discount schemes' liabilities	+/– 0.5%	–/+ 6.5%
Inflation	+/– 0.5%	+/– 5.0%
Life expectancy	+/– 1 year	+/– 3.7%

The sensitivity analysis shows the effect of changes in the principal assumptions used for the measurement of the pension liability. The method used to calculate the sensitivities is approximate and has been determined taking into account the duration of the liabilities and the overall profile of each scheme's membership. This is the same approach as has been adopted in previous years.

The amounts recognised in the balance sheet were:

	Group		Company	
	2023 £m	2022 £m	**2023 £m**	2022 £m
Present value of financial obligations	**(719.5)**	(985.9)	**(139.5)**	(190.7)
Fair value of plan assets	**753.2**	1,056.5	**144.2**	203.1
Surplus/(deficit) of funded plans	**33.7**	70.6	**4.7**	12.4
Less: restriction of surplus	**(4.4)**	(4.3)	**–**	–
Net asset/(liability) recognised in the balance sheet	**29.3**	66.3	**4.7**	12.4

30. Retirement benefit obligations *continued*

The movement in the net defined benefit obligation over the accounting period is as follows:

	2023			2022		
	Present value of obligation £m	**Fair value of plan assets £m**	**Total £m**	Present value of obligation £m	Fair value of plan assets £m	Total £m
At 1 April	**(985.9)**	**1,052.2**	**66.3**	(901.7)	910.5	8.8
Acquisition Bristol Water Group	**–**	**–**	**–**	(175.4)	183.2	7.8
Current service cost	**(1.0)**	**(0.6)**	**(1.6)**	(2.9)	(0.6)	(3.5)
Past service cost, curtailments and gains/losses on settlements	**–**	**–**	**–**	(0.1)	–	(0.1)
Interest (expense)/income	**(26.5)**	**28.5**	**2.0**	(20.8)	21.4	0.6
	(27.5)	**27.9**	**0.4**	(23.8)	20.8	(3.0)
Remeasurements:						
Loss on plan assets excluding amounts included in interest expense	**–**	**(288.7)**	**(288.7)**	–	(33.1)	(33.1)
Gain/(loss) from change in demographic assumptions	**9.7**	**–**	**9.7**	(0.7)	–	(0.7)
Gain from change in financial assumptions	**266.0**	**–**	**266.0**	80.4	–	80.4
Experience (losses)/gains	**(25.9)**	**(0.1)**	**(26.0)**	(22.2)	0.5	(21.7)
	249.8	**(288.8)**	**(39.0)**	57.5	(32.6)	24.9
Contributions:						
Employers	**–**	**1.6**	**1.6**	–	27.8	27.8
Payments from plans:	**–**	**–**	**–**			
Benefit payments	**44.1**	**(44.1)**	**–**	57.5	(57.5)	–
	44.1	**(42.5)**	**1.6**	57.5	(29.7)	27.8
At 31 March	**(719.5)**	**748.8**	**29.3**	(985.9)	1,052.2	66.3

Recognition of surplus on principal pension scheme

In accordance with IAS 19 'Employee Benefits' the value of the net pension scheme surplus that can be recognised in the statement of financial position is restricted to the present value of economic benefits available in the form of refunds from the scheme or reductions in future contributions. In respect of the Group's principal pension scheme, PGPS, the surplus has been recognised as the Group believes that ultimately it has an unconditional right to a refund of any surplus assuming the full settlement of the plan's liabilities in a single event, such as a scheme wind up.

Bristol Water

The Group believes that it has an unconditional right to a refund of surplus and that the gross pension surplus can be recognised. This benefit is only available as a refund as no additional defined pension benefits are being earned. Under UK tax legislation a tax deduction of 35% is applied to a refund from a UK pension scheme, before it is passed to the employer. This tax deduction has been applied to restrict the value of the surplus recognised for this scheme.

The movement in the Company's net defined benefit obligation over the accounting period is as follows:

	2023			2022		
	Present value of obligation £m	**Fair value of plan assets £m**	**Total £m**	Present value of obligation £m	Fair value of plan assets £m	Total £m
At 1 April	**(190.7)**	**203.1**	**12.4**	(205.7)	200.2	(5.5)
Current service cost	**(0.4)**	**–**	**(0.4)**	(0.4)	–	(0.4)
Past service cost and gains and losses on settlements	**–**	**–**	**–**	–	–	–
Interest (expense)/income	**(5.2)**	**5.6**	**0.4**	(4.2)	4.2	–
	(5.6)	**5.6**	**–**	(4.6)	4.2	(0.4)
Remeasurements:						
Loss on plan assets excluding amounts included in interest expense	**–**	**(56.4)**	**(56.4)**	–	(13.7)	(13.7)
Loss from change in demographic assumptions	**2.0**	**–**	**2.0**	–	–	–
Gain/(loss) from change in financial assumptions	**52.6**	**–**	**52.6**	12.3	–	12.3
Experience losses	**(6.2)**	**–**	**(6.2)**	(4.6)	–	(4.6)
	48.4	**(56.4)**	**(8.0)**	7.7	(13.7)	(6.0)
Contributions:						
Employers	**–**	**0.3**	**0.3**	–	24.3	24.3
Payments from plans:						
Benefit payments	**8.4**	**(8.4)**	**–**	11.9	(11.9)	–
	8.4	**(8.1)**	**0.3**	11.9	12.4	24.3
At 31 March	**(139.5)**	**144.2**	**4.7**	(190.7)	203.1	12.4

30. Retirement benefit obligations *continued*

The schemes' assets relating to the Group were:

	2023			2022		
	Quoted prices in active market £m	**Prices not quoted in active market £m**	**Fund %**	Quoted prices in active market £m	Prices not quoted in active market £m	Fund %
Equities	**124.3**	**–**	**17**	219.0	–	21
Government bonds	**14.4**	**–**	**2**	96.1	–	9
Other bonds	**175.8**	**72.1**	**33**	270.1	79.3	33
Diversified growth	**43.9**	**–**	**6**	67.8	–	6
Property/Infrastructure	**19.0**	**22.4**	**5**	69.6	11.4	8
Insurance linked security	**41.2**	**107.0**	**20**	78.2	147.8	22
LDI investments	**109.2**	**–**	**14**	–	–	–
Other (including cash funds)	**6.3**	**13.2**	**3**	3.9	9.0	1
	534.1	**214.7**	**100**	804.7	247.5	100

The Company's share of the schemes' assets at the balance sheet date was:

	2023			2022		
	Quoted prices in active market £m	**Prices not quoted in active market £m**	**Fund %**	Quoted prices in active market £m	Prices not quoted in active market £m	Fund %
Equities	**28.5**	**–**	**20**	49.7	–	24
Government bonds	**3.3**	**–**	**2**	21.8	–	11
Other bonds	**40.3**	**16.5**	**39**	61.3	18.0	39
Diversified growth	**10.1**	**–**	**7**	15.4	–	8
Property/Infrastructure	**4.4**	**5.2**	**7**	15.8	2.6	9
Insurance linked security	**9.5**	**–**	**7**	17.7	–	9
LDI investments	**25.1**	**–**	**17**	–	–	–
Other	**1.4**	**–**	**1**	0.8	–	–
	122.6	**21.7**	**100**	182.5	20.6	100

Through its defined benefit pension plan, the Group is exposed to a number of risks, the most significant of which are detailed below:

Asset volatility	The liabilities are calculated using a discount rate set with reference to corporate bond yields; if assets underperform this yield, this will create a deficit. The schemes hold a proportion of growth assets (equities and diversified growth funds) which are expected to outperform corporate bonds in the long term, but can give rise to volatility and risk in the short term. As the funding of the schemes improves, an increasing proportion of the schemes' assets are invested in less volatile asset classes such as cash and bonds which more closely reflect market movements in the schemes' liabilities. The allocation to growth assets is monitored such that it is suitable with the schemes' long-term objectives.
Changes in bond yields	A decrease in corporate bond yields will increase the schemes' liabilities, although this will be partially offset by an increase in the value of the schemes' bond holdings.
Inflation risk	The majority of the schemes' benefit obligations are linked to inflation, and higher inflation will lead to higher liabilities (although, in most cases, caps on the level of inflationary increases are in place to protect against extreme inflation). The scheme uses LDIs ('Liability Driven Investment Funds') within the asset portfolios to hedge against the value of liabilities changing as a result of movements in long-term interest rates and inflation expectations. The structure allows the scheme to both hedge against the risks and retain capital investment in assets that are expected to generate higher returns. Whilst LDIs are an integral part of the hedging strategy, risk management and monitoring strategies are in place to ensure that the collateral requirements to maintain these structures are closely managed.
Life expectancy	The majority of the schemes' obligations are to provide benefits for the life of the member, so increases in life expectancy will result in an increase in the liabilities.

In conjunction with its investment advisers, the trustees have structured the schemes' investments with the objective of balancing investment returns and levels of risk. The asset allocation for the main scheme has three principal elements:

- Holding of cash funds and bonds which are expected to be less volatile than most other asset classes and reflects market movements in the schemes' liabilities
- A proportion of equities with fund managers having freedom in making investment decisions to maximise returns, and
- Investment of a proportion of the schemes' assets in alternative asset classes which give the potential for diversification (currently property, insurance linked securities and diversified growth).

The liabilities of the defined benefit schemes are measured by using the projected unit credit method which is an accrued benefits valuation method in which the scheme liabilities make allowance for projected increases in pensionable pay.

30. Retirement benefit obligations *continued*

As funding of our principal pension scheme has improved the investment portfolio has been de-risked through increasing the scheme's real gilts hedging position through LDIs (Liability Driven Investments), which are commonly used by UK pension schemes. As has been widely reported, the unprecedented increases in gilt yields in late September 2022 resulted in rapid reductions in collateral in LDI arrangements which schemes are required to increase or the hedging structure is unwound. As permitted by the scheme rules and legislation, Pennon approved a temporary loan facility on 28 September 2022 to provide short-term liquidity to the scheme whilst investments were re-balanced. £25 million was provided on this date and this was fully repaid within 6 days. This loan facility remains undrawn and available for use.

The future cash flows arising from the payment of the defined benefits are expected to be settled primarily in the period between 15 and 40 years from the balance sheet date.

The 2022 triennial actuarial valuation of the principal defined benefit scheme was agreed in 2023 with an actuarial valuation surplus of £8.0 million. No deficit recovery contributions are required as a result of the 2022 valuation. Additional contributions of £1.6 million were paid into the scheme in respect of scheme expenses (2022: £23 million including use of proceeds from the Viridor disposal). The Group monitors funding levels on an annual basis and the Group expects to pay only scheme expenses of around £1.7 million, during the year ended 31 March 2024.

The last formal actuarial valuation of the Bristol Water section of the WCPS was at 31 March 2017.

31. Deferred tax

Deferred tax is provided in full on temporary differences under the liability method using enacted tax rates.

Movements on deferred tax were:

	Group		Company	
	2023 £m	2022 £m	**2023 £m**	2022 £m
Liabilities/(assets) at 1 April	**512.4**	259.6	**(13.1)**	(12.5)
Acquisition of Bristol Water Group	**–**	140.3	**–**	–
(Credited)/charged to the income statement	**(0.9)**	8.9	**(2.4)**	3.1
Charged/(credited) to equity, including impact of change in tax rate	**(2.0)**	4.1	**(1.8)**	(3.5)
Other non-underlying charges/(credits) in the income statement	**(2.5)**	99.5	**(1.3)**	(0.2)
Liabilities/(assets) at 31 March	**507.0**	512.4	**(18.6)**	(13.1)

An adjustment to the preliminary accounting for the Bristol Water acquisition has been made within the measurement period ending 2 June 2022, this adjustment is presented retrospectively and the 31 March 2022 balance sheet figures for deferred tax have been adjusted accordingly (see note 4).

Deferred tax assets have been recognised in respect of all temporary differences giving rise to deferred tax assets because it is probable that these assets will be recovered.

The majority of the Group's deferred tax liability is expected to be recovered over more than one year. The majority of the Company's deferred tax asset is expected to be recovered over more than one year. All deferred tax assets and liabilities within the same jurisdiction are offset.

The movements in deferred tax assets and liabilities were:

Group

Deferred tax liabilities

	Derivatives £m	Accelerated tax depreciation £m	Fair value adjustments £m	Short-term liabilities including provisions £m	Retirement benefit obligations £m	Total £m
At 1 April 2021	–	276.3	17.0	–	–	293.3
Acquisition of Bristol Water Group	–	92.2	74.3	(12.5)	–	154.0
Charged/(credited) to the income statement	–	2.6	(0.9)	–	–	1.7
Non-underlying charge to the income statement	–	88.5	5.3	–	–	93.8
Reclassification from deferred tax assets	–	–	–	18.6	9.7	28.3
At 31 March 2022	–	459.6	95.7	6.1	9.7	571.1
Charged/(credited) to the income statement	–	13.6	(1.2)	(4.6)	3.0	10.8
Non-underlying credit to the income statement	–	–	–	–	–	–
Charged/(credited) to equity	–	–	–	–	(9.8)	(9.8)
Reclassification	2.9	–	–	–	–	2.9
At 31 March 2023	**2.9**	**473.2**	**94.5**	**1.5**	**2.9**	**575.0**

31. Deferred tax *continued*

Deferred tax assets

	Derivatives £m	Share-based payments £m	Tax losses £m	Fair value adjustment £m	Short-term liabilities including provisions £m	Retirement benefit obligations £m	Total £m
At 1 April 2021	(12.0)	(1.7)	(4.8)	(8.3)	(0.9)	(6.0)	(33.7)
Charged/(credited) to the income statement	0.5	(0.1)	(3.3)	1.9	0.4	7.8	7.2
Acquisition of Bristol Water Group	–	–	–	(32.8)	19.1	–	(13.7)
Non-underlying charge/(credit) to the income statement	0.3	(0.2)	(2.5)	(2.2)	–	10.3	5.7
(Credited)/charged to equity, including impact on change in tax rate	6.5	–	–	–	–	(2.4)	4.1
Reclassified to deferred tax liabilities	–	–	–	–	(18.6)	(9.7)	(28.3)
At 31 March 2022	(4.7)	(2.0)	(10.6)	(41.4)	–	–	(58.7)
Charged/(credited) to the income statement	0.3	0.5	(14.7)	2.2	–	–	(11.7)
Non-underlying charge/(credit) to the income statement	–	–	(10.6)	8.1	–	–	(2.5)
Reclassification to deferred tax liabilities	(2.9)	–	–	–	–	–	(2.9)
Charged to equity, including impact on change in tax rate	7.3	0.5	–	–	–	–	7.8
At 31 March 2023	**–**	**(1.0)**	**(35.9)**	**(31.1)**	**–**	**–**	**(68.0)**

Net liability	
At 31 March 2022	512.4
At 31 March 2023	**507.0**

Company

Deferred tax assets

	Retirement benefit obligations £m	Derivatives £m	Share-based payments £m	Tax losses £m	Total £m
At 1 April 2021	(6.8)	–	(0.9)	(4.8)	(12.5)
Charged/(credited) to the income statement	6.5	–	(0.1)	(3.3)	3.1
Non-underlying credit to the income statement	2.5	–	(0.2)	(2.5)	(0.2)
Credited to equity, including impact on change in tax rate	(3.5)	–	–	–	(3.5)
At 31 March 2022	(1.3)	–	(1.2)	(10.6)	(13.1)
Charged/(credited) to the income statement	2.0	–	0.3	(4.7)	(2.4)
Non-underlying charge/(credit) to the income statement	–	–	–	(1.3)	(1.3)
Charged/(credited) to equity, including impact on change in tax rate	(2.0)	–	0.2	–	(1.8)
At 31 March 2023	**(1.3)**	**–**	**(0.7)**	**(16.6)**	**(18.6)**

Deferred tax charged/(credited) to equity or other comprehensive income during the year was:

	Group		Company	
	2023 £m	2022 £m	**2023 £m**	2022 £m
Remeasurement of defined benefit obligations	**(9.8)**	2.4	**(2.0)**	(3.5)
Cash flow hedges	**7.3**	(6.5)	**–**	**–**
Share-based payments	**0.5**	–	**0.2**	**–**
	(2.0)	(4.1)	**(1.8)**	(3.5)

Capital allowances are available when a business incurs qualifying expenditure on capital items such as infrastructure assets. Capital allowances provide tax relief on these items in place of accounting depreciation which is not tax deductible. Over the period of ownership of an asset, cumulative depreciation and capital allowances will equalise. Capital allowance rates are set by the UK Government and every business receives the same rate of allowance. Capital allowance rates typically vary from 3% up to 100% in certain instances. In recent years enhanced allowances known as super deductions at 130% have been available on plant and machinery assets acquired after 3 March 2021 together with 50% first year allowances on special rate assets. From 1 April 2023, super deductions will be replaced by full expensing for three years whilst the 50% first year allowance will be maintained for the same period. Given the Group's continuing capital expenditure programme, it is unlikely that the deferred tax liability will crystallise in the near future.

The different accounting treatment of property, plant and equipment for tax and accounting purposes means that the taxable income of the Group is not the same as the profit reported in the financial statements. The adjustments for this are reflected in the current tax reconciliation. As explained in note 9, the Government has introduced capital expenditure super-deduction allowance incentives for the two year period to April 2023 which increases the rate of capital allowances to up to 130% for expenditure on qualifying plant and machinery. This provides an increase in current tax relief for the Group with a consequently higher deferred tax liability and charge due to the additional capital allowance deductions and the increase in the rate of corporation tax to 25% from April 2023.

31. Deferred tax *continued*

Short term temporary differences arise on items such as retirement benefit obligations, derivatives and share based payments because the treatment of such items are different for tax and accounting purposes. These differences reverse over future years following that in which they arise, as is reflected in the deferred tax charge in these financial statements. Specifically, retirement benefit obligations will crystallise over the life of the pension scheme and/or the period when spreading applies (this can be up to three years for spreading purposes), whilst share based payments will crystallise over the remaining life of the share schemes which are up to 5 years. Short term liabilities including provisions will typically crystallise in the following year.

The fair value liability relates to the revaluation of tangible fixed assets on the acquisition of Bournemouth Water and Bristol Water. The fair value asset relates to the revaluation of debt on the acquisition of Bournemouth Water and Bristol Water. These items will be released over their remaining life which is up to 142 years.

Where interest charges or other costs are capitalised in the accounts, tax relief is either given as the charges are incurred or when the costs are taken to the income statement.

Derivatives reflect the fair value movements on treasury derivatives, these can fluctuate considerably each year. The balance will crystallise when derivative items are either terminated or mature, the life of these items can be up to ten years.

Tax losses relate to trading losses generated in the year and non-trade deficits carried forwards in relation to the UK's corporate interest restriction rules, these are anticipated to be utilised within the next five years.

32. Provisions

	Restructuring £m	Total £m
Group		
At 1 April 2022	1.0	1.0
Utilised	(0.6)	(0.6)
Charged to the income statement	–	–
At 31 March 2023	**0.4**	**0.4**

The restructuring provision relates principally to severance costs and will be utilised within one year.

33. Share capital

Allotted, called-up and fully paid

	Number of shares		
	Treasury shares	Ordinary shares	£m
Group and Company			
At 1 April 2021 ordinary shares of 40.7p each	8,443	422,120,181	171.8
Share consolidation	(2,815)	(140,708,916)	–
For consideration of £3.8 million, shares issued under the Company's Sharesave Scheme	–	582,427	0.4
Shares cancelled	–	(17,146,744)	(10.5)
At 31 March 2022 ordinary shares of 61.05p each	5,628	264,846,948	161.7
For consideration of £2.3 million, shares issued under the Company's Sharesave Scheme	–	379,044	0.2
Shares cancelled	–	(3,910,503)	(2.4)
At 31 March 2023 ordinary shares of 61.05p each	**5,628**	**261,315,489**	**159.5**

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

On 16 July 2021, the Group paid a special dividend of £1.5 billion to shareholders in relation to the return of capital to shareholders announced on 3 June 2021. In order to maintain the comparability of the Company's share price before and after the special dividend, a share consolidation was approved at the General Meeting held on 28 June 2021. Shareholders received 2 New Ordinary shares of 61.05 pence each for every 3 Existing Ordinary shares of 40.7 pence each.

During the prior year, the Group announced and began a process to purchase ordinary shares at an aggregate cost of up to £400 million by September 2022. During the prior year the Group purchased £199.6 million of ordinary shares from the market at an average ordinary share price of 1,164 pence. The shares acquired under the tender offer were immediately cancelled, creating a capital redemption reserve of £10.5 million. The maximum number of shares that can be repurchased in connection with the Programme is 42,183,689 (being the maximum authority granted by Pennon's shareholders at Pennon's AGM on 22 July 2021).

During the year ended 31 March 2023, the Group purchased a further £39.9 million of ordinary shares from the market at an average ordinary share price of 1,022 pence. The total aggregate cost of the Buy-back programme, which has terminated, was £239.5 million. The shares acquired under the tender offer were immediately cancelled, creating a capital redemption reserve of £2.4 million.

Employee share schemes

The Group operates a number of equity-settled share plans for the benefit of employees. Details of each plan are:

i) Sharesave Scheme

An all-employee savings-related plan is operated that enables employees, including Executive Directors, to invest up to a maximum of £500 per month for three or five years. These savings can then be used to buy ordinary shares, at a price set at a 17% or 20% discount to the market value at the start of the savings period, at the third or fifth year anniversary of the option being granted. Options expire six months following the exercise date and, except for certain specific circumstances such as redundancy, lapse if the employee leaves the Group before the option exercise period commences.

33. Share capital *continued*

Outstanding options to subscribe for ordinary shares of 61.05 pence each under the Company's share option schemes are:

	Date granted and subscription price fully paid	Period when options normally exercisable	Thousands of shares in respect of which options outstanding at 31 March	
			2023	2022
28 June 2017	767p	2020 – 2022	**–**	28
3 July 2018	635p	2021 – 2023	**100**	112
9 July 2019	620p	2022 – 2024	**84**	447
19 July 2020	928p	2023 – 2025	**193**	234
6 July 2021	879p	2024 – 2026	**552**	680
5 July 2022	828p	2025 – 2027	**533**	–
			1,462	1,501

The number and weighted average exercise price of Sharesave options are:

	2023		2022	
	Number of ordinary shares (thousands)	**Weighted average exercise price per share (p)**	Number of ordinary shares (thousands)	Weighted average exercise price per share (p)
At 1 April	**1,501**	**789**	1,494	687
Granted	**598**	**828**	723	879
Forfeited	**(215)**	**781**	(43)	695
Exercised	**(379)**	**633**	(582)	640
Expired	**(43)**	**859**	(91)	817
At 31 March	**1,462**	**835**	1,501	789

The weighted average price of the Company's shares at the date of exercise of Sharesave options during the year was 927 pence (2022 1,216 pence). The options outstanding at 31 March 2023 had a weighted average exercise price of 620 pence (2022 789 pence) and a weighted average remaining contractual life of 1.91 years (2022 1.96 years). The number of exercisable Sharesave options at 31 March 2023 was 1,000 (2022 2,000) and the weighted average exercise price of exercisable Sharesave options was 620 pence (2022 635 pence).

The aggregate fair value of Sharesave options granted during the year was £0.7 million (2022 £2.0 million), determined using the Black-Scholes valuation model. The significant inputs into the valuation model at the date of issue of the options were:

	2023	2022
Weighted average share price (pence)	**957**	1,187
Weighted average exercise price (pence)	**828**	879
Expected volatility	**25%**	27%
Expected life	**3.3 years**	3.4 years
Risk-free rate	**1.3%**	0.10%
Expected dividend yield	**4.0%**	3.0%

Expected volatility was determined by calculating the historical volatility of the Group's share price over the previous three years.

ii) Long-term incentive plan (LTIP)

Executive Directors and senior management receive an annual grant of conditional shares. Share awards vest subject to the achievement of specific performance conditions measured over a performance period of not less than three years.

The number and price of shares in the LTIP are:

	2023		2022	
	Number of ordinary shares (thousands)	**Weighted average exercise price per share (p)**	Number of ordinary shares (thousands)	Weighted average exercise price per share (p)
At 1 April	**1,170**	**902**	999	843
Granted	**255**	**1,038**	221	1,141
Vested	**(357)**	**790**	–	–
Lapsed	**(188)**	**876**	(50)	790
At 31 March	**880**	**990**	1,170	902

The awards outstanding at 31 March 2023 had a weighted exercise price of 990 pence (2022 902 pence) and a weighted average remaining contractual life of 2.6 years (2022 2.3 years).

The aggregate fair value of awards granted during the year was £1.1 million (2022 £1.0 million), determined from market value. No option pricing methodology is applied since the vesting of the shares depends on non-market performance vesting conditions.

Having reflected on the exceptional economic backdrop and in particular the cost-of-living crises faced by many of our customers, the CEO recommended that the Remuneration Committee consider lapsing her bonus and 2020 LTIP awards in full, and diverting an equivalent value into the Group's Watershare+ scheme. The Watershare+ scheme directly benefits the Group's customers by either providing money off their bill or via ownership of Pennon Group plc shares. While recognising the performance delivered, the Remuneration Committee accepted and approved the CEO's recommendation regarding her awards.

33. Share capital *continued*

iii) Annual Incentive Bonus Plan – deferred shares

Awards under the plan to Executive Directors and senior management involve the release of ordinary shares in the Company to participants. There is no performance condition since vesting is conditional upon continuous service with the Group for a period of three years from the award. The number and weighted average price of shares in the Annual Incentive Bonus Plan are:

	2023		2022	
	Number of ordinary shares (thousands)	**Weighted average exercise price per share (p)**	Number of ordinary shares (thousands)	Weighted average exercise price per share (p)
At 1 April	**206**	**955**	345	847
Granted	**54**	**988**	82	1,141
Vested	**(110)**	**756**	(75)	761
Lapsed	**(9)**	**1,001**	(2)	941
Cancelled	**–**	**–**	(144)	903
At 31 March	**141**	**1,065**	206	955

The awards outstanding at 31 March 2023 had a weighted average exercise price of 1,065 pence (2022 955 pence) and a weighted average remaining contractual life of 1.3 years (2022 1.1 years). The Company's share price at the date of the awards ranged from 988 pence to 1,141 pence (2022 756 pence to 1,141 pence).

The aggregate fair value of awards granted during the year was £0.5 million (2022 £0.9 million), determined from market value. No option pricing methodology is applied since dividends paid on the shares are receivable by the participants in the scheme.

Further details of the plans and options granted to Directors, included above, are shown in the Directors' remuneration report.

34. Share premium account

	£m
Group and Company	
At 1 April 2021	232.1
Shares issued under the Sharesave Scheme	3.4
At 31 March 2022	235.5
Shares issued under the Sharesave Scheme	2.1
At 31 March 2023	**237.6**

35. Capital redemption reserve

The capital redemption reserve represents the redemption of B shares and cancellation of deferred shares arising from a capital return to shareholders undertaken during 2006, together with the redemption of shares during the years ended 31 March 2023 and 31 March 2022.

	£m
Group and Company	
At 1 April 2021	144.2
Share capital redeemed	10.5
At 31 March 2022	154.7
Share capital redeemed	2.4
At 31 March 2023	**157.1**

36. Retained earnings and other reserves

	Own shares £m	Hedging reserve £m	Retained earnings £m	Total £m
Group				
At 31 March 2021	(3.5)	(17.0)	2,457.3	2,436.8
Profit for the year	–	–	15.4	15.4
Other comprehensive income for the year	–	34.1	27.3	61.4
Dividends paid relating to 2021	–	–	(1,590.3)	(1,590.3)
Credit to equity in respect of share-based payments (net of tax)	–	–	2.2	2.2
Charge in respect of share options vesting	0.8	–	(0.8)	–
Own shares acquired by the Pennon Employee Share Trust in respect of share options granted	(1.2)	–	–	(1.2)
Shares purchased for cancellation (included related expenses)	–	–	(201.7)	(201.7)
At 31 March 2022	(3.9)	17.1	709.4	722.6
Profit for the year	–	–	0.1	0.1
Other comprehensive income/(loss) for the year	–	21.8	(29.2)	(7.4)
Dividends paid relating to 2022	–	–	(101.6)	(101.6)
Credit to equity in respect of share-based payments (net of tax)	–	–	1.9	1.9
Charge in respect of share options vesting	5.4	–	(5.4)	–
Own shares acquired by the Pennon Employee Share Trust in respect of share options granted	(5.0)	–	–	(5.0)
Shares purchased for cancellation (included related expenses)	–	–	(40.0)	(40.0)
At 31 March 2023	**(3.5)**	**38.9**	**535.2**	**570.6**

The own shares reserve represents the cost of ordinary shares in Pennon Group plc issued to or purchased in the market and held by the Pennon Group plc Employee Benefit Trust to satisfy awards under the Group's Annual Incentive Bonus Plan.

The market value of the 152,000 ordinary shares (2022 238,000 ordinary shares) held by the Trust at 31 March 2023 was £1.2 million (2022 £2.6 million).

	Hedging reserve £m	Retained earnings £m	Total £m
Company			
At 1 April 2021	(0.1)	2,410.9	2,410.8
Profit for the year	–	74.5	74.5
Other comprehensive income/(loss) for the year	0.1	(2.6)	(2.5)
Dividends paid relating to 2021 (including £1.5 billion special dividend)	–	(1,590.3)	(1,590.3)
Shares purchased for cancellation (including related expenses)	–	(201.7)	(201.7)
Credit to equity in respect of share-based payments (net of tax)	–	0.9	0.9
Charge in respect of share options vesting	–	(2.6)	(2.6)
At 31 March 2022	–	689.1	689.1
Profit for the year	–	8.4	8.4
Other comprehensive loss for the year	–	(6.1)	(6.1)
Dividends paid relating to 2022	–	(101.6)	(101.6)
Shares purchased for cancellation (including related expenses)	–	(40.0)	(40.0)
Credit to equity in respect of share-based payments (net of tax)	–	1.3	1.3
Charge in respect of share options vesting	–	(5.4)	(5.4)
At 31 March 2023	**–**	**545.7**	**545.7**

In making decisions about the level of dividends to be proposed the Directors take steps to check that retained earnings reflect realised profits and are therefore distributable within the requirements of the Companies Act 2006.

37. Analysis of cash flows given in the statement of cash flows

Reconciliation of profit for the year to cash generated from operations:

Cash generated from operations

	Group		Company	
	2023 £m	2022 £m	**2023 £m**	2022 £m
Profit for the year	**0.4**	15.6	**8.4**	74.5
Adjustments for:				
Share-based payments	**2.4**	2.2	**1.5**	1.1
Profit on disposal of property, plant and equipment	**(0.4)**	(1.0)	**–**	–
Depreciation charge	**151.1**	143.3	**–**	–
Amortisation of intangible assets	**3.6**	3.4	**–**	–
Investment impairment charge	**–**	–	**–**	0.4
non-underlying bond early redemption gain	**(18.4)**		**–**	
non-underlying Bristol Water acquisition costs	**–**	8.9	**–**	8.9
non-underlying CMA merger review and integration costs	**–**	6.9	**–**	4.8
Share of post-tax profit from associated companies	**(0.3)**	–	**–**	–
Finance income (before non-underlying items)	**(9.2)**	(2.6)	**(11.8)**	(6.5)
Finance costs (before non-underlying items)	**145.8**	96.3	**13.3**	10.8
Dividends receivable	**–**	–	**(15.7)**	(94.5)
Taxation (credit)/charge	**(8.9)**	112.1	**(4.3)**	(2.7)
Changes in working capital:				
Increase in inventories	**(2.3)**	(0.6)	**–**	–
Decrease/(increase) in trade and other receivables	**15.9**	(14.3)	**(31.0)**	6.9
Increase/(decrease) in trade and other payables	**34.6**	(12.2)	**0.6**	(9.6)
Increase/(decrease) in retirement benefit obligations from contributions	**–**	(24.2)	**0.1**	(24.0)
(Decrease)/increase in provisions	**(0.6)**	0.4	**–**	–
Cash generated/(outflow) from operations	**313.7**	334.2	**(38.9)**	(29.9)

Reconciliation of total interest paid:

	Group		Company	
	2023 £m	2022 £m	**2023 £m**	2022 £m
Interest paid in operating activities	**159.7**	74.6	**7.7**	6.0
Interest paid in investing activities	**5.0**	1.3	**–**	–
Total interest paid	**164.7**	75.9	**7.7**	6.0

During the year, the Group completed a number of sale and leaseback transactions in respect of its infrastructure assets as part of its ongoing financing arrangements. Cash proceeds of £40.2 million (2022 £15.0 million) were received and a gain of £nil (2022 £nil) was recognised. These assets are being leased back at market rentals over varying lease terms from 7.5 to 9.5 years.

38. Net borrowings

	Group		Company	
	2023 £m	2022 £m	**2023 £m**	2022 £m
Cash and cash deposits	**165.4**	519.0	**104.1**	306.7
Borrowings – current				
Bank and other current borrowings	**(92.7)**	(70.0)	**–**	(30.0)
Lease obligations	**(32.0)**	(170.2)	**–**	–
Amounts owed to subsidiary undertakings	**–**	–	**(279.1)**	(282.8)
Total current borrowings	**(124.7)**	(240.2)	**(279.1)**	(312.8)
Borrowings – non-current				
Bank and other non-current borrowings	**(1,960.9)**	(1,907.4)	**(155.7)**	(154.5)
Listed preference shares	**(12.5)**	(12.5)	**–**	–
Lease obligations	**(1,032.7)**	(1,041.8)	**–**	–
Total non-current borrowings	**(3,006.1)**	(2,961.7)	**(155.7)**	(154.5)
Total net borrowings	**(2,965.4)**	(2,682.9)	**(330.7)**	(160.6)

38. Net borrowings *continued*

The movements in net borrowings during the periods presented were as follows:

Group

	Net borrowings at 1 April 2021 £m	Bristol Water acquisition £m	Cash flows £m	Transfer between non-current and current £m	Other non-cash movements £m	Net borrowings at 31 March 2022 £m
Cash and cash deposits	2,919.3	6.1	(2,406.4)	–	–	519.0
Bank and other current borrowings	(40.1)	(9.0)	49.4	(70.4)	0.1	(70.0)
Current lease obligations	(48.2)	(0.2)	232.8	(365.5)	10.9	(170.2)
Bank and other non-current borrowings	(1,375.7)	(516.7)	(61.0)	70.4	(24.4)	(1,907.4)
Listed preference shares	–	(12.5)	–	–	–	(12.5)
Non-current lease obligations	(1,391.0)	(1.2)	(15.0)	365.5	(0.1)	(1,041.8)
Net cash/(borrowings)	64.3	(533.5)	(2,200.2)	–	(13.5)	(2,682.9)

	Net borrowings at 1 April 2022 £m	Cash flows £m	Transfer between non-current and current £m	Other non-cash movements £m	Net borrowings at 31 March 2023 £m
Cash and cash deposits	**519.0**	**(353.6)**	**–**	**–**	**165.4**
Bank and other current borrowings	**(70.0)**	**20.4**	**(43.3)**	**0.2**	**(92.7)**
Current lease obligations	**(170.2)**	**221.1**	**(49.1)**	**(33.8)**	**(32.0)**
Bank and other non-current borrowings	**(1,907.4)**	**(57.2)**	**43.3**	**(39.6)**	**(1,960.9)**
Listed preference shares	**(12.5)**	**–**	**–**	**–**	**(12.5)**
Non-current lease obligations	**(1,041.8)**	**(40.2)**	**49.1**	**0.2**	**(1,032.7)**
Net borrowings	**(2,682.9)**	**(209.5)**	**–**	**(73.0)**	**(2,965.4)**

Other non-cash movements for the Group in 2023 includes the increase in borrowings from interest which is rolled into the amount repayable.

The movements in net borrowings during the periods presented were as follows:

Company

	Net borrowings at 1 April 2021 £m	Cash flows £m	Other non-cash movements £m	Net borrowings at 31 March 2022 £m
Cash and cash deposits	2,495.6	(2,188.9)	–	306.7
Bank and other loans due within one year	–	–	(30.0)	(30.0)
Amounts due to subsidiary undertakings	(283.4)	0.5	0.1	(282.8)
Bank and other loans due after one year	(184.4)	–	29.9	(154.5)
	2,027.8	(2,188.4)	–	(160.6)

	Net borrowings at 1 April 2022 £m	**Cash flows £m**	**Other non-cash movements £m**	**Net borrowings at 31 March 2023 £m**
Cash and cash deposits	**306.7**	**(202.6)**	**–**	**104.1**
Bank and other loans due within one year	**(30.0)**	**30.0**	**–**	**–**
Amounts due to subsidiary undertakings	**(282.8)**	**3.7**	**–**	**(279.1)**
Bank and other loans due after one year	**(154.5)**	**–**	**(1.2)**	**(155.7)**
	(160.6)	**(168.9)**	**(1.2)**	**(330.7)**

39. Subsidiary and joint venture undertakings at 31 March 2023

Principal subsidiary companies	Registered office address	Country of incorporation, registration and principal operations
Water		
Bristol Water Plc	Bridgwater Road, Bristol, BS13 7AT	England
South West Water Limited*	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
South West Water Finance Plc	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
South West Water Customer Services Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Non-household retail		
Pennon Water Services Limited*(1)	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Other		
Peninsula Insurance Limited*(2)	Level 5, Mill Court, La Charroterie, St Peter Port, GY1 1EJ	Guernsey

* Indicates the shares are held directly by Pennon Group plc, the Company.

1. 80% of share capital owned by Pennon Group plc. All shares in issue are ordinary shares.
2. Captive insurance company established with the specific objective of financing risks emanating from within the Group.

Other trading companies	Registered office address	Country of incorporation
Bristol Water Holdings UK Limited*	Bridgwater Road, Bristol, BS13 7AT	England
Bristol Water Core Holdings Limited	Bridgwater Road, Bristol, BS13 7AT	England
Bristol Water Holdings Limited	Bridgwater Road, Bristol, BS13 7AT	England
Peninsula Properties (Exeter) Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Peninsula Trustees Limited*	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Pennon Defined Contribution Pension Trustee Limited*	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Pennon Pension Trustees Limited*	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Pennon Trustee Limited*	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Avon Valley Water Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Bournemouth Water Investments Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Bournemouth Water Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
BWH Enterprises Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
D.M.P (Holdings) Limited* §	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Exe Continental §	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Greenhill Environmental Limited* §	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Haul Waste Limited* §	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Pennon Share Scheme Trustees Limited*	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Pennon South West Limited* §	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Pennon Waste Management Limited* §	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Seal Security Systems Limited* §	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Source for Business Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
SSWB Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
SWW Pension Trustees Limited*	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Contracting Limited §	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England

The subsidiary undertakings are wholly owned unless stated otherwise and all shares in issue are ordinary shares. All companies above are consolidated in the Group financial statements.

Joint Ventures and Associates	Registered office address	Country of incorporation	Stake (%)
Bristol Wessex Billing Services Limited	1 Clevedon Walk, Nailsea, Bristol, BS48 1WA	England	50
CREWW Executive Board Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England	50
Searchlight Collections Limited	PO BOX 930 Galmington Office, Galmington Trading Estate, Cornishway West, Taunton, Somerset, TA1 9LQ	England	50
Water 2 Business Limited	21e Somerset Square, Nailsea, Bristol, United Kingdom, BS48 1RQ	England	30

* Indicates the shares are held directly by Pennon Group plc, the Company.

*§ Indicates the subsidiary was dissolved since the balance sheet date.

39. Subsidiary and joint venture undertakings at 31 March 2023 *continued*

Subsidiary audit exemption

Pennon Group plc has issued guarantees over the liabilities of the following companies at 31 March 2021 under section 479C of Companies Act 2006 and these entities are exempt from the requirements of the Act relating to the audit of individual accounts by virtue of section 479A of the Act.

Company	Company number
Bristol Water Core Holdings Limited	04637554
Bristol Water Holdings Limited	02630760
Bristol Water Holdings UK Limited	04789566
Peninsula Properties (Exeter) Limited	02307220
Pennon Power Limited	00736732
South West Water Customer Services Limited	07620338
Viridor Waste 2 Limited	02298543

40. Contingencies

Contingent liabilities

	Group		Company	
	2023 £m	2022 £m	**2023 £m**	2022 £m
Guarantees:				
Performance bonds	**9.7**	9.7	**9.7**	9.7
	9.7	9.7	**9.7**	9.7

Guarantees in respect of performance bonds relate to changes to the collateral requirements for the non-household retail business with other wholesalers.

Other contractual and litigation uncertainties

Ofwat and the Environment Agency announced an industry-wide investigation into sewage treatment works on 18 November 2021. On 27 June 2022, as part of its ongoing investigation, Ofwat announced enforcement action against South West Water Limited, the company is now included alongside the five companies which received enforcement notices in March 2022. The company continues to work openly with Ofwat to comply with the notice as part of this ongoing investigation. The potential outcome of these investigations continues to be unknown.

On 23 May 2023 Ofwat announced an investigation into South West Water's 2021/22 operational performance data relating to leakage and per capita consumption. This operational performance data was reported in South West Water's Annual Performance Report 2021/22. This report is subject to assurance processes which include independent checks and balances carried out by an external technical auditor. The company will work openly and constructively with Ofwat to comply with the formal notice issued to South West Water as part of this investigation. The potential outcome of this investigation is currently unknown.

The Group establishes provisions in connection with contracts and litigation where it has a present legal or constructive obligation as a result of past events and where it is more likely than not an outflow of resources will be required to settle the obligation and the amount can be reliably estimated. Where it is uncertain that these conditions are met, a contingent liability is disclosed unless the likelihood of the obligation arising is remote or the matter is not deemed material.

41. Capital commitments

	Group		Company	
	2023 £m	2022 £m	**2023 £m**	2022 £m
Contracted but not provided	**72.0**	59.5	**–**	–

42. Related party transactions

Group companies entered into the following transactions with joint ventures which were not members of the Group. Bristol Wessex Billing Services Limited and Water 2 Business Limited are joint venture investments of Bristol Water Holdings Limited.

	2023 £m	2022 £m
Sales of goods and services		
Water 2 Business Limited	**17.9**	14.5
Purchase of goods and services		
Bristol Wessex Billing Services Limited	**3.5**	2.4

Year-end balances

	2023 £m	2022 £m
Receivables due from related parties		
Water 2 Business Limited (including loan receivable of £9.3 million (2022 £9.6 million)	**10.8**	11.1
Bristol Wessex Billing Services Limited	**1.6**	0.9
Payables due to related parties		
Water 2 Business Limited	**–**	0.4
Bristol Wessex Billing Services Limited	**–**	1.4

42. Related party transactions *continued*

The receivables due from related parties are unsecured and will be settled in cash. No guarantees have been given or received. No provisions have been made, or are considered necessary, for doubtful debts in respect of these amounts due.

The loans to Water 2 Business Limited are due to be repaid on 28 February 2025 and carry interest at SONIA plus 2.00%.

Company

The following transactions with subsidiary undertakings occurred in the year:

	2023 £m	2022 £m
Sales of goods and services (management fees)	**7.9**	9.0
Purchase of goods and services (support services)	**0.5**	0.5
Interest receivable	**3.0**	1.3
Dividends received	**15.7**	94.5

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

	2023 £m	2022 £m
Receivables due from subsidiary undertakings		
Loans	**99.2**	31.5
Trading balances and other receivables	**2.6**	48.2

The loan balance comprises two loans. A loan with a balance of £26.1m is due for repayment in instalments over a five-year period following a receipt of a request to repay. No request to repay has been issued at the current time. Interest on £13.1 million (2022 £13.1 million) of the loans has been charged at a fixed rate of 5%. Interest on £13.0 million (2022 £13.0 million) of the loans has been charged at 12-month SONIA +3.0%. A loan with a balance of £73.1m was repaid on 16 May 2023. This loan was issued on 16 November 2022 to Bristol Water plc and novated to South West Water limited on 1 February 2023. Interest was charged on the loan balance at Bank of England base rate +0.75%.

No material expected credit loss provision has been recognised in respect of loans to subsidiaries (2022 nil).

	2023 £m	2022 £m
Payables due to subsidiary undertakings		
Loans	**279.1**	282.8
Trading balances	**8.5**	8.6

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

43. Acquisition of Bristol Water Group

On 2 June 2021, the Company acquired 100% of the issued share capital and voting rights of Bristol Water Holdings UK Limited, the holding company of the Bristol Water Group. Bristol Water Group comprises Bristol Water plc, a regulated water only company and a 30% share in Water 2 Business Limited, a joint venture with Wessex Water. The purpose of the acquisition was to grow the Group's core water business by expanding into a geographically contiguous region. The acquisition of the Bristol Water Group was reviewed by the Competition and Markets Authority and given full clearance on 7 March 2022. The Bristol Water Group is consolidated in Pennon's accounts with effect from the completion of acquisition at midnight on 2 June 2021.

The net assets recognised in the 31 March 2022 financial statements were based on a provisional assessment of their fair value. The Group had not completed a full tax review by the date the 2022 financial statements were approved for issue by the Board of Directors. In early June 2022 the final review of tax balances was completed, this has led to an increase in the deferred tax liability with an offsetting increase in the total value of goodwill recognised on acquisition of £5.5 million, the amortisation of this deferred tax liability to 31 March 2023 is immaterial. Final fair values on acquisition are shown in the table below. Corresponding amounts for the financial year ended 31 March 2022 have also been restated.

The goodwill that arose on the acquisition can be attributed to synergies expected to be derived from the combination and the value of the workforce which cannot be recognised as a separately identifiable intangible asset. Goodwill has been allocated to the water segment. The goodwill arising is not expected to be tax deductible.

43. Acquisition of Bristol Water Group *continued*

The details of the business combination are as follows:

	£m
Fair value of consideration transferred	
Amount settled in cash	**419.6**
Recognised amounts of identifiable net assets	
Property, plant and equipment	**944.8**
Intangible assets	**12.8**
Other non-current assets	**9.9**
Inventories	**1.7**
Trade and other receivables	**22.3**
Cash and cash deposits (including restricted cash of £6.1 million)	**18.9**
Current tax liability	**(2.2)**
Borrowings	**(545.1)**
Trade and other payables	**(32.2)**
Provisions	**(0.3)**
Retirement benefit obligations	**7.8**
Deferred tax liabilities	**(140.4)**
Identifiable net assets	**298.0**
Goodwill on acquisition	**121.6**
Consideration for equity settled in cash	**419.6**
Payment to acquire loan to former parent	**5.5**
Cash and cash equivalents acquired (excluding restricted cash)	**(12.8)**
Net cash outflow on acquisition	**412.3**
Acquisition costs paid charged to expenses	**8.9**
Net cash paid relating to the acquisition	**421.2**

Acquisition related costs of £8.9 million are not included as part of the consideration transferred and were recognised as an expense in the consolidated income statement within other operating expenses.

The fair value of trade and other receivables acquired as part of the business combination amounted to £22.3 million with a gross contractual amount of £38.9 million. At the acquisition date the Group's best estimate of the contractual cash flows expected not to be collected amounted to £16.6 million.

As part of the acquisition of Bristol Water, the Group acquired interests in two joint ventures, Bristol Wessex Billing Services Limited ("BWBSL") and Water 2 Business Limited ("water2business"). These two interests are accounted for using the equity method. Currently the carrying values of these investments equates to £0.3m (2022 nil), representing the relevant share of the net assets of each of these interests.

The goodwill that arose on the acquisition can be attributed to synergies expected to be derived from the combination and the value of the workforce which cannot be recognised as an intangible asset. Goodwill has been allocated to the water segment. The goodwill arising is not expected to be tax deductible.

44. Events after the reporting period

In May 2023 the Group acquired a c.40 Gwh solar photovoltaic site in Dunfermline which is ready to build with consents in place, and is expected to commence generation in 2024, for total acquisition and build costs of c.£35 million. The site also has the capacity for a two-hour 60 MW battery that will support the UK Grid's move to renewables at a cost of c.£25 million.

On 23 April 2023, South West Water was issued with a fine of £2.15 million in relation to pollution offences occurring between 2016 and 2020, following a case brought by the Environment Agency. The liability for the fine and related costs are recorded on the balance sheet of the Group as at 31 March 2023.

On 23 May 2023 Ofwat announced an investigation into South West Water's 2021/22 operational performance data relating to leakage and per capita consumption. This operational performance data was reported in South West Water's Annual Performance Report 2021/22. This report is subject to rigorous assurance processes which include independent checks and balances carried out by an external technical auditor. The company will work openly and constructively with Ofwat to comply with the formal notice issued to South West Water as part of this investigation. The potential outcome of this investigation is currently unknown.

Alternative performance measures

Alternative performance measures (APMs) are financial measures used in this report that are not defined by International Financial Reporting Standards (IFRS). The Directors believe that these APMs assist in providing additional useful information on the underlying trends, performance and position of the Group as well as enhancing the comparability of information between reporting periods.

As the Group defines the APMs they might not be directly comparable to other companies' APMs. They are not intended to be a substitute for, or superior to, IFRS measurements. The following APMs have been added or amended to those presented previously to reflect the changing nature of the Group for the acquisition of Bristol Water in June 2021 and integration of Bristol Water plc into South West Water Limited's group of companies:

- The APM for 'Effective interest rate' has been updated following changes to Group financial structures during the financial year. Following the acquisition of Bristol Water, Bristol Water plc has been integrated into South West Water Limited's group of companies. This metric has been amended, with the prior year reanalysed, to ensure a consistent, comparable metric is presented and is reflective of South West Water performance.
- An APM for the 'Effective cash cost of interest' has been presented in addition to the 'Effective interest rate' APM to provide an insight into South West Water's interest charges excluding finance costs that are not paid in the year but accrete to the carrying value of debt. This provides a useful insight into South West Water's cash cost of debt.
- The APM 'South West Water return on capital employed' has reverted to 'Group return on capital employed' (as presented in 2021/22 results) given the Group's current balance sheet structure. In the previous two years the APM was altered to 'South West Water return on capital employed' as this provided a more meaningful comparison of performance due to the Group holding a net cash position at 31 March 2021.
- The APM 'Continuing operations operational cash inflows and other movements' has been discontinued as management believe the statutory cash flows from operating activities appropriately reflects performance.
- The APM 'Regulatory Capital Value (RCV)' definition has been added alongside other regulatory APM definitions to provide additional information about the regulatory framework.

Underlying earnings

Underlying earnings are presented alongside statutory results as the Directors believe they provide a more useful comparison on business trends and performance. Note 6 in the notes to the financial statements provides more detail on non-underlying items, and a reconciliation of underlying earnings for the current year and the prior year is as follows:

		Non-underlying items						
Underlying earnings reconciliation 31 March 2023	**Underlying**	**Integration costs**	**WaterShare+**	**Drought incentive**	**Drought costs**	**Bond redemption**	**Statutory results**	**Earnings per share**
	£m	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**p**
EBITDA (see below)	**307.8**	**(4.3)**	**(22.4)**	**(7.6)**	**(9.4)**	**-**	**264.1**	
Operating profit	**153.1**	**(4.3)**	**(22.4)**	**(7.6)**	**(9.4)**	**-**	**109.4**	
Profit before tax	**16.8**	**(4.3)**	**(22.4)**	**(7.6)**	**(9.4)**	**18.4**	**(8.5)**	
Taxation	**3.6**	**1.1**	**5.5**	**1.5**	**1.8**	**(4.6)**	**8.9**	
Profit after tax							**0.4**	
Non-controlling interests							**(0.3)**	
Profit after tax attributable to shareholders							**0.1**	**-**

		Non-underlying items			
Underlying earnings reconciliation 31 March 2022	Underlying £m	Deferred tax change of rate £m	Acquisition and merger review related costs £m	Statutory results £m	Earnings per share p
EBITDA (see below)	383.9	-	(15.8)	368.1	
Operating profit	237.2	-	(15.8)	221.4	
Profit before tax	143.5	-	(15.8)	127.7	
Taxation	(13.9)	(99.5)	1.3	(112.1)	
Profit after tax				15.6	
Non-controlling interests				(0.2)	
Profit after tax attributable to shareholders				15.4	4.9

Underlying EBITDA

Underlying EBITDA (earnings before interest, tax, depreciation and amortisation and non-underlying items) is used to assess and monitor operational underlying performance.

Basic adjusted earnings per share (adjusted for share consolidation)

	2023	2022
Basic weighted average number of shares		
Basic weighted average number of shares (millions) (note 11)	**261.9**	312.1
Adjustment to reflect the post-consolidation share base as if it had been in place from the start of the previous financial year (millions)	**-**	(36.6)
Adjusted basic weighted average number of shares (adjusted for share consolidation) (millions)	**261.9**	275.5
Basic adjusted earnings per share from continuing operations before non-underlying items and deferred tax (pence) (note 11)	**7.3**	44.3
Adjustment to reflect the post-consolidation share base as if it had been in place from the start of the previous financial year (pence)	**-**	5.9
Basic adjusted earnings per share before non-underlying items and deferred tax (adjusted for share consolidation) (pence)	**7.3**	50.2

Effective interest rate

A measure of the mean average interest rate payable on net debt associated with South West Water Limited's group of companies, including Bristol Water plc, which excludes interest costs not directly associated with net debt. This measure is presented to assess and monitor the relative cost of financing for South West Water.

	2023 £m	2022[1] £m
Net finance costs before non-underlying items (note 8)	**136.6**	93.7
Remove: net finance income before non-underlying items not associated with South West Water Limited's group of companies	**8.7**	6.7
Net finance costs before non-underlying items associated with South West Water Limited's group of companies	**145.3**	100.4
Net interest on retirement benefit obligations associated with South West Water Limited's group of companies	**1.6**	0.2
Capitalised interest (note 8)	**5.0**	1.3
Net finance costs for effective interest rate calculation	**151.9**	101.9
Group net debt / (cash) (opening) (note 38)	**2,682.9**	(64.3)
Remove: opening net debt not associated with South West Water Limited's group of companies	**(43.8)**	2,658.5
Opening net debt for calculation	**2,639.1**	2,594.2
Group net debt / (cash) (opening) (note 38)	**2,965.4**	2,682.9
Remove: closing net debt not associated with South West Water Limited's group of companies	**(100.1)**	(43.8)
Closing net debt for calculation	**2,865.3**	2,639.1
Average net debt (opening net debt + closing net debt divided by 2)	**2,752.2**	2.616.7
Effective interest rate (%)	**5.5**	3.9

1. 2021/22 water business comparator of 3.7% re-analysed to provide comparative performance under post-integration South West Water Limited group of companies' structure

Effective cash cost of interest

Effective cash cost of interest for South West Water Limited's group of companies is based on the effective interest cost calculation above, but excludes finance costs that are not paid in cash, but accrete to the carrying value of debt (principally the inflationary impact of indexation on index-linked debt).

	2023 £m	2022 £m
Net finance costs for effective interest rate calculation (as above)	**151.9**	101.9
Remove non-cash interest accrued (income statement indexation charge)	**(66.8)**	(35.7)
Net finance costs for effective cash cost of interest calculation	**85.1**	66.2
Opening net debt (as above)	**2,639.1**	2,594.2
Closing net debt (as above)	**2,865.3**	2,639.1
Average net debt (opening net debt + closing net debt divided by 2)	**2,752.2**	2.616.7
Effective cash cost of interest (%)	**3.1**	2.5

Underlying interest cover

Underlying net finance costs (excluding pensions net interest cost) divided by operating profit before non-underlying items.

	2023 £m	2022 £m
Net finance costs after non-underlying items (note 8)	**136.6**	93.7
Net interest on retirement benefit obligations (note 8)	**2.0**	0.6
Net finance costs for interest cover calculation	**138.6**	94.3
Operating profit before non-underlying items (see 'Underlying earnings' above)	**153.1**	237.2
Interest cover (times)	**1.1**	2.5

EBITDA dividend cover

Underlying EBITDA for the Group divided by proposed combined interim and final dividends.

	2023 £m	2022 £m
Underlying EBITDA (see 'Underlying earnings' above)	**307.8**	383.9
Proposed dividends (note 12)	**111.7**	102.0
EBITDA dividend cover (times)	**2.8**	3.8

Group dividend cover

Proposed dividends divided by profit for the year before non-underlying items and deferred tax.

	2023 £m	2022 £m
Proposed dividends (note 12)	**111.7**	102.0
Profit for the year attributable to ordinary shareholders	**0.1**	15.4
Deferred tax charge before non-underlying items (note 9)	**(0.9)**	8.9
Non-underlying items after tax in profit for the year (note 6)	**20.0**	114.1
Adjusted profit for dividend cover calculation	**19.2**	134.8
Dividend cover (times)	**0.2**	1.4

Capital investment

Property, plant and equipment and intangible asset additions. The measure is presented to assess and monitor the total capital investment by the Group.

	2023 £m	2022 £m
Additions to property, plant and equipment (note 17)	**353.7**	237.3
Additions to intangible assets (note 16)	**4.6**	3.6
Capital investment	**358.3**	240.9

Capital payments

Payments for property, plant and equipment (PPE) and intangible asset additions, net of proceeds from sale of PPE and intangible assets. The measure is presented to assess and monitor the net cash spend on PPE and intangible assets.

	2023 £m	2022 £m
Cash flow statements: purchase of property, plant and equipment	**326.6**	225.6
Cash flow statements: purchase of intangible assets	**4.6**	3.4
Cash flow statements: proceeds from sale of property, plant and equipment	**(0.7)**	(1.4)
Capital payments relating to the Group	**330.5**	227.6

Return on capital employed

The total of underlying operating profit divided by capital employed (net debt plus total equity invested). An average value for this metric is part of the long-term incentive plan for Directors under the 2020 LTIP award.

	2023 £m	2022[1] £m
Capital employed (opening):		
Net debt (note 38)	**2,682.9**	2,198.6
Total equity invested (notes 33, 34, 35)	**551.9**	250.9
Opening capital employed for return on capital employed calculation	**3,234.8**	2,449.5
Capital employed (closing):		
Net debt (note 38)	**2,965.4**	2,233.8
Total equity invested (notes 33, 34, 35)	**554.2**	295.9
Closing capital employed for return on capital employed calculation	**3,519.6**	2,529.7
Underlying operating profit (see 'Underlying earnings' above)	**153.1**	214.5
Capital employed for return on capital employed calculation (opening capital employed + closing capital employed divided by 2)	**3,377.2**	2,486.6
Return on capital employed (%)	**4.5**	8.6

1. 2022 presentation reflects South West Water return on capital employed, re-analysed on an average capital employed basis

Return on Regulated Equity (RoRE)

This is a key regulatory metric which represents the returns to shareholders expressed as a percentage of regulated equity.

Returns are made up of a base return (set by Ofwat, the water business regulator, at c.3.9% for South West Water and c.4.4% for Bristol Water for the period 2020-25) plus totex outperformance, financing outperformance and ODI outperformance. Returns are calculated post tax and post sharing (only a proportion of returns are attributed to shareholders and shown within RoRE). The three different types of return calculated and added to the base return are:

- Totex outperformance – totex is defined below and outperformance is the difference between actual reported results for the regulated business compared to the Final Determination (Ofwat published document at the start of a regulatory period), in a constant price base
- Financing outperformance – is based on the difference between a company's actual effective interest rate compared with Ofwat's allowed cost of debt
- ODI outperformance – the net reward or penalty a company earns based on a number of different key performance indicators, again set in the Final Determination.

Regulated equity is a notional proportion of regulated capital value (RCV which is set by Ofwat at the start of every five-year regulatory period, adjusted for actual inflation). For 2020-25, the notional equity proportion is 40.0%.

References are made to Ofwat RoRE and Watershare RoRE which utilise differing inflation assumptions and the disclosure of tax.

Further information on this metric can be found in South West Water and Bristol Water's annual performance report and regulatory reporting, published in July each year.

Totex

Operating costs and capital expenditure of the regulated water and wastewater business (based on the Regulated Accounting Guidelines).

Outcome Delivery Incentives (ODIs)

ODIs are designed to incentivise companies to deliver improvements to service and outcomes based on customers' priorities and preferences. If a company exceeds these targets a reward can be earned through future higher revenues. If a company fails to meet them, they can incur a penalty through lower future allowed revenues.

Regulatory Capital Value (RCV)

RCV has been developed for regulatory purposes and is primarily used in setting price limits.

RCV is widely used by the investment community as a proxy for the market value of the regulated business and forms part of covenant debt limits.

Shadow RCV reflects the addition of anticipated regulatory adjustments which amend RCV at the end of a regulatory period. These changes are accrued due to performance through ODIs, changes in levels of totex expenditure, changes in inflation rates and other regulatory adjustments.

Five-year financial summary

	Continuing operations[1]				Total Group	
	2023 £m	2022 £m	2021 £m	2020 £m	2020 £m	2019 £m
Income statement						
Revenue before non-underlying items	**825.0**	792.3	644.6	636.7	1,389.9	1,478.2
Operating profit before non-underlying items	**153.1**	237.2	215.3	245.5	361.5	351.0
Net finance costs before non-underlying items	**(136.6)**	(93.7)	(58.3)	(62.5)	(88.7)	(83.2)
Share of profit in joint ventures	**0.3**	–	–	–	14.8	12.4
Profit before tax and non-underlying items	**16.8**	143.5	157.0	183.0	287.6	280.2
Net non-underlying items before tax	**(25.3)**	(15.8)	(24.9)	10.1	13.9	(19.9)
Taxation charge	**8.9**	(112.1)	(24.8)	(70.6)	(95.2)	(37.7)
Profit for the year	**0.4**	15.6	107.3	122.5	206.3	222.6
Attributable to:						
Ordinary shareholders of the parent	**0.1**	15.4	107.5	116.6	200.4	214.3
Perpetual capital security holders	**–**	–	–	7.0	7.0	8.6
Non-controlling interests	**0.3**	0.2	(0.2)	(1.1)	(1.1)	(0.3)
Dividends proposed/declared	**111.7**	102.0	91.8	184.3	184.3	172.7
Earnings per ordinary share (basic):						
From continuing and discontinuing operations						
Earnings per share	**–**	4.9p	25.5p	27.7p	47.7p	51.1p
Deferred tax before non-underlying items	**(0.3p)**	2.6p	1.6p	2.4p	7.9p	3.1p
Non-underlying items (net of tax)	**7.6p**	36.5p	4.8p	5.3p	6.9p	3.6p
Non-controlling interests' share of non-underlying items	**–**	–	–	(0.2p)	(0.2p)	–
Adjustment for full year depreciation charge in the Disposal Group	**–**	–	–	–	(0.6p)	–
Proportional adjustment on perpetual capital returns	**–**	–	–	–	–	–
Earnings per share before non-underlying and deferred tax	**7.3p**	44.3p	31.9p	35.2p	61.7p	57.8p
Declared dividends per share	**42.73p**	38.53p	21.74p	43.77p	43.77p	41.06p

	2023 £m	2022 £m	2021 £m	2020 £m	2019 £m
Capital expenditure					
Acquisitions (including investment in joint ventures)	**–**	425.1	–	–	54.8
Property, plant and equipment	**353.7**	237.3	168.3	326.8	387.2
Balance sheet					
Non-current assets	**4,743.0**	4,527.0	3,277.1	3,226.0	5,364.5
Net current assets[2]	**87.0**	389.5	2,919.1	2,595.8	583.9
Non-current liabilities	**(3,704.8)**	(3,641.9)	(3,211.4)	(4,109.7)	(4,268.6)
Net assets	**1,125.2**	1274.6	2,984.8	1,712.1	1,679.8
Number of employees (average full time equivalent for year)					
Water	**2,639**	2,394	1,745	1,623	1,616
Waste management	**–**	–	–	2,986	3,426
Non-household retail	**158**	177	160	143	104
Other businesses	**67**	65	82	101	93
	2,864	2,636	1,987	4,853	5,239

1. Continuing operations comparative values for 2020 and 2021 are presented excluding discontinued operations following the sale of Viridor (with associated assets held for sale at March 2021, resulting in no 'Total Group' comparative for this period). Results for 2022 and 2023 reflect the current Group totals, but remain classified as 'Continuing operations' in this table for comparative purposes.
2. Net current assets for 2020 includes assets held for sale of £2,675.3 million and liabilities directly associated with assets classified as held for sale of £756.3 million.

Glossary

C-MeX	customer measure of experience, a mechanism to incentivise water companies to provide an excellent customer experience for residential customers, across both the retail and wholesale parts of the value chain
CPI	consumer price index, a measure of inflation in a representative sample of retail goods and services using a geometric mean and excluding e.g. housing costs
CPIH	consumer price index, a measure of inflation in a representative sample of retail goods and services using a geometric mean, including owner occupiers' housing costs
DNV	an independent management consultancy specialising in technical assurance in the utility sector
EBITDA	earnings before interest, tax, depreciation and amortisation
ESG	environmental, social and governance
Fair Tax Mark	an independent certification scheme which recognises organisations that demonstrate they are paying the right amount of corporation tax at the right time. In December 2018, Pennon became the first water services and waste management utility to receive it (see page 47)
GHG	greenhouse gases (see page 67)
HomeSafe	our health & safety improvement programme (see page 34 and 35)
K7	the current regulatory price review period
KPI	key performance indicator, our measures of business performance against the key targets monitored by Board and Pennon Executive (see page 17)
LTIFR	lost time injury frequency rate
ODI	outcome delivery incentives, 15 of which are common across all water companies while others are bespoke to South West Water (see page 17)
Ofwat	The Water Services Regulation Authority, or Ofwat, is the body responsible for economic regulation of the privatised water and sewerage industry in England and Wales
ROCE	return on capital employed
RoRE	return on regulated equity
RPI	retail price index, a measure of inflation in a representative sample of retail goods and services using an arithmetic mean
STEM	science, technology, engineering and mathematics
Sustainable Financing Framework	the way we link financial impacts with sustainability impacts; the Framework aligns with the Green Bond Principles, the Social Bond Principles and the Green Loan Principles (see page 48)
TCFD	Task force on climate-related financial disclosures
Totex	total expenditure
TUPE	Transfer of Undertakings (Protection of Employment) Regulations 2006 as amended
WaterShare	the programme through which we shared the benefits of outperformance against our 2015-20 business plan targets with water customers
WaterShare+	the enhanced benefit sharing mechanism introduced for water customers under our 2020-25 New Deal business plan (see page 27)
WaterShare+ Advisory Panel	established to protect the interests of our customers. The Panel provides an independent review of our business plan commitments and Board pledges.

Shareholder information

Financial calendar, including Dividend Reinvestment Plan (DRIP) alternative

Financial year end	31 March
Full Year Results 2022/23	01 June 2023
Annual Report and Accounts Published	19 June 2023
Annual General Meeting 2023	20 July 2023
Ordinary shares quoted ex-dividend	20 July 2023*
Record date for final dividend	21 July 2023*
Final date for receipt of DRIP applications	10 August 2023*
Final dividend payment date	04 September 2023*
Trading Statement	05 October 2023
PR24 - Spotlight presentation and Q&A	05 October 2023
Half Year Results 2023/24	29 November 2023
Ordinary shares quoted ex-dividend	25 January 2024
Record date for interim dividend	26 January 2024
Final date for receipt of DRIP applications	15 March 2024
Trading Statement	28 March 2024
Interim dividend payment date	05 April 2024
Full Year Results 2023/24	21 May 2024

* Subject to obtaining shareholder approval at the 2023 Annual General Meeting.

Shareholder analysis at 31 March 2023

Number of holding of shares	Number of shareholders	% of total shareholders	% of ordinary shares
1-100	2,651	17.15	0.03
101-1,000	7,561	48.91	1.39
1,001-5,000	4,334	28.04	3.45
5,001-50,000	649	4.198	2.97
50,001-100,000	70	0.453	1.96
100,001+	194	1.663	90.20
	15,459		

	Number of accounts	% of total accounts	% of total shares
Individuals	14,706	91.2090	6.3889
Companies	656	4.2434	82.7438
Trust companies (pension funds etc.)	6	0.0388	0.0041
Banks and nominees	91	0.2458	8.4790
	15,459		

Major shareholdings

Investors who have notified interests in the issued share capital of the Company pursuant to the Financial Conduct Authority's Disclosure Guidance and Transparency Rules are as follows. This includes all notifications up to 30 May 2023 (being a date not more than one month prior to the date of the Company's Notice of Annual General Meeting).:

	Number of voting rights (direct and indirect)	% of voting rights	Date notified
BlackRock Inc	16,413,878	5.82	25 /08/21
Lazard Asset Management LLC	13,443,374	5.076	18/05/22
Pictet Asset Management	13,035,981	4.989	24/02/23
Impax Asset Management	12,663,862	4.736	16/02/22

Registrar

All enquiries concerning shareholdings including notification of change of address, loss of a share certificate or dividend payments should be made to the Company's registrar, Link Asset Services, who can be contacted as follows:

Link Asset Services
Pennon Group Share Register 10th Floor
Central Square
29 Wellington Street Leeds
LS1 4DL

Telephone: 0371 664 9234 (calls are charged at standard geographic rate and will vary by provider).

Lines are open 8.30am-5.30pm Monday-Friday, excluding public holidays in England and Wales.

Overseas telephone: +44 371 664 9234
(calls outside the United Kingdom will be charged at the applicable international rate).

Email: pennon@linkgroup.co.uk
Website: www.signalshares.com

ShareGift service

Through ShareGift, an independent charity share donation scheme, shareholders who only have a small number of shares with a value that makes it uneconomical to sell them can donate such shares to charity. Donations can be made by completion of a simple share transfer form which is available from the Company's registrar, Link Asset Services, or by contacting ShareGift on 020 7930 3737 (www.sharegift.org).

Individual savings accounts

Shareholders may gain tax advantages by holding their shares in the Company in an Individual Savings Account (ISA).

Dividend Reinvestment Plan (DRIP)

Subject to obtaining shareholder approval at the 2023 Annual General Meeting for the payment of a final dividend for the year ended 31 March 2023, full details of the DRIP and how to participate will be published on the Company's website at www.pennon-group.co.uk/dividends/dividend-reinvestment-plan-drip.

The full timetable for offering the DRIP is given opposite.

The DRIP provides shareholders with an opportunity to invest the cash dividend they receive on their Pennon Group plc shares to buy further shares in the Company at preferable dealing rates.

Corporate information

Registered office

Peninsula House Rydon Lane Exeter
Devon EX2 7HR

Company registration number: 2366640

Company Secretary

Andrew Garard

Corporate brokers

Barclays Bank PLC
Morgan Stanley & Co. International plc

Independent auditors

Ernst & Young LLP

Online portfolio service

The online portfolio service provided by Link Asset Services gives shareholders access to more information on their investments. Details of the portfolio service are available online at www.signalshares.com.

Electronic communications

The Company has passed a resolution which allows it to communicate with its shareholders by means of its website.

Shareholders currently receiving a printed copy of the annual report who now wish to sign up to receive all future shareholder communications electronically can do so by registering with Link Asset Services' share portal.

Go to http://www.signalshares.com to register, select 'Account Registration' and then follow the on-screen instructions by inputting your surname, your Investor Code (which can be found on your proxy form) and your postcode, as well as entering an email address and selecting a password.

By registering to receive your shareholder communications electronically, you will also automatically receive your dividend confirmations electronically.

Electronic proxy voting

Pennon encourages the use of electronic proxy voting and no longer provides paper proxy forms alongside the AGM Notice. We believe that is both more efficient and consistent with our important environmental sustainability responsibilities and objectives.

You may register your proxy votes via www.signalshares.com.

Registering your vote electronically is entirely secure and ensures the privacy of your personal information. Alternatively, if you wish to vote by post you may request a hard copy proxy form by contacting our registrar, Link Asset Services. Contact details are provided above.

Pennon's website

http://www.pennon-group.co.uk provides news and details of the Company's activities plus links to its subsidiaries' websites.

The Investor Information section contains up-to-date information for shareholders including detailed share price information, financial results, dividend payment dates and amounts, and stock exchange announcements. There is also a comprehensive shareholder services section which includes information on buying, selling and transferring shares, and how to notify a change in personal circumstances, for example, a change of address.

Beware of share fraud

The following is taken from the ScamSmart section of the Financial Conduct Authority's website (www.fca.org.uk/scamsmart).

Fraudsters use persuasive and high-pressure tactics to lure investors into scams. They may offer to sell shares that turn out to be worthless or non-existent, or to buy shares at an inflated price in return for an upfront payment.

While high profits are promised, if you buy or sell shares in this way you will probably lose your money.

How to avoid share fraud

- Keep in mind that firms authorised by the Financial Conduct Authority (FCA) are unlikely to contact you out of the blue with an offer to buy or sell shares.
- Do not get into a conversation; note the name of the person and firm contacting you and then end the call.

Check the Financial Services Register from http://www.fca.org.uk to see if the person and firm contacting you is authorised by the FCA.

- Beware of fraudsters claiming to be from an authorised firm, copying its website or giving you false contact details.
- Use the firm's contact details listed on the Register if you want to call it back.
- Call the FCA on 0800 111 6768 if the firm does not have contact details on the Register or you are told they are out of date.

Search the FCA Warning List of unauthorised firms at www.fca.org.uk/scamsmart.

Consider that if you buy or sell shares from an unauthorised firm you will not have access to the Financial Ombudsman Service or Financial Services Compensation Scheme. Seek impartial advice from a financial adviser before you make an investment.

- Remember: if it sounds too good to be true, it probably is!

5,000 people contact the Financial Conduct Authority about share fraud each year, with victims losing an average of £20,000.

Report a scam

If you are approached by fraudsters, please tell the FCA using the share fraud reporting form at http://www.fca.org.uk/scams where you can find out more about investment scams. You can also call the FCA Consumer Helpline on 0800 111 6768.

If you have already paid money to share fraudsters you can report this at any time to Action Fraud using their Online Fraud Report Tool at www.actionfraud.police.uk/reporting-fraud-and-cyber-crime or by calling 0300 123 2040.

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The paper is Carbon Balanced with the World Land Trust, an international conservation charity, who offset carbon emissions through the purchase and preservation of high conservation value land.

Through protecting standing forests, under threat of clearance, carbon is locked in that would otherwise be released. These protected forests are then able to continue absorbing carbon from the atmosphere, referred to as REDD (Reduced Emissions from Deforestation and forest Degradation). This is now recognised as one of the most cost-effective and swiftest ways to arrest the rise in atmospheric CO_2 and global warming effects. Additional to the carbon benefits is the flora and fauna this land preserves, including a number of species identified at risk of extinction on the IUCN Red List of Threatened Species.

Consultancy and design by Black Sun Global

Pennon

Pennon Group plc

Peninsula House
Rydon Lane
Exeter
Devon
England EX2 7HR

www.pennon-group.co.uk

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