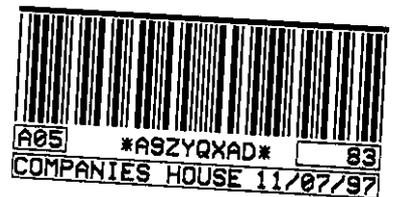
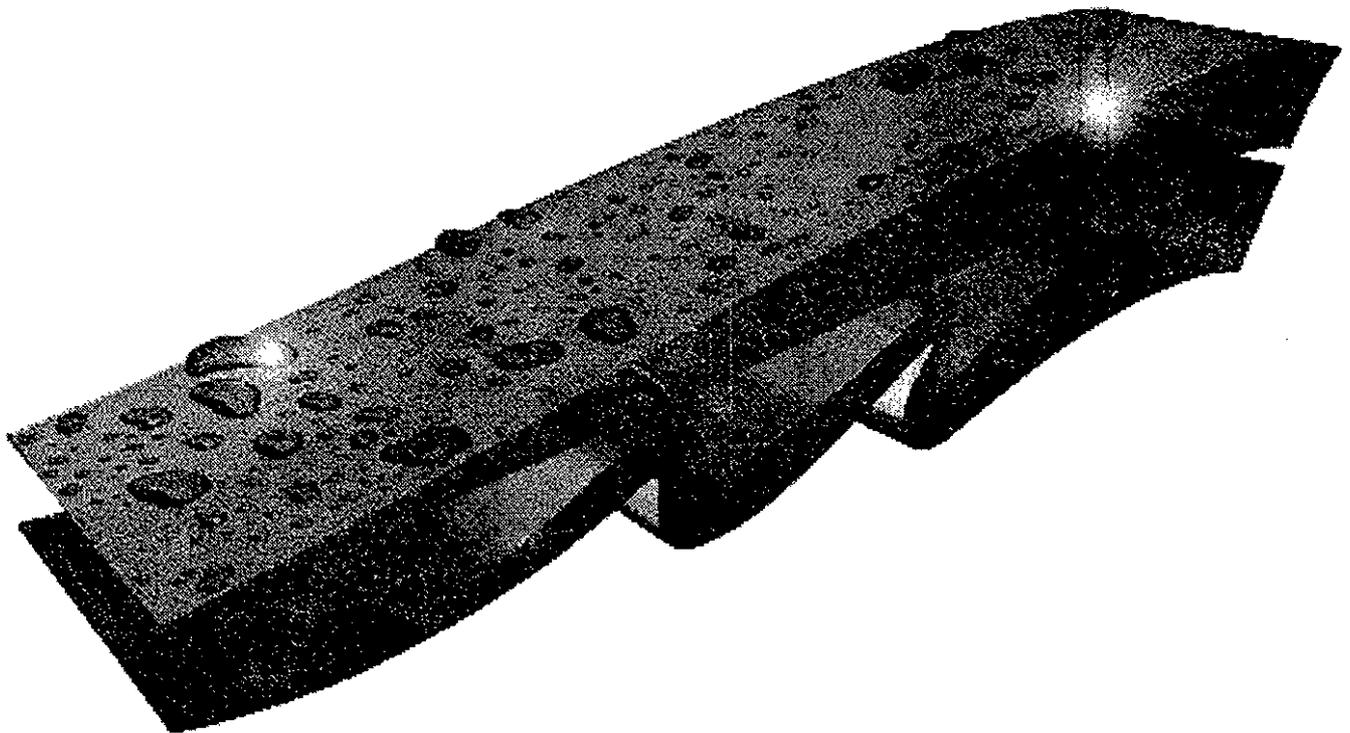


ANNUAL REPORT & ACCOUNTS 1997

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SOUTH WEST WATER PLC

South West Water Plc operates and invests primarily in the areas of water and waste engineering, waste management and environmental instrumentation.

The principal subsidiary, South West Water Services Limited, holds the water and sewerage appointments for South West England.

The non-regulated businesses include one of the top five waste disposal companies in the UK, a specialist environmental instrumentation company with leading positions in its key segments worldwide, and a leading regional construction services company.

The Group has assets of £1.7 billion and currently employs over 3,000 people.

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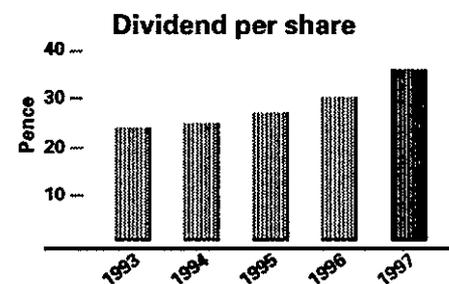
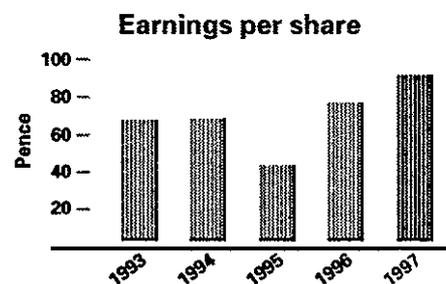
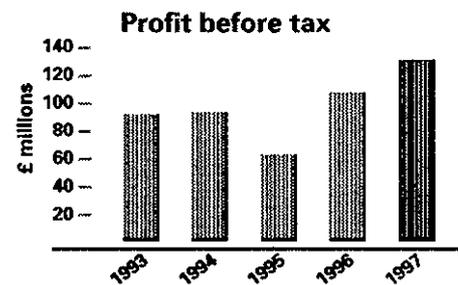
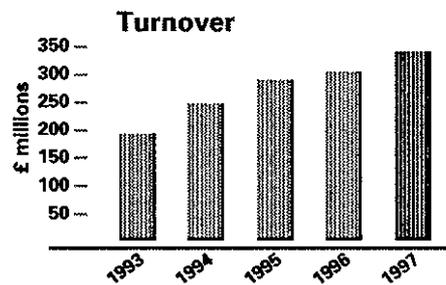


Highlights of the year

Excellent results were delivered during the year in both regulated and non-regulated businesses.

- Turnover up 9.3% to £343.6 million.
- Profit before tax up 21.5% to £132.6 million.
- Earnings per share up 18.5% to 92.1 pence.
- Full year dividend up 20.3% to 36.7 pence.
- Customer rebate of £15 per customer paid in March 1997.

Financial summary





Chairman's statement



‘ The Directors are confident that the underlying business strength of the Group will support the declared dividend policy. ’

I am pleased to be making my first statement as Chairman of South West Water Plc, having succeeded Keith Court on 1 March 1997.

1996/97 was a year of tremendous activity for the Company and, despite much of senior management's time being devoted to external matters, the performance of the various businesses improved significantly. Profit before tax rose by 21.5% to £132.6 million and earnings per share by 18.5% to 92.1p. The Directors are recommending a final dividend of 24.9p per share which, together with the interim dividend, will result in a full year dividend of 36.7p – an increase of 20.3% over last year.

The year was clearly dominated by the unsolicited approaches by Severn Trent Plc and Wessex Water Plc and the reference of their proposed bids to the Monopolies and Mergers Commission. An enormous amount of time and money was devoted to dealing with these proposals and the MMC investigation. This ultimately resulted in the President of the Board of Trade disallowing the proposed bids which both secured the independence of the Company, and had wider implications for the water sector. The principle of comparative competition and South West Water's value as a comparator were both upheld.

Water and sewerage business

South West Water Services Limited improved customer service and continued to deliver efficiency improvements greater than implicit in the 1995 MMC price determination.

The most visible demonstration of customer focus was the payment of a £15 rebate per customer in March 1997 which followed the £10 rebate in July 1996.

The ongoing capital programme and improvement in operating practices led to further benefits in product quality and reliability, customer service and environmental protection – all described in more detail in the Operating Review.

Following an unprecedented series of droughts and a very dry spring, water resource levels continue to be of concern. Many different actions have been taken to provide higher levels of security of water supplies and these will continue to develop and refine the water supply strategy.

Non-regulated businesses

The Enterprise Division strengthened its focus on the core activities of waste management and disposal, environmental instrumentation and construction services. The Company's interest in Westcountry Television and its Peninsula Park office campus were both sold at a profit.

Haul Waste, ELE and T J Brent all strengthened their market positions. Haul Waste commenced development of a major new landfill site in Scotland and obtained planning permission to develop two new sites in South West England.

This cluster of related, environmental businesses is making a significant and growing contribution to Group profitability, as described in the Operating Review.

Prospects

The two major factors facing the Group are the new Government's taxation policy, and the Director General's 1999 review of water and sewerage price limits.

The Board does not believe that the proposed windfall profits tax is justified, but it is recognised that it is the Government's responsibility to determine taxation requirements. The Board believes that the proposed windfall profits tax should be applied equitably, and representations have been made in this matter to the Government.

The price review will require a significant input of time and effort, and it is important that the Director General's final decision should be such as to provide the water and sewerage company with a reasonable financial position for the beginning of the new millennium.

The Directors are confident that the underlying business strength of the Group will support the declared dividend policy of 8% per annum real growth, in the absence of unforeseen circumstances, for the immediate future.

The impact of the potential Year 2000 problem on the Company's information technology infrastructure is being addressed and given high priority.

Board matters

The results of the Group as set out in this Report are a testament to the leadership, determination and clear strategic direction demonstrated by my predecessor, Keith Court. His unselfish decision to stay in post beyond his planned retirement date to deal with the bid situation ensured that strong representation was made which ultimately resulted in the Group retaining its independence. My Board colleagues and I pay tribute to and thank him for his significant contribution.

Tim Leader retired from the Board and his wise counsel will be missed. Stanislas Yassukovich was appointed Deputy Chairman in November 1996. Congratulations are due to Sir Simon Day on his Knighthood for political and public service.

Bruce Hewett retired as a full time Executive Director, but he remains as a Non-executive Director with a special interest in environmental matters. The search for a Group Chief Executive continues, and I anticipate that an announcement will be made in the near future.

Employees

1996/97 was a demanding and, at times, challenging year for our employees. The continued growth and success of the Group is only made possible by their individual and collective efforts. I thank them most sincerely.



K G HARVEY, CHAIRMAN
SOUTH WEST WATER PLC



OPERATING REVIEW

Water and sewerage services

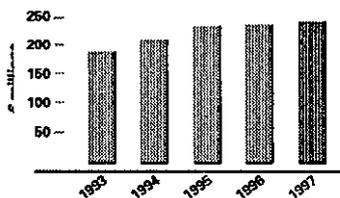
Our vision for the future

The transformation of South West Water Services Limited from a capital works focused company to a customer oriented company continued throughout the year. Despite the bid activity which prevailed, we were not deflected from our avowed intention of delivering substantial efficiencies, improved product and customer service, and enhanced guarantees for our customers.

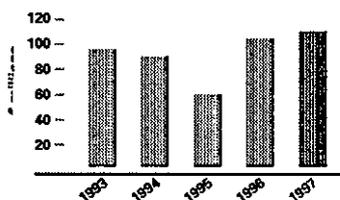
Indeed, our resolve has become even stronger and we have developed a vision for the future of the business within the overall theme of 'Working for a Better Westcountry'.

In accordance with our philosophy of sharing the benefits of improved financial and operational efficiencies with our customers, a rebate of £15 on charges for 1997/98 was made. This, in addition to the £10 rebate on 1996/97 charges, is a clear indication that our vision for the future is already becoming a reality.

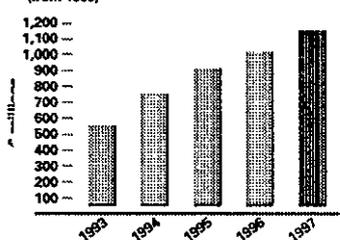
Water and sewerage services – Turnover



Water and sewerage services – Profit before tax



Water and sewerage services – Cumulative capital expenditure (from 1990)



Financial progress

Water and sewerage services turnover increased by 2.2% to £244.6 million (net of the rebate). Further operational savings of £5.1 million were achieved in 1996/97 as the company continued to drive down costs and improve efficiency. These savings were more than offset by the impact of the capital programme and customer rebate, causing operating profits to fall by 3.3%. However, the use of financing initiatives enabled the profit before tax position to rise by 6.7% to £111.7 million.

Capital expenditure for the year was £151.4 million with £79.5 million invested in water supply improvements, including mains rehabilitation, leakage control and water treatment works upgrading. Waste water services benefited from an investment of £71.9 million of which £53.7 million was invested in the company's 'Clean Sweep' bathing water improvements programme.

Customer initiatives

At the end of 1995 the water and sewerage services business initiated an extensive programme of customer benefits to help re-focus the company. During 1996/97 the company significantly enhanced its programme of customer initiatives and the local Ofwat Customer Service Committee consider it to be one of the most comprehensive, both within and outside the water industry.

During the year the company was the first to introduce voluntarily, guaranteed compensation for customers where their supplies are interrupted due to drought,

and agreed with the Director General of Water Services an amendment of its operating licence.

In addition, the company provided metered customers with the opportunity of reverting to a non-metered tariff on change of property ownership, change of tenancy or reversion of commercial premises to domestic occupancy. It also began pilot trials of budget payment units for customers who require an alternative method of paying their bills.

In order to provide consistently high standards of customer service, the company developed and introduced a 'Customer First' initiative to re-engineer customer contact processes, supported by the introduction of new information management systems.

Communication with customers was improved considerably by the launch of two mobile customer service units and all customers were provided with 'The Really Useful Handbook' containing key information on services.

The company is confident that once again many of its customer service levels will be improved or maintained when Ofwat publishes its next annual report on levels of service later this year.

Bob Baty, Managing Director of South West Water Services Limited, with a customer at one of the company's mobile customer service units.

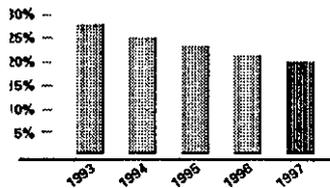


‘ The transformation of South West Water Services from a capital works focused company to a customer oriented company continued throughout the year. ’

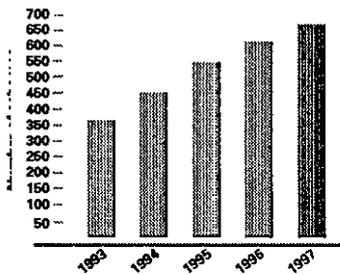


OPERATING REVIEW – WATER AND SEWERAGE SERVICES

Leakage reduction



Cumulative major capital scheme completions (from 1990)



Drinking water supplies

Water supplies were maintained throughout the region despite the low levels of reservoirs following the summer drought of 1995, apart from limited water restrictions in North Devon affecting around only 5% of customers.

A series of measures costing more than £20 million were initiated by the company in 1995 to further reinforce supplies to customers. They included the building of a series of strategic water supply links across the region and the completion of new pumped storage schemes for two of our three strategic reservoirs, Roadford in West Devon and Wimbleball on Exmoor.

Following unprecedented demands for water in 1995, the company accelerated elements of its £99 million water distribution improvement and leakage reduction programme to help conserve existing resources. Leakage from the company's pipelines has been reduced from 28% in 1992 to 21% across the region – a 25% reduction – and the company is on track to meet the target of 15% by the end of 1999. The company is currently saving around seven million gallons of water each day via its leakage reduction initiative.

Drinking water quality was at the very high level of 99.7% overall compliance. Supplies to 370,000 customers in Devon and Cornwall were enhanced by the completion of improvements to water treatment works in Plymouth, Totnes and Torrington.

The company is defending a prosecution being brought by the Secretary of State for the Environment following an outbreak of cryptosporidiosis in South Devon in 1995.

Protecting and enhancing the environment

The company's 'Clean Sweep' coastal sewage treatment improvement initiative continues to be the largest investment area, and during the year schemes were completed at St Agnes, Combe Martin and Ilfracombe at a cost of £26.2 million. By the end of the financial year 32 of the original 33 schemes were completed or under construction with a cost to date of £427 million. 56 bathing waters have now been significantly improved.

Construction began in July 1996 on the scheme for Plymouth, one of the largest in the 'Clean Sweep' programme, which will provide sewage treatment for 120,000 people for the first time.

In November 1996 plans were announced to accelerate delivery of the £20 million scheme to replace the outdated sewers and sea outfalls serving Newquay. This was another clear demonstration of the company's determination to work with others as a partner in the economic regeneration of the region, and the company plans to complete the project by the end of 1999, three years ahead of the previous timetable.

The Newquay scheme is one of 13 currently using, or planned to incorporate the use of, ultraviolet disinfection.

In addition, work continues to complete the major coastal sewage treatment schemes required to comply with the Urban Waste Water Treatment Directive by the Year 2000 at Sidmouth and Dawlish in Devon, and Camborne and Redruth in Cornwall.

The continuing upgrading of inland waste water treatment works helped the company to achieve 95.5% compliance with stringent consent standards. In tandem with providing enhanced levels of environmental protection for inland waterways, over 370 planning embargoes have been lifted since 1989 as a direct result of investment.

Awards

During the year the company won the Norsk Hydro Award for water quality improvement for the Penzance & St Ives 'Clean Sweep' scheme and the national Visa Purchasing Department of the Year award.

‘ Leakage from the company’s pipelines has been reduced from 28% to 21% across the region – a 25% reduction. ’

Seeking leaks in the still of the night.





OPERATING REVIEW – WATER AND SEWERAGE SERVICES

Research and development

Cost effective installation and operation of new clean and waste water treatment processes benefits from the company's ongoing research and technology development initiatives.

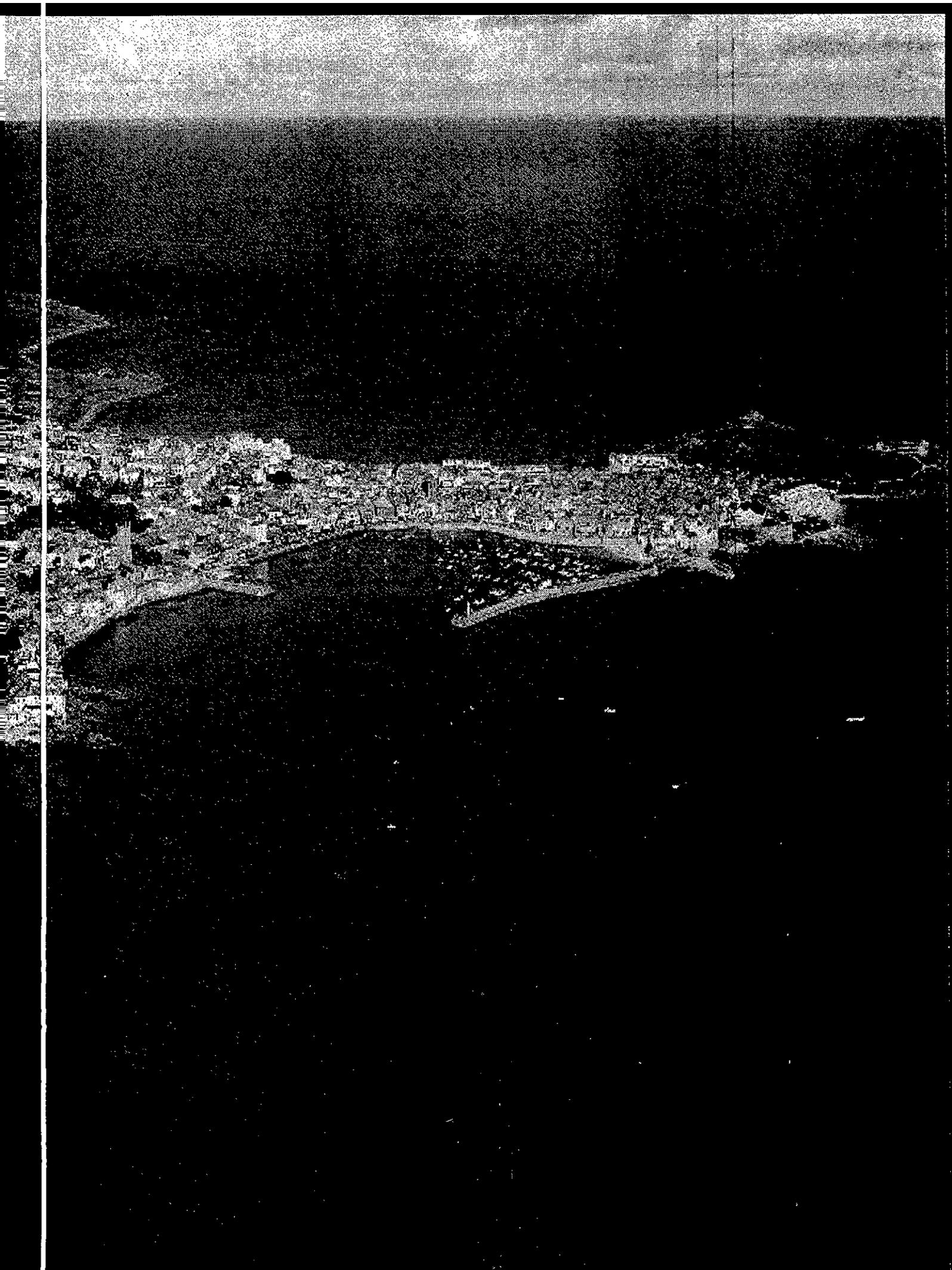
Development of clean water technology continued with the introduction of new coagulants, development of advanced dosing control techniques, together with the monitoring and evaluation of progress in membrane filtration processes.

Sludge treatment technology development will enable processing of additional quantities of sludge arising from new treatment works and the cessation of sea disposal during 1998, and the evaluation of advanced waste water treatment techniques will provide cost effective solutions to enable the company to meet the challenge of the Urban Waste Water Treatment Directive.

R J BATY
MANAGING DIRECTOR
SOUTH WEST WATER SERVICES LIMITED

*St Ives –
benefiting from
the award-
winning
Penzance & St
Ives 'Clean Sweep'
scheme.*

‘ During the
year the company
won the Norsk
Hydro Award
for water quality
improvement. ’





OPERATING REVIEW

Non-regulated businesses

A successful strategic focus

South West Water Plc has successfully built a group of related, environmental businesses, each of which has a strong position and good prospects in its respective sectors.

It continued to concentrate on the core activities of waste management (especially disposal), environmental instrumentation and construction services. During the year selective profitable disposals were made, confirming the Group's focused strategy. The non-regulated businesses continue to make a positive, growing contribution to total Group profits.

Financial progress

Non-regulated businesses turnover grew by 30.7% to £145.9 million during the year, and operating profit by 44.8% to £15.2 million (51.6% and £14.1 million after consolidating out intra-group business). Profit before tax grew from £5.1 million to £8.6 million – before business disposals. The Group disposed of its interest in Westcountry Television Limited, sold its Peninsula Park office campus in Exeter, and selectively disposed of other businesses, realising a profit of £17.5 million.

These results flow from the overall strategic focus and specific attention to margin enhancement in the key subsidiaries. They represent a major achievement over the past five years.

Waste management

During the year Haul Waste – one of the top five waste disposal companies in the United Kingdom in terms of consented landfill – commenced a project to develop and operate a new strategic landfill at Dunbar in Scotland with a capacity of 13 million cubic metres. Due to open in September 1997 the site is contracted to take a minimum of 150,000 tonnes of waste per annum from the City of Edinburgh.

Haul Waste also achieved planning permission to develop a fully engineered landfill site at Uffculme in Devon. This, coupled with the previously reported planning success at Warmwell in Dorset, increased Haul Waste's consented void capacity by five million cubic metres to 44 million cubic metres. Haul Waste is now well positioned to capitalise on the increasing shortage of landfill disposal capacity within the United Kingdom.

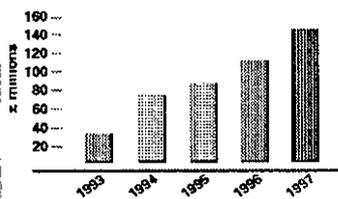
New landfill gas power generation schemes, with electricity prices guaranteed under NFFO3, were commissioned at Haul Waste's Ardley (Oxfordshire) and Horton (West Sussex) sites. Under NFFO4 contracts awarded in 1997, the company will increase its landfill gas power generation capacity from 13 to 25 megawatts. The award of the contracts to Haul Waste will see the South West Water Group as a whole generating the equivalent of nearly 80% of its electricity needs in 1998/99 compared with less than half in 1995/96.

In keeping with the policy of focusing on waste disposal and mainstream collection activities, Haul Waste sold its peripheral Bristol-area dry waste collection service, and its trade waste collection service in Devon, Cornwall and Somerset during the year, realising a profit of £1.6 million.

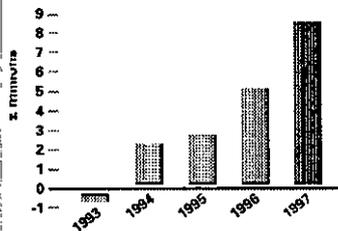
In recognition of its environmental management systems, Haul Waste gained BS7750 environmental accreditation at three locations in Devon, Somerset and Dorset. This complements Haul Waste's existing BS5750 accreditations for quality management systems.

Haul Waste showed an operating profit of £8.0 million – 19.1% of sales, compared to the previous year's figure of £5.3 million – 15.5% of sales.

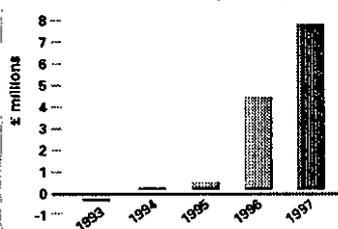
Non-regulated businesses – Turnover



Non-regulated businesses – Profit before tax (excluding business disposals)

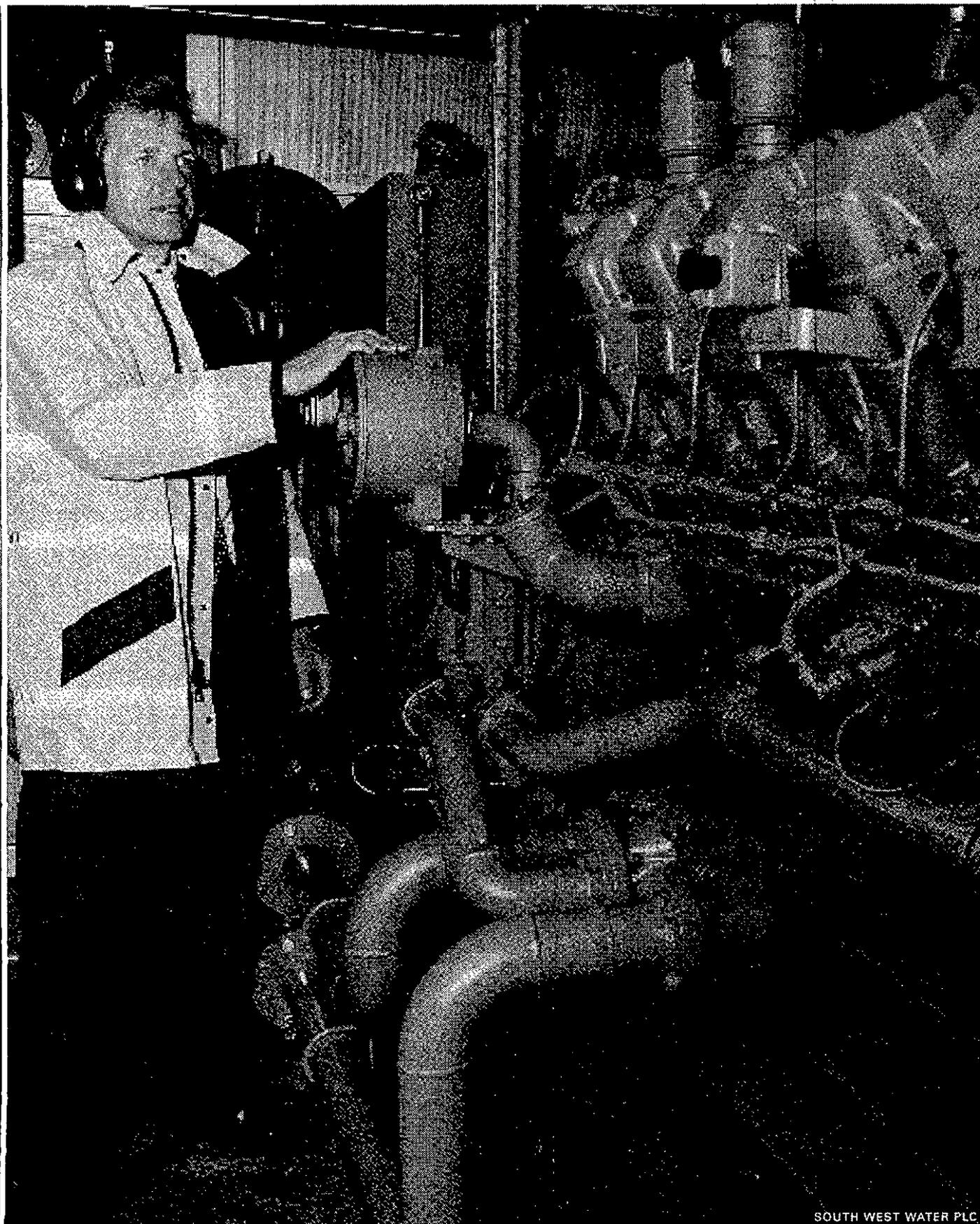


Waste management – Profit before tax (excluding business disposals)



‘ Through its carefully focused strategy, South West Water has successfully built a group of related, environmental businesses. ’

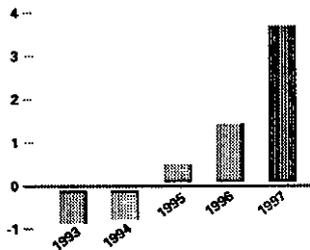
*Colin Drummond,
Managing Director
of the Enterprise
Division at the
Ardley landfill site
gas power
generation unit.*



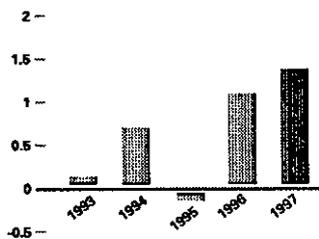


OPERATING REVIEW – NON-REGULATED BUSINESSES

Environmental instrumentation – Profit before tax (excluding business disposals)



Construction services – Profit before tax (including business disposals)



Environmental instrumentation

The ELE Group is a leading international specialist environmental instrumentation business with a 20% share of the world market in key product areas. The group trades in over 100 countries, with development and manufacturing facilities in the United Kingdom and America. It is well positioned to exploit growth opportunities from the continuing enhancement of environmental standards and infrastructure developments worldwide. During the year it maintained its successful growth pattern in both turnover and margins, despite the effect of the strength of sterling later in the year.

Throughout the year the ELE group continued to develop its share of international business, demonstrating particular strength in Latin America and the Far East. Notable new projects included a contract for the supply of laboratory equipment to the Ministry of Education in Ethiopia and a contract for four mobile laboratories in Uzbekistan.

Whilst the ELE group continues to capitalise on its well established product range and worldwide reputation, it is also pursuing an on-going programme of product development designed to preserve and enhance its strong market position. In September 1996 the ELE group acquired the assets and goodwill of Didcot Instruments, a manufacturer of environmental and meteorological sensors. It has introduced a new environmentally friendly asphalt testing system for the civil engineering market, and a new series of analysers which in conjunction with sensor development, present a comprehensive range of latest technology products for the water instrumentation market.

The ELE group continued to make significant financial progress during the year, again benefiting from specific margin enhancement initiatives, with operating profit growing to £4.0 million in 1996/97 – 10% of sales, compared to £1.7 million in 1995/96 – 5.4% of sales.

Construction services

T J Brent Limited – a market leader in construction services in South West England – continued to make substantial progress with major growth in both turnover and profit. Over one third of turnover was generated outside the Group. Engineered Products Limited, acquired in February 1996, was successfully integrated into the existing T J Brent operation and positive marketing synergies were achieved throughout the year.

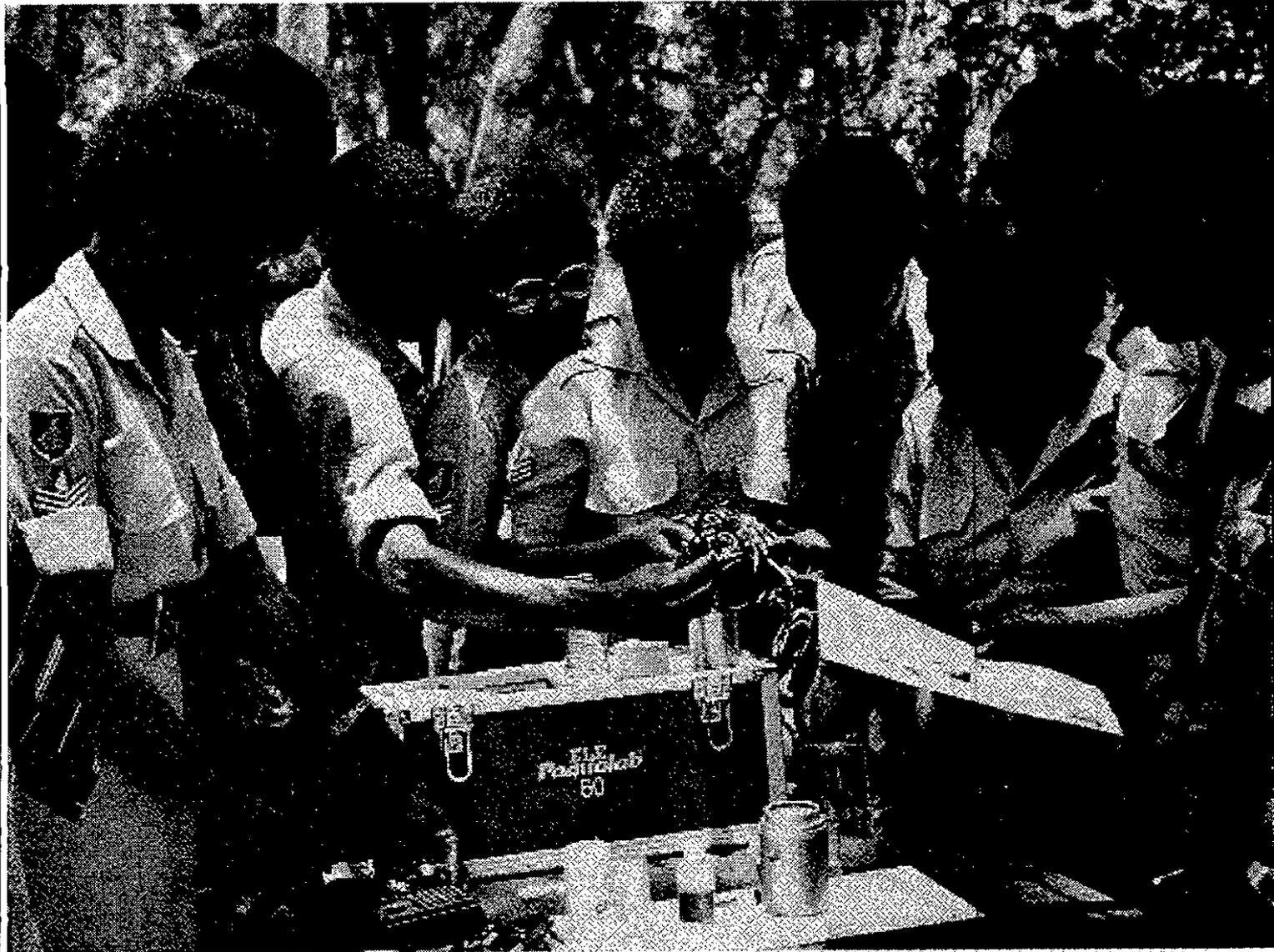
Copa, the waste water process division of T J Brent, had a very successful year with increased sales of its Biological Aerated Filter waste water treatment plant, and storm overflow improvement products.

T J Brent won a number of significant external contracts during 1996/97 including the renewal of their contract to carry out cable laying work for South Western Electricity Plc and a water mains rehabilitation contract with Wessex Water. Other major external contracts included helicopter washing facilities and term maintenance contracts at Royal Naval Air Station Culdrose in Cornwall.

As a result of the above and other projects, the company's external turnover increased to £18.7 million – 36% of annual turnover. Total operating profit rose from £1.4 million to £1.7 million.

C I J H DRUMMOND
MANAGING DIRECTOR
ENTERPRISE DIVISION

ELE Paqualabs were supplied to the Zimbabwe Army Medical Corps for use during peacekeeping missions in Mozambique and Somalia.

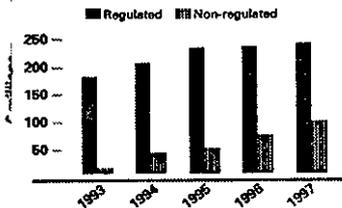


‘ The ELE Group trades in over 100 countries. ’



Financial review

Group turnover



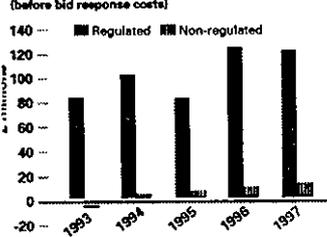
Operating profit

Group turnover for the year increased by 9.3% to £343.6 million. Turnover of the water and sewerage services business with third parties was £242.9 million, up by 2.1% on 1996. Turnover of non-regulated businesses with third parties increased by 31.5% to £100.7 million, and now forms 29% of the Group total. Total turnover for the non-regulated businesses reached £145.9 million, including £41.9 million from the waste management activities; £40.0 million from environmental instrumentation; and £51.8 million from the construction services business.

Operating costs for the year of £214.1 million increased by 18.4% influenced largely by non-regulated business growth. The total includes £5.2 million exceptional costs deemed necessary to respond to the Wessex Water and Severn Trent approaches. The proposed bids were blocked by the President of the Board of Trade in October 1996.

Operating profit was £130.2 million for 1996/97, after £5.2 million proposed bid response costs. The water and sewerage services business contributed an operating profit of £121.3 million. Non-regulated businesses contributed an operating profit of £14.1 million, up £4.8 million, or over 50%, on the profit of the previous year.

Group operating profit



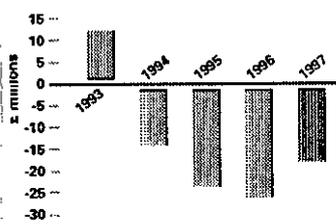
Finance costs

Gross interest payable totalled £44.7 million. Substantially all borrowings are sterling denominated. Interest receivable of £18.0 million is derived from investment of temporarily surplus funds in financial investments, and on the money market, predominantly in sterling.

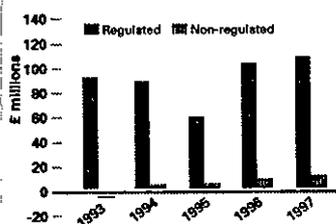
Net interest payable was £18.0 million for the year, £8.6 million lower than in 1996, benefiting from an £8.7 million advantage arising from a finance lease facility utilised during the year.

In September 1996, building on the successful extensive finance leasing facilities already arranged, a further £180 million of finance lease facilities were put in place for the purchase of plant and equipment for the water and sewerage business. These facilities, utilising standby letters of credit counter-indemnified by cash deposits, provide an added dimension to that used in conventional finance leasing. As well as allowing South West Water Services Limited to take the drawn facilities, and cash deposit, off-balance sheet, it permits immediate recognition of the economic, and cash, benefit derived from this cost effective form of finance. £65.4 million was drawn down under these facilities during 1996/97.

Group net interest receivable/(payable)



Group profit before tax



Profit before tax

Profit before tax at £132.6 million was £23.5 million, or 21.5%, ahead of 1996. Group profits in 1996/97 have benefited from a £19.2 million profit from business disposals. This includes £14.8 million from the sale of the Group's holding in Westcountry Television Limited and £2.6 million from the sale of the Peninsula Park, Exeter office campus.

Non-regulated businesses contributed a profit before tax of £26.1 million, including business disposal profits of £17.5 million, which compares with £5.1 million in 1996.

Taxation

The Group's taxation charge for the year was £14.3 million. This includes a mainstream UK corporation tax charge, though the major part remains a write-off of currently non-recoverable advance corporation tax on the current year dividends. The Group's capital investment programme continues to generate substantial capital allowances to be set against taxable profits.

The Board awaits details of the Government's proposed windfall profits tax which it believes should be applied equitably.

Dividends and retained earnings

The Directors recommend the payment of a final dividend of 24.9p per share for the year ended 31 March 1997. Together with the interim dividend of 11.8p per share paid on 7 April 1997, this makes a total dividend for the year of 36.7p per share, an increase of 20.3% on the dividend for 1996.

Construction of the 'Clean Sweep' scheme for Ilfracombe, where the treatment plant has been substantially funded through finance leasing.



Ken Hill,
Group Director of Finance, South West Water Plc

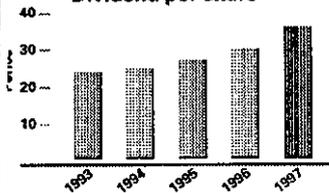




FINANCIAL REVIEW

‘ The increased dividend for 1996/97 signifies the introduction of an enhanced dividend policy. ’

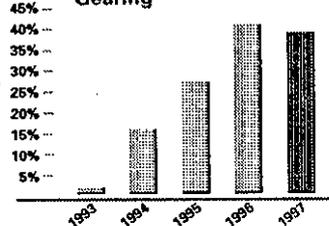
Dividend per share



The increased dividend for 1996/97 signifies the introduction of an enhanced dividend policy. The Directors intend, in the absence of unforeseen circumstances, to continue with this policy for the immediate future. The total cost of the interim and recommended final dividend of the Company is £59.3 million (including advance corporation tax).

The dividend paid by South West Water Services Limited to the Company for 1996/97 amounted to £56.1 million.

Gearing



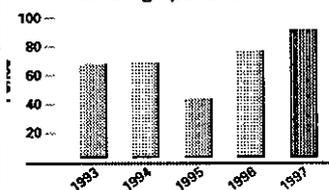
Investment

Capital expenditure by the Group on tangible fixed assets was £157.2 million (1996 £110.3 million) of which £151.4 million was for the water and sewerage services business.

Business disposals during the year generated a £31.9 million cash inflow (1996 £0.4 million).

In the opinion of the Directors the current market value of land and buildings is not significantly different from the holding cost shown in the financial statements.

Earnings per share



Financing

Cash flow from operating activities has improved to £155.9 million (1996 £142.5 million). Capital expenditure and financial investment cash outflow accelerated from £106.3 million in 1996 to £141.6 million in 1997. Overall cash outflow by the Group, before the use of liquid resources and financing, was £22.7 million (1996 £117.3 million).

During the year £65.4 million of finance lease facilities were drawn down, and £52.7 million was placed on deposit with financial institutions, as part of the financing initiative referred to in note 6 to the financial statements. There were no other material long term borrowings during the year.

At 31 March 1997 loan and finance lease obligations were £543.5 million and the Group held current asset investments and cash of £187.7 million. Net borrowings, which increased by £11.0 million during the year to £355.8 million, represent 39% of shareholders' funds (1996 41%).

At 31 March 1997 the Group had finance lease facilities in place and undrawn totalling £128 million and uncommitted short-term borrowing facilities of around £300 million.

The balance between fixed and floating rate debt and current asset investments is varied by means of interest rate swaps and is aimed at minimising interest rate exposure and ensuring that at least 50% of net debt is at fixed interest rates. The debt maturity profile is shown in note 26 to the financial statements. Borrowings to fund regulated activities are ring-fenced from the rest of the Group. Current asset investments derived therefrom are similarly ring-fenced.

The borrowing powers of the Directors are limited to two and a half times capital and reserves, as defined in the Company's Articles of Association. At 31 March 1997 the limit was £2.3 billion. The Directors confirm that the Group can meet its short-term requirements from the existing borrowing facilities without breaching covenants or other borrowing restrictions.

Share capital

During the year the issued ordinary share capital increased from £127.4 million to £129.1 million largely as a result of shares issued under the Company's scrip dividend alternative and the Sharesave and Executive Share Option Schemes.

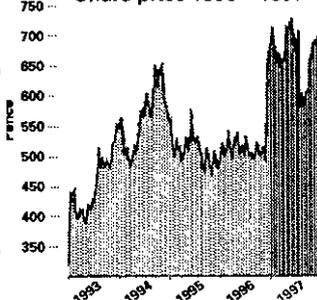
Shareholders' return

The dividend of 36.7p is paid out of earnings per share of 92.1p. On a net basis, the cover for payment of dividends is 2.5 times. There would be no significant dilution of earnings per share if the outstanding shares which might be issued in respect of the Company's share option schemes had been in issue during the year.

The Company's share price started the year at 677p and was 669p at 31 March 1997. The value of net assets per share at book value, at 31 March 1997, was 709p.

K L HILL
GROUP DIRECTOR OF FINANCE
SOUTH WEST WATER PLC

South West Water Share price 1993 - 1997



Board of Directors

Kenneth George Harvey

BSc, CEng, FIEE, CIMgt (56)

Non-executive Chairman

was appointed on 1 March 1997. He was formerly chairman and chief executive of NORWEB Plc. He was chairman of National Grid Holdings in 1995 and was previously deputy chairman of London Electricity and earlier its engineering director. He is a Non-executive director of several other companies.

Stanislas Michael Yassukovich

CBE (62)

Non-executive Deputy Chairman

was appointed on 16 November 1992 and became Deputy Chairman on 13 November 1996. He is chairman of Easdaq SA, Hemingway Properties Plc and of Flextech Plc, vice chairman of Bristol & West Building Society, director of Henderson Plc and of several other companies. He was formerly chairman of Merrill Lynch Europe and Middle East. He has been a deputy chairman of the Stock Exchange and from 1988 to 1991 was chairman of the Securities Association.

Robert John Baty

CEng, FICE, FCIWEM, MIMgt, ACI Arb, FIWO (53)

Managing Director, South West Water Services Limited

was appointed on 1 March 1996. He was formerly engineering and scientific director of South West Water Services Limited having joined South West Water Authority in 1988. Previously he held engineering and operational appointments with North West Water Authority.

Colin Irwin John Hamilton Drummond

MA, MBA (46)

Managing Director, Enterprise Division

was appointed on 1 April 1992. Prior to joining the Company he was a divisional chief executive of Coats Viyella, having previously been corporate development director of Renold plc, a strategy consultant with the Boston Consulting Group and an official of the Bank of England.

Kenneth Leslie Hill

CPFA (56)

Group Director of Finance

was appointed on 21 September 1989. He is a public finance accountant with wide experience in the water industry. Prior to joining the Company he was finance director of Severn Trent Water. He is a City Disputes panellist.

Sir Geoffrey Howes Chipperfield

KCB (64)

Non-executive Director

was appointed on 1 October 1993. He was the permanent secretary and chief executive of PSA Services from 1991 and previously he was permanent secretary in the Department of Energy. He is chairman of the Energy Advisory Panel of the Department of Trade and Industry, chairman of the British Cement Association and deputy pro-chancellor of University of Kent.

Sir Simon James Day

MA (62)

Non-executive Director

was appointed on 1 September 1989 and was a member of South West Water Authority from October 1983. He was vice chairman of the Association of County Councils and is a member of the Committee of the Regions of the European Union. He is a member and former leader of Devon County Council and is chairman of governors of Bicton College of Agriculture.

Alan Thomas Fletcher

MA (62)

Non-executive Director

was appointed on 26 May 1993. He is managing partner of Rubicon Partners, chairman of Vector Industries Limited, deputy chairman of Shepherd Building Group and a director of several other companies. Formerly he was chairman and chief executive of the Wilkinson Sword Group and chief operating officer of Swedish Match.

Bruce Alexander Ogston Hewett

BSc(Eng), MSc, Eurlng, CEng, FICE, FCIWEM, FIMgt (61)

Non-executive Director

was appointed on 1 April 1993 as Director of Technical and Environmental Affairs. On his retirement from this executive position on 31 March 1997 he became a Non-executive Director. He has over 30 years' experience in the water industry, including nine years with international consulting engineers and has held senior appointments with Southern Water Plc, including managing director of Southern Water Services Limited. He is a member of Eureau Commission 3 and the British Committee of the International Water Supply Association.

Committees of the Board

Audit

Sir Geoffrey H Chipperfield (Chairman)
Sir Simon J Day
A T Fletcher

Environment

B A O Hewett (Chairman)
R J Baty
C I J H Drummond

Finance

K G Harvey (Chairman)
Sir Simon J Day
A T Fletcher
K L Hill
S M Yassukovich

Nomination

S M Yassukovich (Chairman)
Sir Geoffrey H Chipperfield
A T Fletcher
K G Harvey

Remuneration

A T Fletcher (Chairman)
Sir Geoffrey H Chipperfield
K G Harvey

Company secretary and registered office

R C Milligan,
Pentinsula House, Rydon Lane,
Exeter, EX2 7HR.
Registered in England No 2366640

Auditors

Price Waterhouse,
Chartered Accountants,
31 George Street, Bristol, BS1 5QD.

Registrars

Lloyds Bank Plc,
Lloyds Bank Registrars,
54 Pershore Road South,
Birmingham, B30 3EP.



Report of the Directors

The Directors of South West Water Plc ('the Company') present their eighth Annual Report, in respect of the year ended 31 March 1997, together with the audited Financial Statements of the Company for that year.

The Financial Statements will be laid before the shareholders at the eighth annual general meeting of the Company, to be held on 29 July 1997, notice of which is enclosed with this Report.

Principal activities

The principal activities of the Company and its subsidiaries ('the Group') continued to be the provision of water and waste engineering, waste management and environmental instrumentation. The activities are described in more detail in the Operating Reviews.

Financial results and dividend

Group profit on ordinary activities after taxation was £118.3 million. The Directors recommend a final dividend of 24.9p per ordinary share, making a total for the year of 36.7p, the cost of which would be £47.4 million, leaving retained profit of £70.9 million to be transferred to reserves.

The Financial Review on pages 14 to 16 analyses the results in more detail, and sets out other financial information.

Corporate governance

The Company complies fully with the provisions of the Cadbury Committee's Code of Best Practice.

Board of Directors

The Board of Directors currently comprises three Executive and six Non-executive Directors. The Board and the Audit, Finance and Remuneration Committees meet on a regular basis. The Nomination Committee meets when a vacancy occurs on the Board. The Environment Committee was established on 1 April 1997 to keep under review the environmental policy and performance of the Group. Strategic and key operational decisions are determined by the Board. The Audit Committee reviews the audit plan, financial controls and procedures as well as regulatory compliance matters; the Finance Committee reviews dividend policy, financial statements and accounting policies and the Remuneration Committee reviews the remuneration and benefits of the Executive Directors and the overall remuneration and benefits policy for senior management. Details of membership of the Committees is given on page 17

and the Report of the Remuneration Committee is on pages 21 to 25.

A procedure has been established for Directors to take independent professional advice, if necessary, at the Company's expense.

Directors' responsibility statement

The Directors are required by the Companies Act 1985 to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Company and the Group as at the end of the financial year and of the profit of the Group for the financial year.

In preparing the financial statements, appropriate accounting policies have been used and consistently applied and reasonable and prudent judgements and estimates have been made. All relevant accounting standards which the Directors consider to be applicable have been followed.

The Directors have responsibility for ensuring that accounting records are kept which disclose with reasonable accuracy the financial position of the Company and the Group which enable them to ensure that the financial statements comply with the Companies Act 1985. They are responsible for safeguarding the assets of the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Internal financial control

The Directors are responsible for the Group's system of internal financial control. A system can only provide reasonable and not absolute assurance against material misstatement or loss.

There is an established internal control framework which comprises:

- a* a clearly defined structure which delegates authority, responsibility and accountability, including responsibility for internal financial control, to management of operating units;
- b* a comprehensive budgeting and reporting function, with an annual budget approved by the Board of Directors, which also monitors monthly achieved results and updated forecasts for the year against budget;
- c* documented financial control procedures; managers of operating units are required to confirm annually that they have adequate financial controls in operation, and to report all material areas of financial risk; compliance with procedures is reviewed by the Company's internal audit function; and

d an investment appraisal process for evaluating proposals for all major capital expenditure and acquisitions, with defined levels of approval and a system for monitoring the progress of capital projects.

The Audit Committee regularly reviews the operation and effectiveness of this framework.

Going concern

The Directors consider, after making appropriate enquiries, that the Company and the Group have adequate resources to continue in operational existence for the foreseeable future. For this reason they continue to adopt the going concern basis in preparing the financial statements.

Directors

Mr K W Court retired as Executive Chairman and Mr T C Leader retired as Non-executive Director on 28 February 1997. Mr K G Harvey was appointed Non-executive Chairman on 1 March 1997.

Mr B A O Hewett retired as an Executive Director on 31 March 1997 and continues on the Board as a Non-executive Director.

Mr C I J H Drummond and Mr A T Fletcher are due to retire by rotation at the annual general meeting. Having been appointed by the Board during the year Mr K G Harvey is also due to retire at the annual general meeting. All of the Directors due to retire offer themselves for re-election and resolutions for their re-election will be proposed at the annual general meeting.

Mr K G Harvey and Mr C I J H Drummond have service contracts which provide for not less than one year's notice of termination, by the Company or by the respective Director, expiring at any time. Mr A T Fletcher does not have a service contract with the Company.

No Director has, or has had, a material interest, directly or indirectly, at any time during the year under review in any contract significant to the Company's business.

Details of Directors' interests in shares of the Company are given on pages 24 and 25.

Employees

The Company is committed to effective communication with all employees. Employees in South West Water Services Limited elect representatives from all levels to a Staff Council, which deals with matters of concern to all staff

employees, both trade union and non-trade union members alike. The Staff Council complements other forms of employee communication used throughout the Group, including a monthly employee briefing system, an employee newspaper and an employee ideas scheme. Member representation arrangements in connection with the main pension schemes have been reviewed as a consequence of the Pensions Act 1995.

Employees are encouraged to become shareholders in the Company through the employee profit sharing and sharesave schemes.

Training and development of staff is a priority and particular attention is given to the management of change and training for revised working processes.

The Group operates a non-discriminatory employment policy and makes every reasonable effort to provide disabled people with equal opportunities for employment, training and development, having regard to their particular aptitudes and abilities.

Research and development

Research and development activities continued throughout the Group during the year, with expenditure of £2.0 million. Further information is included in the Operating Reviews.

Donations

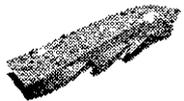
During the year charitable donations amounting to £30,000 were made. No political donations were made.

Tax status

The Company is not a close company within the meaning of the Income and Corporation Taxes Act 1988.

Payments to suppliers

It is the Company's payment policy for the year ending 31 March 1998 to follow the Confederation of British Industry (CBI) Code of Practice on supplier payments. The Company will agree payment terms with individual suppliers in advance and abide by such terms. Information about the Code, and copies thereof, may be obtained from the CBI at Centre Point, 103 New Oxford Street, London WC1A 1DJ. The ratio, expressed in days, between the amount invoiced to the Company by its suppliers during 1996/97 and the amount owed to its trade creditors at 31 March 1997, was 39 days.



Substantial shareholdings

At 26 June 1997 interests in the issued share capital had been reported by:

	Shares	%
PDFM/UBS International	16,733,120	12.98
Norwich Union Plc	8,484,180	6.56
AXA Group	7,966,434	6.19

Future developments

The Board awaits details of the Government's proposed windfall profits tax. The outcome of the Director General's 1999 review of price limits will be important to the financial position of the water and sewerage services company in the new millennium. In light of the underlying business strength of the Group the Directors are confident that the dividend policy of 8% per annum real growth will be sustainable for the immediate future in the absence of unforeseen circumstances.

Auditors

Price Waterhouse were appointed auditors until the conclusion of the eighth annual general meeting and have indicated their willingness to continue in office. A resolution for their re-appointment will be proposed at the annual general meeting.

Appointed business

South West Water Services Limited is required to publish additional financial information relating to the 'Appointed Business' as water and sewerage undertaker in accordance with the Instrument of Appointment from the Secretary of State for the Environment. A copy of this information will be available from 15 July 1997 by application to the Company Secretary at Peninsula House, Rydon Lane, Exeter EX2 7HR.

Annual general meeting

The eighth annual general meeting will be held at The Great Hall, University of Exeter, Exeter, Devon on 29 July 1997 at 11.00 a.m.

In addition to routine business, resolutions will be proposed at the annual general meeting to renew the existing authorities to allot and issue a limited number of shares and to purchase up to 10% of the existing issued share capital; to request authority to make changes to the Company's Articles of Association and to establish a restricted share plan. Details are set out in the accompanying notice of meeting.

By Order of the Board


R C Milligan, Company Secretary,
Peninsula House, Rydon Lane, Exeter, EX2 7HR.

26 June 1997

Report by the Auditors on corporate governance matters

Report by the Auditors to the Directors of South West Water Plc on corporate governance matters.

In addition to our audit of the financial statements we have reviewed your statements on pages 18 and 19 concerning the Group's compliance with the paragraphs of the Cadbury Code of Best Practice specified for our review by the London Stock Exchange and the adoption of the going concern basis in preparing the financial statements. The objective of our review is to draw attention to non-compliance with Listing Rules 12.43(j) and 12.43(v) if not otherwise disclosed.

Basis of opinion

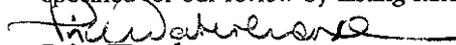
We carried out our review having regard to guidance issued by the Auditing Practices Board. That guidance does not require us to perform the additional work necessary to, and we do not, express any opinion on the effectiveness of either the Group's system of internal financial control or

corporate governance procedures nor on the ability of the Group to continue in operational existence.

Opinion

In our opinion, your statements on internal financial controls on pages 18 and 19 and on going concern on page 19 have provided the disclosures required by the Listing Rules referred to above and are consistent with the information which came to our attention as a result of our audit work on the financial statements.

In our opinion, based on enquiry of certain Directors and officers of the Company and examination of relevant documents, your statement on page 18 appropriately reflects the Group's compliance with the other aspects of the Code specified for our review by Listing Rule 12.43(j).



Price Waterhouse
Chartered Accountants
26 June 1997

Report of the Remuneration Committee

Remuneration Committee

The Remuneration Committee consists of Mr A T Fletcher, Non-executive Director, who is Chairman of the Committee, Sir Geoffrey H Chipperfield, Non-executive Director and Mr K G Harvey, Non-executive Chairman of the Company.

The Remuneration Committee operates within agreed terms of reference which are in compliance with the Greenbury Code of Best Practice and with Section A of the Best Practice Provisions on Directors' Remuneration, annexed to the Stock Exchange Listing Rules and the Company has therefore complied with Section A of the Listing Rules throughout the accounting period. It has also given full consideration to Section B of the Best Practice Provisions.

The fees and any other benefits received by Remuneration Committee members and other Non-executive Directors are determined by the Board, after taking external professional advice. Non-executive Directors do not vote on any resolution submitted as part of this process. The other benefits

received by Non-executive Directors include reimbursement of reasonable travel and accommodation expenses. Non-executive Directors are also covered by the Company's insurance policy when on Company business.

Service agreements

All Executive Directors and the Non-executive Chairman have one year rolling service agreements.

At the annual general meeting on 29 July 1997, shareholders will be requested to approve an amendment to the Articles of Association to delete the provisions under which a Managing Director, or Chief Executive Director, or executive Chairman of the Company are exempt from the requirement to retire by rotation.

Further details on directors' service agreements are contained in the Directors' Report on page 19. This includes details of unexpired terms of those Directors who have put themselves forward for re-election at the annual general meeting.

Remuneration policy

The policy of the Remuneration Committee is to provide for Executive Directors a remuneration package which is adequate to attract, retain and motivate good quality executives and which is commensurate with the remuneration packages provided by companies of similar size and complexity and in doing this makes use of the Arthur Andersen Complexity and Size (AACSTM) methodology.

The remuneration package comprises salary, annual incentive bonus, pension benefits, participation in employee share schemes and other benefits consistent with those provided by other comparable companies. Regarding longer term incentives, a new restricted share plan is proposed.

In ensuring that the value of that package is appropriate to the circumstances of the business, the Remuneration Committee also considers arrangements in other businesses within the water and sewerage sector within England and Wales. In this and all other respects, the Committee's policy remains unchanged from that set out in its last Report.

Annual incentive bonus plan

Executive Directors and senior management participate in the annual incentive bonus plan. The continuation of this plan, its structure and its participants are reviewed by the Remuneration Committee on an annual basis. The plan is designed to reinforce the major aspects of performance which are particularly important to the Company in the short-term and provides rewards based on achievement of overall corporate and individual objectives as set by the Remuneration Committee. In the case of Executive Directors, the maximum bonus achievable is 40% of basic salary.

Long-term incentive: restricted share plan

Subsequent to the Board's decision that no further options be granted under the Company's Executive Share Option Scheme, the Remuneration Committee has reviewed whether the Executive Directors and senior management should be eligible to receive benefits under a long-term incentive arrangement. As a result of this, proposals for a new restricted share plan are being submitted to shareholders at the annual general meeting on 29 July 1997. In line with the recommendations contained in the Best Practice Provisions, the Committee will ensure that awards under the new plan will be fully subject to challenging performance criteria, reflecting the Company's relative performance against comparators and will also ensure that awards made under the plan are phased over time.

Executive pension arrangements

Executive Directors and senior management participate in the South West Water Pension Scheme and the South West Water Executive Pension Scheme. These are funded defined benefit schemes. Through membership of these schemes Executive Directors will be provided with a pension which at normal retirement date will normally amount to two-thirds of final pensionable pay (subject to any restriction in respect of the Earnings Cap) and dependent on length of service.

Messrs Drummond and Hill are subject to the Earnings Cap and are provided with additional pension benefits under the unapproved funded Supplementary Pension Scheme in order to bring their pension benefits up to the level which would have been provided under the other schemes if the Earnings Cap had not applied. Executive Directors included in the unapproved pension arrangements receive payments equivalent to the tax liability which arises in respect of Company contributions to the Supplementary Pension Scheme.

The pensionable pay for participants in these arrangements consists of the highest basic salary in any consecutive twelve month period of service within five years of retirement, plus the average bonus paid over the previous five years. Payments under the annual incentive bonus plan are a significant but variable element of remuneration for Executive Directors and senior management. They are dependent on achievement of corporate and individual objectives. The Remuneration Committee therefore considers that such payments should continue to be pensionable.

In determining remuneration arrangements for Executive Directors, the Remuneration Committee gives full consideration to the impact of these on the pension funds and costs of providing individual pension arrangements.

Board structure

Mr K W Court, Executive Chairman, retired on 28 February 1997. As agreed by the Board last year, his role was separated and Mr K G Harvey was appointed as Non-executive Chairman with effect from 1 March 1997. The search for a Group Chief Executive continues. Mr S M Yassukovich was appointed Deputy Chairman on 13 November 1996. Mr T C Leader retired as a Non-executive Director on 28 February 1997 and Mr B A O Hewett retired as an Executive Director on 31 March 1997 but continues as a Non-executive Director.

Emoluments of Directors

The emoluments of individual Directors, and the defined benefit pension accrued and payable on retirement for Directors holding office during 1996/97, are shown in the table below:

	Emoluments				Total 1997 £000	Total 1996 £000	Defined benefit pension accrued (payable on retirement)	
	Salary/ fees £000	Performance bonus £000	Other emoluments £000	Payments related to supplementary pension £000			March 1997 £000	March 1996 £000
<i>Non-executive Chairman</i>								
K G Harvey (appointed 1 March 1997)	7				7			
<i>Executive Directors</i>								
R J Baty (appointed 1 March 1996)	85	14	8		107	8	52	41
K W Court (retired 28 February 1997)	127	34	7	4	172	125	44	34
C I J H Drummond	85	28	9	11	133	113	10	7
B A O Hewett (Non-executive from 1 April 1997)	91	21	8	9	129	107	7	5
K L Hill	92	29	9	8	138	120	55	51
<i>Non-executive Directors</i>								
Sir Geoffrey H Chipperfield	19				19	18		
Sir Simon J Day	19				19	18		
A T Fletcher	24				24	18		
T C Leader (retired 28 February 1997)	21				21	26		
S M Yassukovich	19				19	17		
<i>Directors resigned in 1995/96</i>								
Executive Directors						162		
Non-executive Directors						11		
	589	126	41	32	788	743	168	138

Other emoluments include car benefit and health cover.

In addition to the sums included in the above table:

- Mr B A O Hewett received £29,000 to reflect early retirement from his executive position;
- Mr W H Fraser, a former Director, was paid £50,000 in accordance with the terms of his consultancy agreement; and
- Mr K W Court and Mr B A O Hewett are entitled to performance bonuses in respect of 1996/97, which have not yet been determined, and which will be disclosed in the 1998 financial statements.

Directors' share interests

a Shareholdings

The number of shares of the Company in which Directors held beneficial interests at 31 March 1997 and 31 March 1996 (or date of appointment if later) were:

	1997	1996		1997	1996
R J Baty	11,562	11,005	K G Harvey	–	–
Sir Geoffrey H Chipperfield	1,500	1,500	B A O Hewett	11,493	1,141
Sir Simon J Day	1,500	1,500	K L Hill	13,043	12,580
C I J H Drummond	1,556	1,462	S M Yassukovich	–	–
A T Fletcher	1,146	1,089			

As a result of electing for a scrip dividend alternative the following Directors acquired additional shares on 7 April 1997:

R J Baty	33	B A O Hewett	23
C I J H Drummond	2	K L Hill	259
A T Fletcher	23		

R J Baty and C I J H Drummond acquired an additional 36 and 20 shares respectively on 9 April 1997 as a result of reinvestment of dividends in a Personal Equity Plan.

On 5 June 1997 B A O Hewett sold 3,000 shares and on 9 June 1997 K G Harvey acquired an interest in 2,000 shares.

No Director had any interest in the shares of any subsidiary undertaking during the year.

b Executive Share Option Scheme

Options to subscribe for shares of the Company under the Executive Share Option Scheme at 31 March 1997 and 31 March 1996 (or date of appointment if later) were:

Grant date	1995	1993	1992	1991	1997 Total	1996 Total
Subscription price	503p	496p	418p	328p		
R J Baty	7,500	15,000	4,600	20,000	47,100	47,100
C I J H Drummond	8,000	22,500	–	–	30,500	30,500
B A O Hewett	15,000	–	–	–	15,000	45,000
K L Hill	8,000	25,500	–	–	33,500	33,500

During the year, Mr K W Court exercised options under the scheme in respect of 40,000 shares at an exercise price of 328p per share and Mr B A O Hewett exercised options under the scheme in respect of 30,000 shares at an exercise price of 496p per share. At the date of these exercises, the market price of the shares was 687.5p. No other Director exercised any options during the year and no options were granted or lapsed during the year in respect of Directors. The exercise dates of the above options and the performance targets in respect of exercise are shown in note 23 to the financial statements.

c Sharesave Scheme

Options to subscribe for shares of the Company under the Sharesave Scheme as at 31 March 1997 and 31 March 1996 (or date of appointment if later) were:

Grant date	1995	1993	1992	1997 Total	1996 Total
Subscription price	373p	393p	332p		
R J Baty	2,774	–	2,259	5,033	5,033
B A O Hewett	–	4,389	–	4,389	4,389

No Director exercised any options during the year and no options were granted or lapsed during the year in respect of Directors. The exercise dates of the above options are shown in note 23 to the financial statements.

d Share price

The market price of the Company's shares at 31 March 1997 was 669p (1996 677p) and the range during the year to that date was 575p to 729p (1996 489p to 678p).

A T Fletcher, Chairman
Remuneration Committee
26 June 1997



Report by the Auditors on the financial statements

Auditors' report to the shareholders of South West Water Plc

We have audited the financial statements on pages 26 to 53 (including the additional disclosures on pages 23 to 25 relating to the remuneration of the Directors specified for our review by the London Stock Exchange) which have been prepared under the historical cost convention and the accounting policies set out on pages 29 and 30.

Respective responsibilities of Directors and Auditors

As described on page 18, the Company's Directors are responsible for the preparation of financial statements. It is our responsibility to form an independent opinion, based on our audit, on those statements and to report our opinion to you.

Basis of opinion

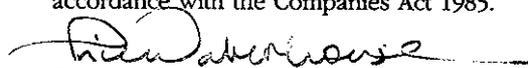
We conducted our audit in accordance with Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the Directors in the

preparation of the financial statements, and of whether the accounting policies are appropriate to the circumstances of the Company and the Group, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatements, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

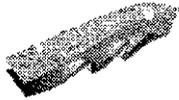
Opinion

In our opinion the financial statements give a true and fair view of the state of affairs of the Company and of the Group at 31 March 1997, and of the profit and cash flows of the Group for the year then ended, and have been properly prepared in accordance with the Companies Act 1985.



Price Waterhouse

Chartered Accountants and Registered Auditors
26 June 1997



Group profit and loss account

for the year ended 31 March 1997

	Notes	1997 £m	1996 £m
Turnover	2	343.6	314.4
Other operating income		0.7	0.6
Operating costs	3	(214.1)	(180.9)
Operating profit	2	130.2	134.1
Business disposal profits	5	19.2	–
Income from interests in associated undertakings		1.2	1.6
Net interest payable	6	(18.0)	(26.6)
Profit on ordinary activities before taxation	2	132.6	109.1
Tax on profit on ordinary activities	7	(14.3)	(10.3)
Profit on ordinary activities after taxation	8	118.3	98.8
Dividends	9	(47.4)	(38.9)
Retained profit transferred to reserves	24	70.9	59.9
Earnings per share	10	92.1p	77.7p

The notes on pages 29 to 53 form part of these financial statements.

All the activities are continuing operations.

There were no recognised gains or losses for the Group or the Company, other than the profit for the year, in 1997 or 1996.

A statement of movements in reserves is given in note 24.

Balance sheets

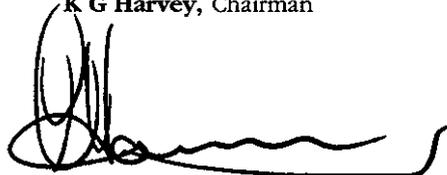
at 31 March 1997

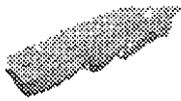
	Notes	Group		Company	
		1997 £m	1996 £m	1997 £m	1996 £m
Fixed assets					
Tangible assets	13	1,396.4	1,294.1	0.9	1.8
Investments	14	1.4	7.1	533.6	531.4
		1,397.8	1,301.2	534.5	533.2
Current assets					
Stocks	15	19.6	19.7	–	–
Debtors: amounts falling due after more than one year	16	10.8	5.4	171.6	188.3
Debtors: amounts falling due within one year	17	70.8	62.6	23.2	14.3
Investments	18	185.3	200.1	60.9	20.5
Cash at bank and in hand		2.4	0.9	–	–
		288.9	288.7	255.7	223.1
Current liabilities					
Creditors: amounts falling due within one year	19	(331.8)	(225.1)	(208.7)	(110.6)
Net current (liabilities)/assets		(42.9)	63.6	47.0	112.5
Total assets less current liabilities					
Creditors: amounts falling due after more than one year	20	(395.1)	(482.7)	(150.3)	(235.7)
Provisions for liabilities and charges	21	(21.5)	(18.8)	–	–
Deferred income	22	(22.4)	(23.2)	–	–
Net assets	2	915.9	840.1	431.2	410.0
Capital and reserves					
Called-up share capital	23	129.1	127.4	129.1	127.4
Share premium account	24	148.5	144.9	148.5	144.9
Other reserves	24	–	–	3.1	3.1
Profit and loss account	24	638.3	567.8	150.5	134.6
Shareholders' funds	25	915.9	840.1	431.2	410.0

The notes on pages 29 to 53 form part of these financial statements.

Approved by the Board on 26 June 1997 and signed on its behalf by:

K G Harvey, Chairman





Group cash flow statement

for the year ended 31 March 1997

	Notes	1997 £m	1996 £m
Cash inflow from operating activities	32a	155.9	142.5
Returns on investments and servicing of finance	32b	(18.6)	(20.2)
Taxation		(11.0)	(7.8)
Capital expenditure and financial investment	32b	(141.6)	(106.3)
Acquisitions and disposals	32b	28.0	(93.0)
Equity dividends paid		(35.4)	(32.5)
Cash outflow before use of liquid resources and financing		(22.7)	(117.3)
Management of liquid resources	32b	18.9	236.6
Financing	32b	10.3	(111.5)
Increase in cash in year		6.5	7.8

Notes to the financial statements

1 Accounting policies

The following paragraphs describe the main policies:

a Accounting convention

The financial statements have been prepared under the historical cost convention and in compliance with all applicable accounting standards, the requirements of the London Stock Exchange and, except for the treatment of grants and contributions on infrastructure assets, with the Companies Act 1985. An explanation of this departure from the requirements of the Companies Act 1985 is given in note 1f below.

b Basis of consolidation

The Group financial statements include the results of the Company and its subsidiary undertakings, each made up to 31 March 1997, together with the attributable share of results and reserves of associated undertakings on the basis of their latest financial statements. The results of subsidiary and associated undertakings acquired or disposed of during the year are included for the periods of ownership.

c Turnover

Turnover, excluding Value Added Tax, represents the income receivable in the ordinary course of business for goods and services provided.

d Tangible fixed assets and depreciation

i *Infrastructure assets* (being mains and sewers, impounding and pumped raw water storage reservoirs, dams, sludge pipelines and sea outfalls)

Infrastructure assets comprise a network of systems. Expenditure on infrastructure assets relating to increases in capacity or enhancements of the network is treated as capital expenditure on tangible fixed assets and included at cost after deducting grants and contributions. No depreciation is charged on infrastructure assets because the network of systems is required to be maintained in perpetuity and therefore has no finite economic life.

Expenditure on maintaining the operating capability of the network is charged as an operating cost. Expenditure on the maintenance of infrastructure assets may vary significantly from the long term normal annual level. In such instances, the charge against profits is equalised by way of accruals or deferrals as appropriate to reflect the long term normal level of charges, in accordance with defined standards of service.

ii *Landfill sites*

Landfill sites are included at cost less accumulated depreciation. The cost of a landfill site is depreciated over its estimated operational life taking account of the usage of void space. Cost includes acquisition and development expenses.

iii *Other assets* (including properties, overground plant and equipment)

Other assets are stated at cost less accumulated depreciation.

Freehold land is not depreciated. Other assets are depreciated evenly over their estimated economic lives, which are principally as follows:

Leasehold buildings	Over the period of the lease
Freehold buildings	30-60 years
Operational structures	40-80 years
Fixed plant	20-40 years
Vehicles, mobile plant and computers	3-10 years

Assets in the course of construction are not depreciated until commissioned.

e *Leased assets*

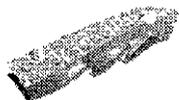
Assets held under finance leases are included in the balance sheet as tangible fixed assets at their equivalent capital value and are depreciated over their estimated economic lives or the finance lease period, whichever is the shorter. The corresponding liability is recorded as a creditor. The interest element of the rental costs is charged against profits, using the actuarial method, over the period of the lease.

Rental costs arising under operating leases are charged against profits in the year they are incurred.

f *Grants and contributions*

Grants and contributions receivable in respect of capital expenditure on non-infrastructure assets are included in the balance sheet as deferred income and are released to profits over the depreciable lives of the assets to which they relate.

Grants and contributions receivable relating to infrastructure assets have been deducted from the cost of tangible fixed assets. This is not in accordance with the Companies Act 1985 which requires tangible fixed assets to be shown at cost and hence grants and contributions as deferred income. This departure from the requirements of the Companies Act 1985 is, in the opinion of the Directors, necessary for the financial statements to



Notes to the financial statements

f Grants and contributions continued

show a true and fair view as no provision is made for depreciation and any grants and contributions relating to such assets would not be taken to the profit and loss account. The effect of this treatment on the value of tangible fixed assets is disclosed in note 13.

Grants and contributions receivable in respect of expenditure charged against profits in the year have been included in the profit and loss account.

g Investments

Listed investments held as current assets are stated at the lower of cost and net realisable value.

Short dated unlisted securities held as current assets are stated at cost plus accrued income.

h Stocks

Stocks are stated at the lower of cost and net realisable value. Cost includes labour, materials and an element of overheads.

i Pension costs

The expected cost of pensions in respect of the Group's defined benefit pension schemes is charged against profits so as to spread evenly the cost of pensions over the service lives of employees in the schemes. A pension surplus is released to profits using the straight line method, over the average remaining service lives of employees in the scheme.

Pension costs for the Group's defined contribution schemes are charged against profits in the year in which they are incurred.

j Research and development expenditure

Research and development expenditure is charged against profits in the year in which it is incurred.

k Taxation

Tax payable on profits for the year is provided at current rates. Tax deferred or accelerated as a result of timing differences between the treatment of certain items for taxation and for accounting purposes is provided for to the extent that it is probable that a material liability or asset will crystallise in the foreseeable future.

l Goodwill

Goodwill, arising from the purchase of subsidiary and associated undertakings, representing the excess of the purchase consideration over the fair value of net assets acquired, is written off to Group reserves. When a previously acquired subsidiary or associated undertaking is sold the profit or loss on disposal is determined by including the attributable amount of goodwill previously written off to Group reserves.

m Foreign currency

Assets and liabilities denominated in foreign currencies are translated into sterling at the rates ruling at the balance sheet date. Profit and loss accounts are translated at average rates for the relevant accounting period. Exchange differences arising from the retranslation of the opening net investment in overseas enterprises at closing rates, offset by translation differences on foreign currency loans which finance such investments, are dealt with in reserves.

n Landfill restoration and environmental costs

Provisions for restoration, aftercare and environmental control costs are made over the estimated operational life of landfill sites taking account of the usage of void space.

2 Segmental analysis

By class of business:

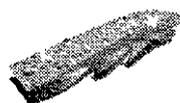
	Turnover		Operating profit		Profit before tax	
	1997	1996	1997	1996	1997	1996
	£m	£m	£m	£m	£m	£m
Water and sewerage services	244.6	239.3	121.3	125.5	110.0	104.7
Business disposal profits	-	-	-	-	1.7	-
Less: Intra-group trading	(1.7)	(1.5)	-	-	-	-
	242.9	237.8	121.3	125.5	111.7	104.7
Non-regulated businesses:						
Waste management	41.9	34.1	8.0	5.3	7.8	4.5
Environmental instrumentation	40.0	31.5	4.0	1.7	3.7	1.4
Construction services	51.8	31.7	1.7	1.4	1.4	1.1
Business disposal profits	-	-	-	-	17.5	-
Other	12.2	14.3	1.5	2.1	(3.2)	(0.6)
	145.9	111.6	15.2	10.5	27.2	6.4
Less: Intra-group trading	(45.2)	(35.0)	(1.1)	(1.2)	(1.1)	(1.3)
	100.7	76.6	14.1	9.3	26.1	5.1
Proposed bids costs	-	-	(5.2)	(0.7)	(5.2)	(0.7)
	343.6	314.4	130.2	134.1	132.6	109.1

	Net assets/(liabilities)		Employees (average number)	
	1997	1996	1997	1996
	£m	£m		
Water and sewerage services	948.3	908.1	1,765	1,815
Non-regulated businesses:				
Waste management	47.1	38.5	297	322
Environmental instrumentation	13.4	11.2	411	357
Construction services	1.6	0.6	567	398
Other	(88.2)	(108.6)	113	113
	(26.1)	(58.3)	1,388	1,190
Intra-group trading	(6.3)	(9.7)	-	-
	915.9	840.1	3,153	3,005

Water and sewerage services comprise the regulated water and waste water business.

Net liabilities of Other includes parent company financing of the acquisition of non-regulated businesses, and profit before tax of Other is shown after interest arising thereon.

The costs of the proposed bids have been separately disclosed, because of increased materiality in 1997, and the comparatives have been amended accordingly.



Notes to the financial statements

2 Segmental analysis continued

By geographical origin:

	Turnover		Operating profit		Profit before tax	
	1997	1996	1997	1996	1997	1996
	£m	£m	£m	£m	£m	£m
United Kingdom	325.2	301.1	128.2	133.1	130.6	108.0
Americas	18.4	13.3	2.0	1.0	2.0	1.1
	343.6	314.4	130.2	134.1	132.6	109.1

By geographical destination:

	Turnover		Operating profit		Profit before tax	
	1997	1996	1997	1996	1997	1996
	£m	£m	£m	£m	£m	£m
United Kingdom	309.4	287.5	126.6	132.7	129.0	107.4
Continental Europe	4.8	3.7	0.4	(0.1)	0.4	0.1
Americas	16.8	11.7	2.2	0.9	2.2	1.0
Other	12.6	11.5	1.0	0.6	1.0	0.6
	343.6	314.4	130.2	134.1	132.6	109.1

Net assets are not separately disclosed by geographic origin and destination since they are substantially located in the United Kingdom.

The employee numbers include 211 working outside the United Kingdom (1996 155).

3 Operating costs

	1997	1996
	£m	£m
Manpower costs (note 11)	45.4	37.5
Raw materials and consumables	37.1	30.6
Rentals under operating leases:		
Hire of plant and machinery	1.9	2.0
Other operating leases	1.7	1.4
Research and development expenditure	2.0	1.7
Auditors' remuneration	0.2	0.2
Other external charges	59.3	49.7
Depreciation:		
On owned assets	25.4	18.8
On assets held under finance leases	9.7	12.9
On assets held under defeased finance leases	0.4	—
Deferred income released to profits	(1.2)	(0.8)
Infrastructure renewals charge	6.8	6.9
Other operating charges	25.4	20.0
	214.1	180.9

Fees payable to the Company's auditors for non-audit work, mainly in connection with taxation advice and the proposed bids, amounted to £0.8m (1996 £0.5m).

Operating costs include the exceptional items set out in note 4.

4 Exceptional items

	1997	1996
	£m	£m
Operating profit is after charging/(crediting) the following exceptional items:		
Costs associated with the proposed bids	5.2	0.7
Water and sewerage business restructuring provision release	–	(7.5)
	5.2	(6.8)

In 1996 £6.9m was charged against profits, as an exceptional item, to cover the cost of a £10 water and sewerage customer rebate. In 1997 a second rebate, of £15, costing £10.0m has been provided. Given the second occurrence it is no longer considered appropriate to treat the 1996 cost as exceptional and the comparatives have been amended accordingly.

5 Business disposal profits

	1997	1996
	£m	£m
During the year the Group realised a profit from the disposal of interests in:		
Westcountry Television Limited	14.8	–
Other businesses	4.4	–
	19.2	–

The profit on disposal is after charging £0.6m of acquisition goodwill previously written off to reserves.

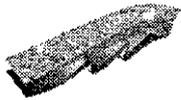
No tax charge arose on the disposal profits.

The profits arising from the operation of the businesses disposed of during the year are not material to the profits of the Group.

6 Net interest payable

	1997	1996
	£m	£m
Interest payable:		
Bank loans and overdrafts	(13.8)	(15.9)
Other loans	(23.0)	(23.0)
Interest element of finance lease rentals	(7.6)	(10.2)
Other finance costs	(0.3)	(0.1)
	(44.7)	(49.2)
Interest receivable:		
Listed redeemable securities	2.3	4.3
Other investments (as defined in note 18)	15.7	18.3
	18.0	22.6
Gain on defeasance of finance leases	8.7	–
Net interest payable	(18.0)	(26.6)

Interest element of finance lease rentals is shown after netting £7.2m (1996 £6.4m) interest receivable on cash deposited against collateralized finance lease obligations (note 26).



Notes to the financial statements

6 Net interest payable continued

The gain on defeasance of finance leases results from the in-substance early settlement (defeasance) of obligations under finance leases. South West Water Services Limited has:

- a utilised finance lease facilities for certain water and sewerage services tangible fixed assets; and
- b deposited amounts, equal to the present value of rental obligations arising from those finance leases, with UK financial institutions, to counter-indemnify the letters of credit issued by those financial institutions to the lessors in order to secure those rental obligations.

These deposited funds, which totalled £52.7m at 31 March 1997 (1996 nil), together with interest earned thereon, may be used to settle the rental obligations under those finance leases. If the finance leases terminate due to the insolvency of the financial institutions which have issued the letters of credit no liability will fall on South West Water Services Limited, or any South West Water Group company.

The rentals payable under the finance leases will vary if interest rates, or effective tax rates, change. The Group has made provision, based upon the Directors' assessment of likely outcomes, for possible future costs arising from such variations in arriving at the gain recognised.

A gain of £8.7m (1996 nil) has been recognised, equivalent to the difference between the finance lease proceeds and the funds deposited with financial institutions to cover rentals arising therefrom, after making provision for possible rental variations and costs as follows:

	1997 £m	1996 £m
Gain on defeasance of finance leases	12.7	–
less provision for finance lease rental variations (note 21)	(2.9)	–
less costs	(1.1)	–
	8.7	–

7 Tax on profit on ordinary activities

	1997 £m	1996 £m
United Kingdom taxation:		
Corporation tax at 33%:		
Current year	12.7	2.7
Prior year	(2.9)	–
Advance corporation tax:		
Current year dividends	10.7	8.9
Previous year utilisation	(6.3)	(1.4)
Overseas taxation	0.1	0.1
	14.3	10.3

The corporation tax charge for the year has been reduced by the availability of capital allowances for which no deferred tax has been provided (note 21).

8 Profit of parent company

	1997 £m	1996 £m
Profit on ordinary activities after taxation dealt with in the accounts of the parent company	60.6	32.7

As permitted by section 230 of the Companies Act 1985, no profit and loss account is presented for the Company.

9 Dividends

	1997 £m	1996 £m
Interim dividend of 11.8p (1996 9.8p) per share paid 7 April 1997	15.1	12.5
Proposed final dividend of 24.9p (1996 20.7p) per share payable 1 October 1997	32.3	26.4
	47.4	38.9

10 Earnings per share

	1997	1996
Profit on ordinary activities after taxation	£118.3m	£98.8m
Earnings per share	92.1p	77.7p

Earnings per share for 1997, calculated in accordance with the guidelines issued by the Institute of Investment Management and Research, were 77.2p (1996 77.7p). This has been calculated by eliminating the business disposal profits (equivalent to 14.9p per share) and is provided for clarification purposes for users of the financial statements.

Earnings per share on the nil distribution basis was 100.5p (1996 84.7p). This has been calculated by eliminating the taxation charge of £10.7m (1996 £8.9m) in respect of irrecoverable advance corporation tax on the interim and proposed final dividends.

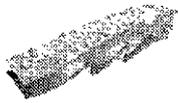
The above earnings per share figures have been calculated by dividing the profit on ordinary activities by 128.4 million being the weighted average number of shares in issue during the year (1996 127.1 million). There would have been no significant dilution of earnings per share if the outstanding shares which might be issued in respect of the Company's share option schemes, referred to in note 23, had been in issue during the year.

11 Employees and employment costs

The average number of persons (including Directors) employed by the Group was 3,153 (1996 3,005).

Employment costs comprise:

	1997 £m	1996 £m
Wages and salaries:		
excluding exceptional items	57.7	54.9
exceptional items	—	(0.2)
Social security costs	5.4	5.1
Pension costs (note 30):		
excluding exceptional items	(2.0)	(0.8)
exceptional items	—	(7.3)
Total employment costs	61.1	51.7



Notes to the financial statements

11 Employees and employment costs continued

	1997 £m	1996 £m
Charged as follows:		
Manpower costs (note 3):		
excluding exceptional items	45.4	45.0
exceptional items	–	(7.5)
	45.4	37.5
Research and development expenditure	1.5	1.2
Capital schemes and infrastructure renewals expenditure	14.2	11.9
Restructuring provision	–	1.1
	61.1	51.7

12 Directors' emoluments

	1997 £000	1996 £000
Executive Directors:		
Remuneration – salary	480	475
– performance bonus	126	54
Other emoluments	41	48
Payments in respect of tax liability from supplementary pension arrangements	32	58
Non-executive Directors:		
Salary/fees	109	108
Total emoluments	788	743
Compensation in respect of a service agreement	29	336

Total gains made by Directors on the exercise of share options were £201,000 (1996 £105,000).

The emoluments of the highest paid Director, including gains on the exercise of share options of £144,000 (1996 £72,000), were £316,000 (1996 £192,000).

Total emoluments include £112,000 (1996 £151,000) payable to Directors for services as directors of subsidiary undertakings.

At 31 March 1997 retirement benefits were accruing to 4 Directors under defined benefit pension schemes (1996 4 under defined benefit, and 1 under defined benefit and defined contribution, pension schemes). Pension contributions to defined contribution schemes were £6,000 (1996 £16,000). Pension contributions to defined contribution schemes for the highest paid Director were £6,000 (1996 nil).

As a consequence of changes to the Companies Act 1985 the format of disclosure has been changed and certain comparatives have accordingly been modified.

Performance bonuses for 1996 have been disclosed in 1997 numbers above. The bonuses payable for 1997 performance have not yet been determined and will be disclosed in the 1998 financial statements.

More detailed information concerning Directors' emoluments, shareholdings and share options is shown in the Report of the Remuneration Committee on pages 23 to 25.

13 Tangible fixed assets

Group

	Land and buildings £m	Infrastructure assets £m	Operational properties £m	Fixed and mobile plant, vehicles and computers £m	Construction in progress £m	Total 1997 £m
Cost:						
At 1 April 1996	84.4	533.8	389.4	380.4	95.4	1,483.4
Additions	2.1	21.2	19.7	46.6	67.6	157.2
Grants and contributions		(2.8)				(2.8)
Arising on acquisitions	–	–	–	0.2	–	0.2
Foreign currency retranslation	(0.1)	–	–	(0.2)	–	(0.3)
Disposals	(13.9)	–	–	(8.2)	–	(22.1)
Transfers	–	22.0	22.5	5.7	(50.2)	–
At 31 March 1997	72.5	574.2	431.6	424.5	112.8	1,615.6
Depreciation:						
At 1 April 1996	12.0		65.8	111.5		189.3
Charge for year	3.6		7.9	25.8		37.3
Foreign currency retranslation	–		–	(0.1)		(0.1)
Disposals	(2.0)		–	(5.3)		(7.3)
At 31 March 1997	13.6		73.7	131.9		219.2
Net book value:						
At 31 March 1997	58.9	574.2	357.9	292.6	112.8	1,396.4
At 31 March 1996	72.4	533.8	323.6	268.9	95.4	1,294.1
Assets held under finance leases included above:						
Cost: At 31 March 1997	–	–	189.5	115.6	4.3	309.4
Depreciation: Charge for year	–		2.4	7.3		9.7
Depreciation: At 31 March 1997	–		9.6	36.5		46.1
Assets held under defeased finance leases included above:						
Cost: At 31 March 1997	–	31.8	8.6	10.3	14.7	65.4
Depreciation: Charge for year and at 31 March 1997	–		0.1	0.3		0.4



Notes to the financial statements

13 Tangible fixed assets continued

Group continued

The cost of land and buildings and of operational properties includes non-depreciable land of £1.6m (1996 £3.9m) and £7.2m (1996 £7.6m) respectively.

The net book value of land and buildings comprises:

	1997 £m	1996 £m
Freehold	52.3	65.1
Long leasehold	0.2	0.2
Short leasehold	6.4	7.1
	58.9	72.4

Included within freehold land and buildings is £2.5m (1996 £2.5m) for an investment property that has been valued by an employee of the Group who is a Chartered Surveyor.

The net book value of infrastructure assets is stated after deducting £33.7m (1996 £30.9m) grants and contributions.

Out of the total depreciation charge for the Group of £37.3m (1996 £33.2m), the sum of £1.8m (1996 £1.5m) has been charged to capital projects and £35.5m (1996 £31.7m) against profits.

Company

	Freehold land and buildings £m	Fixed and mobile plant, vehicles and computers £m	Total 1997 £m
Cost:			
At 1 April 1996	1.9	1.2	3.1
Additions	13.9	0.1	14.0
Disposals	(14.8)	(0.3)	(15.1)
At 31 March 1997	1.0	1.0	2.0
Depreciation:			
At 1 April 1996	0.6	0.7	1.3
Charge for year	-	0.1	0.1
Disposals	(0.1)	(0.2)	(0.3)
At 31 March 1997	0.5	0.6	1.1
Net book value:			
At 31 March 1997	0.5	0.4	0.9
At 31 March 1996	1.3	0.5	1.8

14 Fixed asset investments

	Shares £m	Loans £m	Group Total 1997 £m	Shares £m	loans £m	Company Total 1997 £m
<i>Subsidiary undertakings</i>						
Cost:						
At 1 April 1996				527.0	–	527.0
Additions				9.2	–	9.2
Provisions				(2.6)	–	(2.6)
At 31 March 1997				533.6	–	533.6
<i>Associated undertakings</i>						
Cost (Company) or share of net assets (Group):						
At 1 April 1996	2.9	4.2	7.1	1.4	3.0	4.4
Additions	(1.8)	3.0	1.2	0.3	–	0.3
Goodwill	0.4	(2.2)	(1.8)			
Provisions	–	(0.4)	(0.4)	–	–	–
Foreign currency retranslation	–	(0.2)	(0.2)	–	–	–
Profit for year	0.7	–	0.7			
Dividends received	(0.3)	–	(0.3)			
Disposals	(1.9)	(3.0)	(4.9)	(1.7)	(3.0)	(4.7)
At 31 March 1997	–	1.4	1.4	–	–	–
<i>Total investments</i>						
At 31 March 1997	–	1.4	1.4	533.6	–	533.6
At 31 March 1996	2.9	4.2	7.1	528.4	3.0	531.4

Goodwill includes £2.0m resulting from acquisitions (note 28) offset by £0.2m arising on a business disposal.

Profit for year of £0.7m (1996 £0.8m) comprised income from interests in associated undertakings at £1.2m (1996 £1.6m), disclosed in the profit and loss account, less £0.5m (1996 £0.8m) included elsewhere in the balance sheet.

Details of principal subsidiary and associated undertakings of the Group are set out in note 29.

15 Stocks

	Group		Company	
	1997 £m	1996 £m	1997 £m	1996 £m
Raw materials and consumables	5.5	4.5	–	–
Work in progress	10.0	11.0	–	–
Finished goods	4.1	4.2	–	–
	19.6	19.7	–	–



Notes to the financial statements

16 Debtors: amounts falling due after more than one year

	Group		Company	
	1997 £m	1996 £m	1997 £m	1996 £m
Amounts owed by subsidiary undertakings			168.0	187.3
Prepayments for pension costs	8.2	5.4	1.0	1.0
Other prepayments and accrued income	2.6	–	2.6	–
	10.8	5.4	171.6	188.3

17 Debtors: amounts falling due within one year

	Group		Company	
	1997 £m	1996 £m	1997 £m	1996 £m
Trade debtors	46.1	40.7	–	–
Amounts owed by subsidiary undertakings			20.2	13.5
Amounts owed by associated undertakings	–	0.8	–	0.5
Other debtors	8.1	3.1	0.9	0.1
Prepayments and accrued income	16.4	17.9	2.1	0.2
Advance corporation tax recoverable	0.2	0.1	–	–
	70.8	62.6	23.2	14.3

18 Current asset investments

	Group		Company	
	1997 £m	1996 £m	1997 £m	1996 £m
Listed investments	31.3	57.5	–	–
Other investments:				
Overnight deposits	4.7	0.6	–	–
Other	149.3	142.0	60.9	20.5
	154.0	142.6	60.9	20.5
	185.3	200.1	60.9	20.5
Market value of listed investments	31.4	57.7	–	–

Other investments include certificates of deposit, variable rate notes, commercial paper and other short-dated unlisted securities.

The analysis of other investments has been expanded to provide disclosure of overnight deposits following the introduction of Financial Reporting Standard 1 (Revised 1996) 'Cash Flow Statements'.

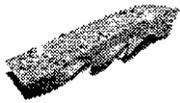
£150.0m (1996 £150.0m) deposited against collateralized finance lease obligations (note 26) is not included in the Group numbers.

19 Creditors: amounts falling due within one year

	Group		Company	
	1997 £m	1996 £m	1997 £m	1996 £m
Loans:				
Bank loans and overdrafts	1.3	2.2	18.9	15.4
Short-term loans	35.7	35.4	35.0	35.0
Sterling notes	85.4	0.5	85.4	0.5
European Investment Bank loans	9.0	7.8	—	—
Series B unsecured loan stock notes	4.2	4.4	4.2	4.4
	135.6	50.3	143.5	55.3
Obligations under finance leases	15.1	15.5	—	—
Trade creditors	72.6	63.3	1.2	6.2
Amounts owed to associated undertakings	—	0.5	—	—
Other creditors	13.4	7.8	5.5	1.2
Advance corporation tax	11.9	9.8	11.9	9.8
Corporation tax	3.6	2.4	—	—
Other taxation and social security	5.7	4.3	—	—
Accruals and deferred income	27.7	33.2	0.4	0.1
Interim dividend	13.9	11.6	13.9	11.6
Proposed final dividend	32.3	26.4	32.3	26.4
	331.8	225.1	208.7	110.6

20 Creditors: amounts falling due after more than one year

	Group		Company	
	1997 £m	1996 £m	1997 £m	1996 £m
Loans:				
Sterling bond	150.0	150.0	150.0	150.0
Sterling notes	—	85.4	—	85.4
European Investment Bank loans	106.7	115.6	—	—
Other loans	0.1	0.3	—	—
	256.8	351.3	150.0	235.4
Obligations under finance leases	136.0	128.7	—	—
Amounts owed to subsidiary undertakings	—	—	0.2	0.2
Other creditors	2.3	2.7	0.1	0.1
	395.1	482.7	150.3	235.7



Notes to the financial statements

21 Provisions for liabilities and charges

	At 1 April 1996	Charged against profits	Arising on acquisitions	Utilised during year	Group At 31 March 1997
	£m	£m	£m	£m	£m
Infrastructure renewals	2.1	6.8	–	(6.5)	2.4
Environmental and landfill restoration	11.0	2.2	1.0	(0.5)	13.7
Restructuring costs	5.7	–	–	(3.2)	2.5
Finance lease rental variations (note 6)	–	2.9	–	–	2.9
	18.8	11.9	1.0	(10.2)	21.5

Deferred taxation

The maximum potential liability for deferred taxation, for which no provision is considered necessary, was:

	Group	
	1997 £m	1996 £m
Tax effect of timing differences due to:		
Accelerated capital allowances	72.3	61.8
Other timing differences	(4.3)	(5.4)
	68.0	56.4
Advance corporation tax recoverable	(41.2)	(34.1)
Maximum potential liability	26.8	22.3

As infrastructure assets are not depreciated, deferred taxation will only crystallise in the event of their disposal at amounts in excess of their tax written-down value. The tax effect (at 33%) due to accelerated capital allowances on infrastructure assets which has been excluded above amounts to £144.8m (1996 £128.1m). Advance corporation tax of £4.4m, additional to the amount set out in the table above, is available to be set against this liability (1996 £8.8m). In the opinion of the Directors, the likelihood of a liability crystallising in the foreseeable future is remote.

22 Deferred income

	Group	
	1997 £m	1996 £m
At 1 April	24.2	24.5
Additions	0.4	0.5
Released to profits	(1.2)	(0.8)
At 31 March	23.4	24.2
To be released within one year	(1.0)	(1.0)
To be released after more than one year	22.4	23.2

23 Called-up share capital

	1997 £m	1996 £m
<i>Authorised</i>		
175,000,000 ordinary shares of £1 each	175.0	175.0
<i>Allotted, called-up and fully paid</i>		
129,137,651 ordinary shares of £1 each (1996 127,421,387)	129.1	127.4
<i>Ordinary shares allotted during year</i>		
	1997 Number	1996 Number
In lieu of £3.5m cash (1996 £2.1m) under scrip dividend alternative	585,817	405,681
For consideration of £2.6m (1996 £1.4m) under South West Water Executive Share Option Scheme to Directors and senior employees who exercised their options	608,850	365,100
For consideration of £0.7m (1996 £0.4m) under South West Water Sharesave Scheme to employees who exercised their options	218,100	146,820
For consideration of £1.1m (1996 nil) to SWW Trustees Limited on behalf of employees who exercised their options under the South West Water Sharesave Scheme	164,906	–
For consideration of £0.9m (1996 nil) to SWW Share Schemes Trustees Limited on behalf of participants in the Profit Sharing Scheme	138,591	–
	1,716,264	917,601

Share options

Outstanding options to subscribe for shares of £1 each under the Company's share option schemes are:

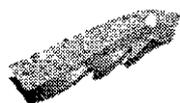
Nature of scheme	Date granted and subscription price fully paid	Performance targets	Period when options normally exercisable	Thousands of shares in respect of which options outstanding at 31 March		
				1997	1996	
Sharesave	12 Dec 1989	176p	–	1995 – 1997	25	206
	5 July 1991	287p	–	1996 – 1998	159	358
	3 July 1992	332p	–	1997 – 1999	242	257
	2 July 1993	393p	–	1998 – 2000	160	177
	6 Jan 1995	373p	–	2000 – 2002	391	426
Executive	5 July 1991	328p	a	1994 – 2001	63	273
	3 July 1992	418p	a	1995 – 2002	97	256
	5 July 1993	496p	b	1996 – 2003	257	455
	6 Jan 1995	503p	c	1998 – 2005	266	313
					1,660	2,721

The performance targets for exercise of Executive Scheme options are:

- a gross dividend yield of 9.68% on the 1989 water share offer price;
- b increase in earnings per share in excess of the Retail Price Index movement over the period March 1993 to date of exercise; and
- c increase in earnings per share in excess of the Retail Price Index movement over the period March 1994 to date of exercise.

At 31 March 1997 there were 923 participants in the Sharesave Scheme (1996 992) and 64 in the Executive Scheme (1996 80).

Options granted to Directors, included above, are shown in the Report of the Remuneration Committee on pages 24 and 25.



Notes to the financial statements

24 Reserves

	Group and Company share premium account £m	Company other reserves £m	Group profit and loss account £m	Company profit and loss account £m
At 1 April 1996	144.9	3.1	567.8	134.6
Retained profit for year			70.9	13.2
Premium on shares issued	3.3			
Adjustment for shares issued under the scrip dividend alternative	(0.6)		3.6	3.6
Adjustment for shares issued under the Sharesave Scheme through employee share ownership trust	0.9		(0.9)	(0.9)
Goodwill arising on acquisitions			(3.7)	
Goodwill written back on disposals			0.6	
At 31 March 1997	148.5	3.1	638.3	150.5

The cumulative value of goodwill at 31 March 1997 resulting from acquisitions, which has been written off to reserves, is £111.7m (1996 £108.6m).

Exchange differences arising from the retranslation of the net investment in overseas businesses, dealt with in the Group profit and loss account, are offset by a gain on matching currency hedges.

25 Statement of movements in shareholders' funds

	Group		Company	
	1997 £m	1996 £m	1997 £m	1996 £m
Profit on ordinary activities after taxation	118.3	98.8	60.6	32.7
Dividends	(47.4)	(38.9)	(47.4)	(38.9)
	70.9	59.9	13.2	(6.2)
Adjustment for shares issued under the scrip dividend alternative	3.6	2.4	3.6	2.4
Shares issued for cash consideration	5.3	1.8	5.3	1.8
Adjustment for shares issued under the Sharesave Scheme through employee share ownership trust	(0.9)	–	(0.9)	–
Goodwill written off (net)	(3.1)	(68.3)	–	–
Shareholders' funds (equity interest):				
Addition/(reduction) for year	75.8	(4.2)	21.2	(2.0)
At 1 April	840.1	844.3	410.0	412.0
At 31 March	915.9	840.1	431.2	410.0

26 Loans and other borrowings

Loans	Group		Company	
	1997 £m	1996 £m	1997 £m	1996 £m
Repayable:				
After five years	212.0	224.1	150.0	150.0
Between two and five years	34.4	32.8	–	–
Between one and two years	10.4	94.4	–	85.4
Falling due after more than one year (note 20)	256.8	351.3	150.0	235.4
Falling due within one year (note 19)	135.6	50.3	143.5	55.3
	392.4	401.6	293.5	290.7

26 Loans and other borrowings continued

<i>Obligations under finance leases</i>	Group		Company	
	1997 £m	1996 £m	1997 £m	1996 £m
Repayable:				
After five years	118.4	113.4	—	—
Between two and five years	7.0	9.1	—	—
Between one and two years	10.6	6.2	—	—
Falling due after more than one year (note 20)	136.0	128.7	—	—
Falling due within one year (note 19)	15.1	15.5	—	—
	151.1	144.2	—	—

Included above are finance charges arising on obligations under finance leases totalling £15.2m (1996 £9.8m), of which £8.8m (1996 £9.4m) is repayable within one year.

Obligations under finance leases of £150.0m (1996 £150.0m) are not included above because cash of an equal amount has been deposited with the lessor's bank group (collateralization); South West Water Services Limited can insist this cash is utilised to meet the finance lease obligations as they fall due. Such cash deposits are likewise not shown on the balance sheet. South West Water Services Limited has no present plans to withdraw the cash deposits but, in the event that some, or all, of the deposits were withdrawn, an equivalent amount of finance lease obligations would require to be reinstated as a liability on the balance sheet.

Loans and obligations under finance leases

Included above are instalment debts, of which any part falls due for repayment after five years, and non-instalment debts due after five years:

	Group		Company	
	1997 £m	1996 £m	1997 £m	1996 £m
Loans	265.6	265.7	150.0	150.0
Obligations under finance leases	133.6	122.4	—	—
	399.2	388.1	150.0	150.0

Loans and other borrowings are predominantly denominated in sterling and are repayable over the period 1997 to 2021. The rates of interest payable on loans and other borrowings, any part of which is due after five years, range between 4% and 11%.



Notes to the financial statements

27 Financial instruments and risk management

The principal financial risk faced by the Group arises from interest rate movements.

The Group uses derivative financial instruments to manage and adjust its exposure to market risk from changes in interest rates including, inter alia, ensuring that at least 50% of net debt is at fixed rate. The precise mix is at times adjusted to reflect anticipated movements in short-term interest rates.

The Board approves treasury policies and procedures relating to the use of financial instruments. Trading for speculative purposes is not permitted. Major transactions are individually approved by the Board.

The principal interest rate swap agreements outstanding at 31 March 1997 covered a notional amount of £62.8m and aligned the basis of interest receivable from current asset investments with that payable on certain finance lease obligations. During the year the Group entered into a series of interest rate swaps, subsequently closed, based on a notional principal of £150.0m and with maturities ranging to 2001/03.

The notional principal amounts are used to determine settlements under interest rate swaps and are not, therefore, an exposure of the Group.

28 Acquisitions

On 16 October 1996 South West Water Services Limited, a 100% owned Group company, acquired an unincorporated hydro electric business from National Power Plc for a cash consideration of £0.4m. Goodwill on acquisition amounting to £1.4m has been written off to reserves.

On 30 August 1996 and 12 October 1996 Haul Waste Limited, a 100% owned Group company, acquired two unincorporated waste management businesses for a cash consideration of £0.5m. Goodwill on acquisition amounting to £0.3m has been written off to reserves.

Provisional fair values were used for the acquisition of a 50% interest in Elcar Srl (subsequently renamed Societa Italo Britannica dell'Acqua Srl) in the previous financial year. The following adjustments, including a revision to the contingent consideration, have been made:

	Associated undertakings		
	Provisional £m	Adjustments £m	Final £m
Fair value acquired	1.4	(3.8)	(2.4)
Goodwill written off to reserves	5.1	2.0	7.1
Consideration and costs	6.5	(1.8)	4.7

The adjustment to the fair value acquired was in respect of debtors due within and over one year, and work in progress.

28 Acquisitions continued

All acquisitions were accounted for using the acquisition method. Results of the businesses acquired for pre-acquisition and subsequent periods were not material. The analysis of the fair value of net assets acquired is shown in note 32e.

During the year £1.0m fair value acquisition accruals and provisions were established (1996 £9.6m), £0.9m were utilised (1996 £0.8m) and at 31 March 1997 £10.6m (1996 £10.5m) was carried forward.

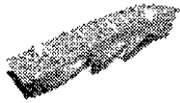
29 Principal subsidiary and associated undertakings

<i>Subsidiary undertakings (wholly owned):</i>	Country of incorporation, registration and principal operations	Activity
South West Water Services Limited*	England	Water and sewerage services
Haul Waste Group Limited*	England	Holding company
Haul Waste Limited	England	Waste management
Haul Waste Disposal Limited	England	Waste management
ELE Group Limited*	England	Holding company
ELE International Limited	England	Instrumentation
ELE International Inc.	United States	Instrumentation
GLI International Limited	England	Instrumentation
Water West Limited*	England	Holding company
Exe International Inc.	United States	Holding company
GLI International Inc.	United States	Instrumentation
T J Brent Limited*	England	Construction services
Exe Continental Limited*	England	Holding company
Peninsula Insurance Limited*	Guernsey	Insurance
Peninsula Properties (Exeter) Limited*	England	Property development

Shares of those undertakings marked with an asterisk (*) were held directly by the Company. Otherwise, except for Haul Waste Disposal Limited, all the shares of subsidiary undertakings were held by the immediately preceding holding company in the list above. All shares in issue are ordinary shares except those of Haul Waste Disposal Limited.

Haul Waste Disposal Limited has ordinary, preference and deferred shares in issue. The ordinary and deferred shares are held by Haul Waste Group Limited and the preference shares are held by South West Water Plc.

<i>Associated undertakings:</i>	Share and loan capital in issue	Percentage held	Activity
Societa Italo Britannica dell'Acqua Srl (Incorporated in Italy, and shares held by Exe Continental Limited)	20 billion lire share capital	50%	Construction and operating concessions
	18 billion lire subordinated loan stock	50%	



Notes to the financial statements

30 Pensions

The Group operates a number of pension schemes. The two major schemes are funded defined benefit schemes and the assets of the schemes are held in separate trustee administered funds.

The latest actuarial valuations of the two main schemes were at 31 March 1996. At that date, the market value of the schemes' assets was £140.2m, and the actuarial value of those assets represented 135% and 146% of the benefits that had accrued to members, after allowing for expected future increases in earnings. The assumptions which have the most significant effect on the results of the valuations are those relating to the rate of return on investments and the rates of increase in earnings and pensions. The valuations assume that the investment return would be 9% per annum and pensionable pay increases would average 7% per annum and that present and future pensions would increase at a rate of 4.5% and 5% per annum for the two main schemes.

The pension cost of the defined benefit schemes has been determined on the advice of independent qualified actuaries using the projected unit method. The employers' regular pension cost for the year of the two main schemes is 11.0% and 14.2% of pensionable earnings (1996 10.3% and 13.8%). The actuarial surpluses for the two main schemes are being recognised using the straight line method of amortisation over the average remaining service lives of the current members of each scheme. Because of the actuarial surpluses the net pension credit for the year ended 31 March 1997 was £2.0m (1996 £8.1m, including a £7.3m exceptional item). Following the actuarial valuations, employer contributions to the two main schemes have ceased until the next actuarial review (which is expected to be in 1999).

Pension prepayments included as debtors of the Group amount to £8.2m (1996 £5.4m), representing the accumulated difference between the Group pension credits and employer contributions paid.

31 Commitments and contingent liabilities

	Group		Company	
	1997 £m	1996 £m	1997 £m	1996 £m
<i>Capital commitments</i>				
Contracted but not provided	59.4	28.6	—	—
<i>Commitments under operating leases</i>				
Rentals during the year following the balance sheet date:				
Land and buildings - leases expiring:				
Within one year	0.1	0.1	—	—
Between one and five years	0.4	0.2	—	—
After five years	1.7	0.4	—	—
Other - leases expiring:				
Within one year	0.2	—	—	—
Between one and five years	0.2	—	—	—
	2.6	0.7	—	—
<i>Contingent liabilities</i>				
Contractors' claims on capital schemes	16.7	18.8	—	—
Guarantees	4.9	4.9	274.7	292.5
	21.6	23.7	274.7	292.5

Guarantees by the Company are principally in respect of borrowing facilities of subsidiary undertakings.

32 Notes to the Group cash flow statement

a Reconciliation of operating profit to net cash inflow from operating activities

	1997 £m	1996 £m
Operating profit	130.2	134.1
Depreciation charge	35.5	31.7
Provision for fixed asset investment	0.4	—
Deferred income released to profits	(1.2)	(0.8)
Decrease in provisions for liabilities and charges	(1.2)	(21.1)
Decrease/(increase) in stocks	1.1	(2.7)
Increase in debtors (amounts falling due within and over one year)	(14.3)	(6.9)
Increase in creditors (amounts falling due within and over one year)	5.8	8.5
Profit on disposal of tangible fixed assets	(0.4)	(0.3)
Net cash inflow from operating activities	155.9	142.5

Cash outflows from operating activities accounted for as exceptional items, included above, were £9.0m (1996 £11.8m). These relate to the utilisation of the restructuring provision established in 1995 and costs associated with the proposed bids.

Notes to the financial statements

32 Notes to the Group cash flow statement continued

b Analysis of cash flows for headings netted in the Group cash flow statement

	1997	1996
	£m	£m
<i>(i) Returns on investments and servicing of finance</i>		
Interest received	23.9	23.4
Interest paid	(38.4)	(39.3)
Interest element of finance lease rentals	(4.4)	(4.7)
Costs associated with defeased leases (note 6)	(0.6)	–
Gain on currency hedge	0.7	–
Dividends received	0.2	0.4
Net cash outflow for returns on investments and servicing of finance	(18.6)	(20.2)
<i>(ii) Capital expenditure and financial investment</i>		
Purchase of tangible fixed assets	(147.5)	(109.8)
Grants and contributions:		
Infrastructure assets	3.7	3.2
Non-infrastructure assets	0.6	0.7
Receipts from disposal of tangible fixed assets	1.6	0.8
Loan to associated undertaking	(3.0)	(1.2)
Repayment of loan from associated undertaking	3.0	–
Net cash outflow for capital expenditure and financial investment	(141.6)	(106.3)
<i>(iii) Acquisitions and disposals</i>		
Purchase of businesses	(0.9)	(93.7)
Purchase of interest in associated undertaking	(3.0)	(1.7)
Net cash acquired with businesses	–	2.0
Sale of businesses:		
Associated undertakings	17.8	0.4
Other businesses	14.1	–
Net cash inflow/(outflow) for acquisitions and disposals	28.0	(93.0)
<i>(iv) Management of liquid resources</i>		
Purchase of current asset investments	(353.5)	(354.0)
Sale of current asset investments	372.4	590.6
Net cash inflow from management of liquid resources	18.9	236.6

Liquid resources comprise readily disposable current asset investments.

32 Notes to the Group cash flow statement continued

b Analysis of cash flows for headings netted in the Group cash flow statement – continued

<i>(v) Financing</i>	1997 £m	1996 £m
Issue of ordinary share capital	5.3	1.8
Adjustment for shares issued under Sharesave Scheme through employee share ownership trust	(0.9)	–
	4.4	1.8
Debt due within one year (other than bank overdrafts): (reduction)/increase	(8.2)	35.0
Debt due after more than one year: reduction	(0.1)	(4.7)
Cash deposited against finance lease obligations (note 26)	–	(150.0)
Cash placed on deposit with financial institutions (note 6)	(52.7)	–
Defeased finance lease drawdowns (note 6)	65.4	–
Other finance lease drawdowns	8.1	12.5
Capital element of finance lease rental payments	(6.6)	(6.1)
	5.9	(113.3)
Net cash inflow/(outflow) from financing	10.3	(111.5)

c Analysis of net debt

	At 1 April 1996 £m	Cash flow £m	Non-cash movements £m	Currency retranslation £m	At 31 March 1997 £m
Cash at bank and in hand	0.9	1.6	–	(0.1)	2.4
Current asset investments: overnight deposits	0.6	4.1	–	–	4.7
Bank overdrafts	(2.2)	0.8	–	0.1	(1.3)
	(0.7)	6.5	–	–	5.8
Debt due within one year (other than bank overdrafts)	(48.1)	8.2	(94.4)	–	(134.3)
Debt due after more than one year	(351.3)	0.1	94.4	–	(256.8)
Finance lease obligations	(144.2)	(14.2)	7.3	–	(151.1)
	(543.6)	(5.9)	7.3	–	(542.2)
Current asset investments: other than overnight deposits	199.5	(18.9)	–	–	180.6
	(344.8)	(18.3)	7.3	–	(355.8)

Non-cash movements include transfers between categories of debt for changing maturities, principally sterling notes, £85.4m, and the in-substance settlement of finance lease obligations, £12.7m (note 6).



Notes to the financial statements

32 Notes to the Group cash flow statement continued

d Reconciliation of net cash flow to movement in net debt

	1997 £m	1996 £m
Increase in cash in the period	6.5	7.8
Cash (inflow)/outflow from (increase)/decrease in debt and finance leasing	(5.9)	113.3
Cash inflow from decrease in liquid resources	(18.9)	(236.6)
Change in net debt arising from cash flows	(18.3)	(115.5)
Non-cash movements:		
In-substance settlement of finance lease obligations	12.7	–
Finance lease obligations of businesses acquired	–	(0.1)
Other	(5.4)	(0.7)
Increase in net debt in the year	(11.0)	(116.3)
Net debt at 1 April	(344.8)	(228.5)
Net debt at 31 March	(355.8)	(344.8)

e Purchase of businesses

	1997 £m	1996 £m
Net assets acquired:		
Tangible fixed assets	0.2	42.5
Associated undertakings	–	1.5
Cash at bank and in hand	–	2.7
Other current assets	–	8.6
Bank overdraft	–	(0.7)
Provisions for liabilities and charges	(1.0)	(10.3)
Finance lease obligations	–	(0.1)
Other current and non-current liabilities	–	(9.5)
Fair value of net assets acquired	(0.8)	34.7
Goodwill	1.7	68.3
	0.9	103.0
Satisfied by:		
Cash consideration	0.9	95.4
Loan stock	–	0.4
Contingent consideration	–	7.2
	0.9	103.0

During 1997 £3.0m of the contingent consideration, arising on businesses purchased in 1996, was paid (1996 nil), £0.4m was satisfied by the issue of loan stock, £1.8m was released following a revision of provisional numbers (note 28), and £2.0m remains payable.

The businesses acquired during the year did not materially contribute to the Group's cash flows.

32 Notes to the Group cash flow statement continued

f Sale of businesses

	1997	1996
	£m	£m
Net assets disposed of:		
Tangible fixed assets	13.1	—
Goodwill written back to reserves	0.4	—
	13.5	—
Profit on disposal	4.1	—
	17.6	—
Satisfied by:		
Cash consideration	14.1	—
Deferred consideration	3.5	—
	17.6	—

In addition, a sale of the Group's investment in associated undertakings for a cash consideration of £17.8m (1996 £0.4m) realised a profit on disposal of £15.1m (1996 nil).

The businesses sold during the year did not materially contribute to the Group's cash flows.

The introduction of Financial Reporting Standard 1 (Revised 1996) 'Cash Flow Statements' has required revised presentation of certain comparative figures.

33 Related party transaction

On 3 May 1996 Exe Continental Limited, a 100% owned Group company, subscribed for 7 billion lire (equivalent to £3.0m) of subordinated loan stock in Societa Italo Britannica dell'Acqua Srl, an associated undertaking (additional to 3 billion lire at 31 March 1996). Repayment of 1 billion lire (equivalent to £0.4m) of loan stock has been waived.

Five year financial summary

	1997	1996	1995	1994	1993
	£m	£m	£m	£m	£m
Profit and loss account					
Turnover	343.6	314.4	286.2	251.6	194.4
Operating profit	130.2	134.1	86.2	106.4	82.8
Business disposal profits	19.2	–	–	–	–
Income/(loss) from interests in associated undertakings	1.2	1.6	1.2	0.7	(2.0)
Net interest (payable)/receivable	(18.0)	(26.6)	(24.2)	(14.1)	11.9
Profit on ordinary activities before taxation	132.6	109.1	63.2	93.0	92.7
Tax on profit on ordinary activities	(14.3)	(10.3)	(8.2)	(7.1)	(8.5)
Profit on ordinary activities after taxation	118.3	98.8	55.0	85.9	84.2
Dividends	(47.4)	(38.9)	(34.5)	(32.0)	(29.5)
Retained profit transferred to reserves	70.9	59.9	20.5	53.9	54.7
Earnings per share	92.1p	77.7p	43.7p	68.5p	67.9p
Dividend per share	36.7p	30.5p	27.3p	25.5p	23.7p
Capital expenditure	£m	£m	£m	£m	£m
Acquisitions and investment	0.9	103.0	0.2	17.9	32.1
Tangible fixed assets	157.2	110.3	159.4	203.4	203.7
Balance sheet	£m	£m	£m	£m	£m
Fixed assets	1,397.8	1,301.2	1,182.2	1,063.0	882.1
Net current (liabilities)/assets	(42.9)	63.6	349.5	375.9	394.0
Non-current liabilities	(439.0)	(524.7)	(687.4)	(617.6)	(496.6)
Net assets	915.9	840.1	844.3	821.3	779.5
Number of employees (average for year)					
Water and sewerage services	1,765	1,815	2,084	2,141	2,144
Waste management	297	322	271	242	35
Environmental instrumentation	411	357	255	244	119
Construction services	567	398	339	291	111
Other businesses	113	113	134	142	147
	3,153	3,005	3,083	3,060	2,556

Shareholder information

Financial calendar

Financial year end	31 March
Eighth annual general meeting	29 July 1997
1997 Final dividend payable	1 October 1997
1998 Interim results announcement	November 1997
1998 Interim dividend payable	April 1998
1998 Preliminary results announcement	May 1998
Ninth annual general meeting	July 1998
1998 Final dividend payable	October 1998

Shareholders' analysis at 31 March 1997

	Number of shareholders	Percentage of total shareholders	Percentage of ordinary shares
1 - 100	4,430	14.1	0.2
101 - 1,000	23,084	73.4	7.2
1,001 - 5,000	3,165	10.1	3.9
5,001 - 50,000	487	1.5	7.4
50,001 - 100,000	105	0.3	5.9
Over 100,000	198	0.6	75.4
	<hr/>	<hr/>	<hr/>
	31,469	100.0	100.0
	<hr/>	<hr/>	<hr/>
Individuals	29,064	92.3	10.7
Companies	422	1.3	4.3
Trust companies (pension funds, etc)	14	0.1	0.1
Banks and nominees	1,947	6.2	82.6
Insurance companies	22	0.1	2.3
	<hr/>	<hr/>	<hr/>
	31,469	100.0	100.0
	<hr/>	<hr/>	<hr/>

Shareholder services

Share dealing service

The low-cost share dealing service enables investors to buy and sell shares in the Company on a low-cost basis and to make regular investments in the Company.

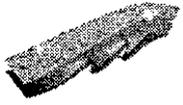
Personal equity plans

By holding their shares in the Company in the general or the single company personal equity plan, shareholders may gain tax advantages.

Scrip dividend alternative

The scrip dividend alternative enables shareholders to receive their dividends in the form of shares instead of cash.

Details of the scrip dividend alternative are enclosed and details of the other shareholder services are available from the Company Secretary's Department (telephone: (01392) 446688).



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