

2015 HIGHLIGHTS

Group turnover

£1,801.3m

2014: £1,756.7m (restated)**

Group underlying profit before tax*

£300.4m

2014: £276.1m (restated)**

Group profit before tax

£148.2m

2014: £318.9m (restated)**

Dividend per share

84.90p

2014: 80.40p

Earnings per share**

107.2p

2014: 92.5p (restated)**

* Before tax, exceptional items and gains/losses on financial instruments.

** Before deferred tax, exceptional items and gains/losses on financial instruments.

*** Restated to classify Water Purification as a discontinued operation.

- Good financial performance:
 - Adjusted EPS up 15.9% year on year
 - Underlying group PBIT £540.3 million, up 3.2% year on year
 - Reported group PBIT up 2.6% year on year
- Focus on operational improvement:
 - Improved or stable performance on 12 out of 14 Ofwat KPIs year on year
 - Achieved target of 10% reduction in leakage over AMP5
- Invested a further £547.4 million to complete AMP5 programme of £2.6 billion: RCV¹ £7.7 billion at April 2015
- Customer bills remain the lowest in Britain at £329 for 2015/16
- Severn Trent Services re-focused – disposal of Water Purification business (US\$81.2 million)
- Industry leader in renewable energy – self generation equivalent to 28% of Severn Trent Water's energy needs
- Reported group PBT £148.2 million, reflecting fair value losses on financial instruments
- Well positioned for AMP6:
 - Largest investment programme ever – £3.3² billion capital investment
 - New organisational structure and management team
 - £300 million of £372 million target efficiencies already locked in
 - Focused on outperformance
 - 2015/16 dividend 80.66 pence, followed by annual growth of no less than RPI until 2020

1 Regulatory Capital Value
2 At 2012/2013 prices

Cautionary statement

This document contains statements that are, or may be deemed to be, 'forward-looking statements' with respect to Severn Trent's financial condition, results of operations and business and certain of Severn Trent's plans and objectives with respect to these items.

Forward-looking statements are sometimes, but not always, identified by their use of a date in the future or such words as 'anticipates', 'aims', 'due', 'could', 'may', 'will', 'would', 'should', 'expects', 'believes', 'intends', 'plans', 'projects', 'potential', 'reasonably possible', 'targets', 'goal' or 'estimates' and, in each case, their negative or other variations or comparable terminology. Any forward-looking statements in this document are based on Severn Trent's current expectations and, by their very nature, forward-looking statements are inherently unpredictable, speculative and involve risk and uncertainty because they relate to events and depend on circumstances that may or may not occur in the future.

Forward-looking statements are not guarantees of future performance and no assurances can be given that the forward-looking statements in this document will be realised. There are a number of factors, many of which are beyond Severn Trent's control, that could cause actual results, performance and developments to differ materially from those expressed or implied by these forward-looking statements.

These factors include, but are not limited to, changes in the economies and markets in which the group operates; changes in the regulatory and competition frameworks in which the group operates; the impact of legal or other proceedings against or which affect the group; and changes in interest and exchange rates.

All written or verbal forward-looking statements, made in this document or made subsequently, which are attributable to Severn Trent or any other member of the group or persons acting on their behalf are expressly qualified in their entirety by the factors referred to above. Subject to compliance with applicable laws and regulations, Severn Trent does not intend to update these forward-looking statements and does not undertake any obligation to do so.

Nothing in this document should be regarded as a profits forecast.

This document is not an offer to sell, exchange or transfer any securities of Severn Trent Plc or any of its subsidiaries and is not soliciting an offer to purchase, exchange or transfer such securities in any jurisdiction. Securities may not be offered, sold or transferred in the US absent registration or an applicable exemption from the registration requirements of the US Securities Act of 1933 (as amended).

Financial review

Chief Financial Officer's review

The group has delivered a good financial performance in 2014/15, underpinned by continuing improvements and growth in our regulated business, and continued revenue growth in our non-regulated Severn Trent Services business.

On 13 May 2015 we announced the sale of our Water Purification business to Industrie De Nora. The disposal follows a successful turnaround of the business, and will enable our reorganised Business Services division to focus on its core strengths in water, waste, retail and renewables. The Water Purification business has been classified as a discontinued operation, and our prior year results have been restated to reflect this.

We made some important changes to our financing structure at the end of the year, to reduce short term financing risk and increase exposure to currently low floating interest rates. These included replacing our revolving credit facility with a new £900 million facility and negotiating and drawing down on a new £530 million European Investment Bank (EIB) facility. In addition, we cancelled some floating to fixed interest rate swaps and purchased €183 million of our fixed rate €700 million Eurobond loan, due for repayment in March 2016, which resulted in a one time financing charge of £6.6 million in 2014/15. As a result, we have reduced the interest cost on £415 million of debt and swaps from an average interest rate of 5.1% to a floating rate, currently 1%. This has moved the proportion of our debt that is at floating rates to 10%, in line with our stated policy for AMP6 to increase the level of variable rate debt. Further details are set out in the Treasury management and liquidity section below.

A brief overview of our financial performance for the year is as follows:

Group turnover from continuing operations was £1,801.3 million (2013/14: £1,756.7 million), an increase of 2.5%.

Underlying PBIT¹ increased by 3.2% to £540.3 million (2013/14: £523.8 million).

Net exceptional charges before tax totalled £18.7 million (2013/14: £15.2 million).

Reported group PBIT¹ was £521.6 million (2013/14: £508.6 million).

Net finance costs were £240.0 million (2013/14: £247.9 million).

1. PBIT is profit before interest and tax; underlying PBIT excludes exceptional items as set out in note 8.

Regulated – Severn Trent Water

In Severn Trent Water, underlying PBIT increased by 3.9% to £539.0 million (2013/14: £518.6 million).

Turnover increased by £36.4 million, or 2.4%, to £1,581.2 million as a result of price increases of 1.5% (£23.0 million); higher consumption from metered commercial customers (£1.9 million); growth, net of meter optants (£1.0 million) and other increases including tariff mix effects of £10.5 million.

Operating costs, excluding depreciation and infrastructure maintenance expenditure, increased in line with expectations by 3.1% to £619.1 million.

	2015	2014	Increase/(decrease)	
	£m	£m	£m	%
Employee costs	248.4	242.0	6.4	2.6
Hired and contracted	163.8	154.1	9.7	6.3
Costs capitalised	(92.4)	(92.6)	0.2	0.2
Raw materials and consumables	47.4	42.5	4.9	11.5
Power	63.9	65.3	(1.4)	(2.1)
Bad debts	28.4	31.3	(2.9)	(9.3)
Rates and service charges	113.2	112.3	0.9	0.8
Other	46.4	45.4	1.0	2.2
	619.1	600.3	18.8	3.1

Employee costs were 2.6% higher, broadly in line with annual pay inflation. The benefits of the recent reorganisation, which included a reduction of 500 roles, will be seen from 2015/16. Hired and contracted costs were 6.3% higher as we invested in key operational areas, such as sewer blockages and mains cleaning, to make a fast start in AMP6. The benefits of this will flow through to 2015/16. Raw materials and consumables increased by £4.9 million due to inflation and additional spending on water quality improvements.

Power costs decreased by £1.4 million. We continue to make good progress on our renewable energy generation, and generated the equivalent of 28% of gross consumption from self-generation in the year, providing an effective hedge against energy price volatility.

Bad debt charges improved to 2.0% of turnover (UK GAAP), down from 2.2% in 2013/14 as we saw the benefit of improved collection of older household debt and a range of social tariffs which help customers pay their bills.

Depreciation increased by £2.7 million, due to the growing asset base. Infrastructure maintenance expenditure declined £5.5 million due to operational efficiencies and programme phasing as we closed out AMP5.

We completed our planned capital programme for AMP5, investing £547.4 million (UK GAAP, net of grants and contributions) during the year. Included in this total was net infrastructure maintenance expenditure of £134.8 million, which is charged to the income statement under IFRS.

Non-regulated – Severn Trent Services

	2015	2014	Increase/
	£m	Restated £m	(decrease) %
Turnover			
Services as reported	216.3	210.2	2.9%
Impact of exchange rate fluctuations	–	(3.5)	
Like for like	216.3	206.7	4.6%
Underlying PBIT			
Services as reported	9.7	13.3	(27.1%)
Like for like	9.7	13.3	(27.1%)

The results above exclude the Water Purification business, which has been classified as a discontinued operation.

Financial review continued

In Severn Trent Services we saw good growth in turnover, up 4.6% on a constant currency basis to £216.3 million.

Underlying PBIT was down £3.6 million to just under £10 million. This was due to business development investment in US concessions and a number of one off favourable items in the prior year.

Corporate and other

Corporate overheads totalled £13.2 million (2013/14: £13.6 million). Our other businesses generated a net profit of £1.1 million (2013/14: £2.5 million).

Exceptional items before tax

Net exceptional operating costs totalled £18.7 million (2013/14: £15.2 million) and included:

- In our regulated business:
 - £28.3 million of restructuring costs to transform the business for AMP6, reducing the cost base and de-layering the management levels; offset by
 - £7.7 million of profit on disposal of property.
- In our non-regulated business:
 - £4.4 million of restructuring costs to prepare the business for retail competition in AMP6 and to reduce the cost base; offset by
 - the release of a £6.3 million provision previously made against accounts receivable in Italy.

Net finance costs

The group's net finance costs were £240.0 million, down from £247.9 million in the prior year. The benefits of lower interest rates (in particular on our RPI linked debt) were partially offset by higher levels of net debt.

In addition, in March 2015 the group reduced 2015/16 financing risk by purchasing approximately 26% of the €700.0 million, fixed rate Eurobond which is due for repayment in March 2016. This led to a charge of £6.6 million in finance costs.

Profit before tax

Underlying group profit before tax increased by 8.8% to £300.4 million (2013/14: £276.1 million). Group profit before tax was £148.2 million (2013/14: £318.9 million).

Taxation

The total tax charge for the year was £32.7 million (2013/14: credit of £152.9 million).

The current year tax charge for 2014/15 was £37.8 million (2013/14: £55.8 million before exceptional tax). The deferred tax credit was £5.1 million (2013/14: charge of £21.5 million before exceptional tax).

In the prior year there was an exceptional current tax credit of £59.2 million and an exceptional deferred tax credit of £171.0 million.

See note 13 for further detail.

The underlying effective rate of current tax on continuing operations, excluding prior year credits, exceptional tax credits and tax on exceptional items and financial instruments, calculated on profit from continuing operations before tax, exceptional items and gains/(losses) on financial instruments was 17.6% (2013/14: 17.3%).

We expect the effective rate of current tax, as defined above, for 2015/16 to be in the range of 17% to 19%.

Reported group profit for the period and earnings per share

After a profit of £4.7 million (2013/14: loss of £36.9 million) from discontinued operations, reported group profit for the period was £120.2 million (2013/14: £434.9 million). The decrease was a result of a fair value loss on financial instruments, largely due to lower expectations for future interest rates, and an exceptional tax credit in the prior year which arose from an agreement with HMRC on a long standing discussion regarding overpayments of tax in prior periods.

Adjusted basic earnings per share (from continuing operations, before exceptional items, gains/(losses) on financial instruments, current tax on gains/(losses) on financial instruments and deferred tax) was 107.2 pence (2013/14: 92.5 pence) (see note 15). The main drivers of the increase were an increase in underlying PBIT, as described above, a lower interest charge due to lower RPI year on year, and a lower current tax charge arising from adjustments of prior year computations.

Basic earnings per share were 49.9 pence (2013/14: 182.1 pence).

Group cash flow

	2015 £m	2014 £m
Cash generated from operations	760.1	730.2
Net capital expenditure	(416.1)	(463.9)
Net interest paid	(218.2)	(204.5)
Payment to close out interest rate swaps	(139.2)	-
Tax (paid)/received	(28.6)	27.2
Other cash flows	(1.4)	(0.6)
Free cash flow	(43.4)	88.4
Acquisitions and disposals	-	(11.4)
Dividends	(196.9)	(185.3)
Net issue of shares	(16.7)	2.3
Change in net debt from cash flows	(257.0)	(106.0)
Non cash movements	(48.1)	(44.2)
Change in net debt	(305.1)	(150.2)
Net debt 1 April	(4,447.5)	(4,297.3)
Net debt at 31 March	(4,752.6)	(4,447.5)
Net debt comprises:		
Cash and cash equivalents	176.7	123.2
Bank loans	(1,279.2)	(594.9)
Other loans	(3,467.5)	(3,826.0)
Finance leases	(180.0)	(201.2)
Cross currency swaps hedging debt	(2.6)	51.4
	(4,752.6)	(4,447.5)

Tax paid was £28.6 million (2013/14: received £27.2 million). The group has obtained agreement with HMRC to offset quarterly tax payments for the current year against a refund of overpayment of tax in prior periods, as outlined in the prior year results announcement.

Net debt at 31 March 2015 was £4,752.6 million (2013/14: £4,447.5 million). Balance sheet gearing (net debt/net debt plus equity) at the year end was 85.2% (2013/14: 80.3%). Net debt, expressed as a percentage of RCV at 31 March 2015 of £7,740 million was 61.4% (2013/14: 58.4%). The group's net interest charge, excluding gains/(losses) on financial instruments and net finance costs from pensions, was covered 3.5 times (2013/14: 3.3 times) by profit before interest, tax, depreciation and exceptional items, and 2.3 times (2013/14: 2.1 times) by underlying PBIT.

The fair value of net debt at 31 March 2015 is estimated to be £5,645.4 million (2013/14: £4,799.7 million) compared to the book value of £4,752.6 million (2013/14: £4,447.5 million). The difference between the book value and fair value of debt arises from fixed rate and index linked debt where the interest rate on the debt is higher than prevailing market rates at the year end.

Treasury policy and operations

Our treasury affairs are managed centrally and in accordance with our Treasury Procedures Manual and Policy Statement. The treasury operation's role is to manage liquidity, funding, investment and our financial risk, including risk from volatility in interest and (to a lesser extent) currency rates and counterparty credit risk. The board determines matters of treasury policy and its approval is required for certain treasury transactions. The board has established a Treasury Committee to monitor treasury activities and to facilitate timely responses to changes in market conditions when necessary.

Our strategy is to access a broad range of sources of finance to obtain both the quantum required and lowest cost compatible with the need for continued availability. Our principal operating subsidiary, Severn Trent Water, is a long term business characterised by multi year investment programmes. Our strategic funding objectives reflect this and the liquidity position and availability of committed funding are essential to meeting our objectives and obligations. We therefore aim for a balance of long term funding or commitment of funds across a range of funding sources at the best possible economic cost. The group also seeks to maintain an investment grade credit rating and a flexible and sustainable balance sheet structure.

We use financial derivatives solely to manage risks associated with our normal business activities. We do not hold or issue derivative financial instruments for financial trading.

Except for debt raised in foreign currency, which is fully hedged, our business does not involve significant exposure to foreign exchange transactions. We have investments in various assets denominated in foreign currencies, principally the US dollar and the euro. Our current policy is to hedge an element of the currency translation risk associated with certain foreign currency denominated assets.

The group issues notes in foreign currency under its European Medium Term Note (EMTN) programme and uses cross currency swaps to convert the proceeds to sterling. The effect of these swaps is that interest and principal payments on the borrowings are denominated in sterling and hence the currency risk is eliminated. The foreign currency notes and the cross currency swaps are recorded in the balance sheet at their fair values and the changes in fair values are taken to gains/(losses) on financial instruments in the income statement. Since the terms of the swaps closely match those of the underlying notes, such changes tend to be broadly equal and opposite.

Treasury management and liquidity

In February and March 2015, the group took a number of financing steps in readiness for AMP6, aimed at reducing short term refinancing risk and increasing exposure to currently low floating interest rates. These steps included:

- Entering into a new £530.0 million, floating rate, nine year facility with the EIB. At 31 March 2015, £200 million of the facility had been drawn, with the balance drawn down in April 2015.
- On 31 March 2015 the group purchased €182.6 million of its €700 million Eurobond which is due for repayment in March 2016. On the same date the equivalent amount of the corresponding swap, paying fixed rate 6.325%, was cancelled.
- In March 2015 the group cancelled floating to fixed interest rate swaps with a notional principal amount of £275 million, for a cash payment of £139.2 million. The average fixed rate interest on the swaps was 5.2%. The cash payment was charged against the fair value liability on the balance sheet, and £11 million that had been recognised in reserves was recycled through the income statement.
- On 19 March 2015 the group amended and extended the revolving credit facility which was due to mature in October 2018. The new £900 million facility has a period of five years, with two one year extension options exercisable with lender consent. At 31 March 2015 £485 million of the facility was drawn.

The group continues to ensure it has adequate liquidity to support business requirements and provide headroom for downside risk. At 31 March 2015 the group had £176.7 million (2013/14: £123.2 million) in cash and cash equivalents and committed undrawn facilities amounting to £745.0 million (2013/14: £500 million).

The group is funded for its projected investment and cash flow needs up to at least July 2016.

Cash is invested in deposits with financial institutions benefiting from high credit ratings and the list of counterparties is reviewed regularly.

The group's policy for the management of interest rate risk requires that not less than 45% of the group's borrowings should be at fixed interest rates, or hedged through the use of interest rate swaps or forward rate agreements. Going forward, the group intends to manage its existing debt portfolio and future debt issuance to increase the proportion of debt which is at floating rates. At 31 March 2015, interest rates for 67% (2013/14: 77%) of the group's net debt of £4,752.6 million were at fixed rates of interest.

Financial review continued

The group uses financial derivatives solely to hedge risks associated with its normal business activities including:

- Exchange rate exposure on borrowings denominated in foreign currencies;
- Interest rate exposures on floating rate borrowings; and
- Exposures to increases in electricity prices.

Accounting rules require that these derivatives are revalued at each balance sheet date and, unless the criteria for cash flow hedge accounting are met, the changes in value are taken to the income statement. If the risk that is being hedged does not impact the income statement in the same period, then an accounting mismatch arises from the hedging activities and there is a net charge or credit to the income statement.

Derivatives are typically held to their full term and mismatches will net out over the life of the instrument. The changes in value that are recorded during the lives of the derivatives, unless crystallised, do not represent cash flows. Therefore the group presents adjusted earnings figures that exclude these non-cash items. In exceptional circumstances the group may terminate swap contracts before their maturity date. The payments or receipts arising from the cancellations are charged or credited against the liability or asset on the balance sheet, and amounts previously recognised in reserves are recycled through the income statement.

The group holds interest rate swaps with a net notional principal of £583.7 million and cross currency swaps with a net notional principal of £396.6 million, which economically act to hedge the interest rate risk on floating rate debt or the exchange rate risk on certain foreign currency borrowings. However, the swaps do not meet the hedge accounting rules of IAS 39 and therefore the changes in fair value are taken to gains/(losses) on financial instruments in the income statement. During the year there was a charge of £183.4 million in relation to these instruments.

An analysis of the amounts charged to the income statement in the period is presented in note 12 to the financial statements.

The group manages its electricity costs through a combination of self generation, forward price contracts and financial derivatives. The group has fixed around 100% of the wholesale energy cost for the first two years of AMP6 and around 50% of the energy cost for the third year of AMP6.

The group's long term credit ratings are:

Long term ratings	Severn Trent Plc	Severn Trent Water
Moody's	Baa1	A3
Standard and Poor's	BBB-	BBB+

The outlook is stable for Standard and Poor's, negative for Moody's.

Pensions

The group operates two defined benefit pension schemes for its UK employees, of which the Severn Trent Pension Scheme (STPS) is by far the largest. The most recent formal triennial actuarial valuations and funding agreements were carried out as at 31 March 2013 for both schemes. As a result, deficit reduction contributions of £40 million in 2013/14, £35 million in 2014/15, £15 million in 2015/16 and £12 million per annum in subsequent years to 2024/25 were agreed. Further payments of £8 million per annum through an asset backed funding arrangement will also continue to 31 March 2032.

As previously announced, the defined benefit schemes closed to future accrual on 31 March 2015. On 1 April 2015, members of the defined benefit schemes were transferred to the defined contribution Severn Trent Group Personal Pension scheme, which was opened on 1 April 2012.

The key actuarial assumptions for the defined benefit schemes have been updated for these accounts. On an IAS 19 basis, the estimated net position of the schemes was a deficit of £468.9 million as at 31 March 2015. This compares to a deficit of £348.3 million as at 31 March 2014. The movements in the net deficit can be summarised as follows:

	£m
Present value at 1 April 2014	(348.3)
Change in actuarial assumptions	(336.8)
Asset outperformance	193.4
Contributions in excess of income statement charge	22.8
Present value at 31 March 2015	(468.9)

Accounting policies and presentation of the financial statements

Our consolidated financial statements are prepared in accordance with International Financial Reporting Standards that have been endorsed by the European Union.

The Strategic Report, as set out from the inside front cover through to page 46, has been approved by the board.

By order of the board

Bronagh Kennedy

Group General Counsel and Company Secretary

21 May 2015