

Interim results for the six months to 30 September 2012

Overview

We have reached the mid-point of the new five-year regulatory period in a strong position. As a business we continue to be focused not only on meeting the requirements of regulators but on outperforming these basic obligations in the interests of customers and our other stakeholders.

This month Ofwat has confirmed that we are, once again, the best performing water and sewerage company in England and Wales in all areas of customer service and we topped Ofwat's Service Incentive Mechanism (SIM).

Meanwhile the Environment Agency has announced that we are the best performing water and sewerage company in their annual Environmental Performance Assessment.

The resilience of our services has been put to the test in the first half of the year. Firstly by the environmental drought in our region, followed by the wettest summer period on record and the resulting flooding, and finally through the Olympic events in Weymouth.

We passed these tests: customer satisfaction with our services has remained high throughout and it is now 36 years since we have imposed a hosepipe ban. We achieved this not only through our consistent and long-term approach to investment but also because of the dedication and the customer-focus of our staff.

Our plans are well laid to ensure we fulfil the obligations agreed in our last price determination up to 2015, and our attention is now shifting towards the future. We have spent the summer developing our Strategic Vision up to 2040. This has been tested with customers and endorsed by the independent Customer Scrutiny Group for our region and will be published in the second half of this year.

This revised Strategic Vision will underpin our business plans for the next regulatory five year period (2015-2020), but we are not waiting until then to implement it. Responding to the squeeze on real incomes we plan to introduce an enhanced social tariff in early 2013. Our tariff has been developed with our partners in the debt advice sector, including Citizens Advice, and will allow customers genuinely unable to afford their bill to pay a fair contribution towards the costs. Alongside this they will receive independent debt advice together with practical help with water efficiency.

Meanwhile, the statutory and regulatory landscape in which we operate continues to evolve.

We support government plans to increase the level of choice for commercial customers in the sector, and believe this could deliver real benefits to customers. We are well placed to respond as we already have a joint venture billing company that delivers the highest levels of service with the lowest costs in the industry.

We remain concerned about proposals for greater competition upstream, but are pleased that government and regulators have recognised that they must not disturb the market's view that the water industry is a good, stable and long term investment.

It would be unrealistic to expect the next few years to be anything but difficult for our customers. But at Wessex Water we will continue to seek to go over and above the basic requirements of our regulators in delivering the services customers want at a price they can afford.

Financial performance

Our results for the half year show that historic cost profit after taxation fell by £3.8m from £61.5m to £57.7m:

- Turnover increased by £12.8m or 5.4% from £235.6m to £248.4m. The regulated tariff turnover increased from £230.9m to £243.1m, mainly due to the allowed price increase stipulated by the industry regulator Ofwat for the third year of the current regulatory period. This agreed increase amounted to 7.4% or £17.1m and comprised November 2011 RPI of 5.2%, a K factor of 1.9% and an allowance for tariff rebalancing of 0.3%. There was an additional £1.5m turnover from new customers. These increases were reduced by the impact of customers switching to metered supply, the continuing economic downturn and the impact of a wet summer. Rainfall in the first 6 months of this year was 639mm compared with 325mm for the same period last year, resulting in less demand for water in the domestic, agricultural, tourism and leisure sectors.
- Operational costs (excluding depreciation and capital maintenance) increased by £6.3m from £66.1m to £72.4m. There were a number of factors behind this increase including a rise in business rates, energy prices and bad debts. There was also the impact of the adoption of Private Sewers in October 2011. Apart from these increases there has been good control of wage inflation and chemical prices, and reduced energy consumption.
- Depreciation and capital maintenance increased by £6.4m from £52.8m to £59.2m. There was an increase of £1.4m on base depreciation, as new assets were depreciated for the first time, and an increase of £3.7m in infrastructure maintenance charges mainly due to the adoption of Private Sewers. There was a profit on disposal of fixed assets of £1.2m last year, which became a loss on disposal of £0.1m this year.
- Net interest payable increased by £3.6m. Underlying interest costs increased by £3.5m from £39.4m to £42.9m principally because the level of debt increased by nearly £100m between the two periods. The average cost of debt increased slightly from 5.0% to 5.1%. There was also an increase of £0.1m in respect of the FRS 17 pension cost.
- Taxation increased by £0.3m from £14.8m to £15.1m. There was a £0.2m reduction in corporation tax as profit before tax fell and a £0.5m increase in deferred taxation which reduced last year's credit of £1.2m to £0.7m this year.

Capital investment for the six months totalled £92.8m representing an increase of almost 40% over the same period last year. There were increases in expenditure on quality, capacity and capital maintenance schemes, including expenditure on the Private Sewers adopted in October 2011.

Net debt increased by £27.5m from £1,626.1m to £1,653.6m in the six months to September 2012. The net cash inflow from operations was £179.6m with cash outflows on the capital investment programme of £87.8m, interest payments of £30.3m, tax payments of £6.0m and dividends of £83.0m.

Dividends declared in the six months to September 2012 were £84.6m compared to £107.8m for the same period last year. Part of the reduction was due to the fact that the dividend for the three months to March 2011 was declared within the six month period last year.

£100m of new bond finance was raised during the six months. This was a tap of an existing £200m bond due for repayment in 2021. Part of the proceeds has been used to repay a £50m term loan with total liquidity at 30 September 2012, being cash plus undrawn bank facilities, now standing at a healthy £297m.

Operational performance & Investment

We continue to make good progress in terms of operational performance and capital investment, and we are on target to meet all 2010-15 milestones and regulatory outputs.

	2011-2012	First half 2011-2012	First half 2012-2013
Customer service			
SIM customer satisfaction score	91%	92%	91%
SIM customer contact score (lower is better)	109	50	55
Billing contacts dealt with in 5 days	100%	100%	100%
Written complaints dealt within 10 days	100%	100%	100%
Water supply			
Risk of receiving low pressure (per 10,000 properties)	3	4	3
Unplanned interruptions over 12 hours (per 10,000 properties)	0.4	0	0
Supply restrictions (per 10,000 properties)	0	0	0
Drinking water compliance	99.98%	99.96%	99.97%
Total leakage (millions of litres per day)	69	70	69
Sewerage			
Risk of internal sewage flooding once or more in 10 years (per 10,000 properties)	0.8	0.8	0.8
Internal sewage floodings (per 10,000 properties)	0.9	0.4	1.0
Environmental standards			
Compliance with EA abstraction licences	100%	100%	100%
Number of pollution incidents	65	44	35
Beaches meeting mandatory standards	100%	100%	94%

Population served by compliant sewage treatment works	100%	100%	100%
Sewage sludge disposed satisfactorily	100%	100%	100%
Carbon emissions (thousand tonnes CO ₂ equivalent)	149	77	81

The summer months of 2012 have collectively recorded 210% of the long term average rainfall and have amounted to the wettest summer on record. The wet weather is the main reason for the increase in the number of internal sewer flooding incidents. It has also driven the fall in Bathing Water compliance in the Wessex Region, and resulted in higher levels of sewerage pumping and sewage treatment which has increased our carbon emissions compared to the same period last year.

Delivering for Customers

Service levels

We continue to put customers at the heart of everything we do and we deliver the best performance on customer service and satisfaction in the industry.

This month Ofwat has confirmed that we are, once again, the best performing water and sewerage company in England and Wales topping Ofwat's Service Incentive Mechanism (SIM) league table for 2011/12.

Performance figures for the first six months of this year indicate that we retain this leading position. Such high satisfaction levels are due, we believe, to our prompt, warm voice telephone answering, knowledgeable, dedicated staff, quick response times, first time resolution of problems and our efforts to keep customers informed of what we are doing at all times.

But we are not standing still. Led by our customer experience group we continue to look for ways to improve service and meet the growing expectations of our customers. Part of this is the formation of a Customer Care team who will be contacting customers when we complete any operational work at their property to check the problem is resolved and they are satisfied with the workmanship.

We are also improving our communication by offering customers more choice in the way they contact us or manage their billing account. We are trialling the use of text messaging during operational work and for those customers who want to make greater use of the internet, widening the range of self service options including the launch of e-billing.

Customer guarantees

Through the Wessex Water Promise we continue to provide customer guarantees and compensation well in excess of the statutory guaranteed standards scheme and have the best overall package of guarantees in the industry.

Affordability

The continuing fragile economic climate is bringing growing affordability problems to our customers. Our commitment to tackling this issue is reflected in our strong partnership work with Citizens Advice, other debt advice agencies across our region and National Debtline (Money Advice Trust) to improve the availability of debt advice to customers struggling to pay. This is delivering real benefits for customers, debt advice workers and Wessex Water alike.

Our Assist tariff continues to be popular with more than 8,000 customers now on the tariff. Assist reduces charges to customers who are in extreme financial difficulty and allows them to make a modest contribution towards the costs of water and sewerage services.

We plan to introduce an enhanced social tariff in early 2013, developed with our partners in the debt advice sector. Alongside this we will increase the financial support that we give to these agencies, and continue to offer customers practical help with water and energy efficiency.

Similarly, our schemes for those who can afford their on-going charges but have fallen into debt, perhaps because of past difficulties, continue to be a success. Restart and Restart Plus are both designed to put customers who are in debt back on track and back into the habit of making regular payments to cover their water bills.

Education and community involvement

We continue to provide an education programme offering a range of services to support schools, teachers and students from primary to university level. We are also working with organisations in our region to reach vulnerable customers, as well as offering community talks on wider water and sewerage issues.

Our community partnership programme, the Wessex Water Partnership, incorporates all our community involvement. In addition, it offers proactive help and advice on water conservation, our affordability schemes, our community support programmes and reinvestment of efficiency savings and customer service improvements.

Meeting new demands

Maintaining the supply of water remains a primary objective and last summer marked the 36th year without supply restrictions in the Wessex Water region.

As a result of low rainfall in 2011/12 Wessex Water region started the current financial year classed by the Environment Agency (EA) as 'in environmental drought'. Despite this we still had sufficient water to meet demand - although groundwater levels and river flows were below average our reservoir storage was satisfactory. We have since experienced the wettest summer on record with rainfall between June and August amounting to 210% of the long term average for these months. At the start of November reservoirs are 99% full and groundwater levels and river flows are above average. We expect to remain in a strong resource position for the remainder of the year.

Following public consultation of the draft Drought Plan between January and March we published our Statement of Response to the representations received in April 2012 – this report outlined changes we would make as a result of the consultation. Further liaison with

the EA occurred throughout the summer to refine our Environmental Monitoring Plan associated with drought permit options. In October we submitted the full Plan to Defra for final approval.

We have maintained our focus on reducing leakage from our extensive network of around 11,500 km of mains and met our leakage target in 2011-12. This level of active leakage control continues into this year and we are confident that we will meet the target again for the full year 2012-13.

Our on-going water efficiency initiatives to help customers reduce their consumption include our schools' education service, free device distribution through WaterSave packs, a campaign with guest accommodation providers, offering free water audits to schools with high water consumption and commercial audits.

We are on course to meet our water efficiency target for 2012-13. Work is also on-going to develop our strategy for 2013/14 and the next price review – we intend to progressively shift our focus more towards practical assistance and device installation in addition to device distribution and education.

The demand for the installation of free meters by customers who pay for their water on an unmeasured basis has increased compared with the corresponding six month period last year.

Liaison with developers and planning authorities has been very active with many large sites, which have been in abeyance for some time, now showing signs of progress. Modelling work and detailed discussions on integrated drainage solutions are underway for several strategically significant sites in Bristol and South Gloucestershire.

Design & construction works are progressing on major sewerage schemes serving new development at Filton Airfield site in Bristol and at sites in Trowbridge, Keynsham and Calne.

Detailed analysis of Local Authority Core Strategies has allowed us to produce growth projections of properties and population. We will use these to assess our water supply, sewerage and sewage treatment needs for use in our business plan submission in 2014.

Improving drinking water and the environment

Our mean zonal compliance for the half year is above the industry-wide level and equal to our average compliance over the past three years. The measure is very sensitive to individual failures. In 2012 there have been 13 failures to date out of the 36,000 tests that have been carried out. Eight of the failures relate to taste and odour from Porlock WTW. We have stopped using this source at times of high risk and our next business plan will include proposals to rationalise the network in this zone and retire this source.

Coping with worsening raw water quality

Deteriorating raw water quality has often triggered multi-million pound investment in water treatment works. To avoid these high-cost schemes and to develop more sustainable solutions we are continuing with our innovative strategy of catchment management.

Our catchment management specialists are working alongside the local farming community to identify potential pollutant pathways and find alternative management practices that protect and improve groundwater quality at 15 sources.

Sutton Bingham water treatment works

Construction is well underway for the major process extensions and extensive maintenance works at this works which serves the Yeovil area. The project will improve the performance of the works, first developed in the 1980s, in dealing with pesticides and taste and odour problems. The civil engineering works are substantially complete and the mechanical and electrical equipment will be installed over the winter of 2012/13.

Mains relining for iron compliance and reduction in discoloured water

Our programme of mains rehabilitation to reduce discoloured water complaints and improve our performance with regard to iron compliance continues. The work is targeted at nine particular high-risk zones and the work completed to date has already shown a beneficial effect in reducing the number of discoloured water contacts.

The largest project within the programme in Taunton, known as 'Taunton Clean and Clear', commenced in the summer of 2012. As with the previous phases of the work we adopt a collaborative approach with the highway authorities and an active public relations campaign with local residents and businesses.

Addressing the impact of water abstraction on river flows

We have an active programme of work to address the concerns that have been raised about our groundwater abstractions and their impact on river flows. In particular, to improve river flows in the Wylde and Bourne catchments, in accordance with the National Environment Programme, abstraction licences will be reduced by a further 23.5 Ml/d once the construction of our proposed water supply grid is completed.

In addition the grid will enable us to move water more effectively around our region and ensure future demand is met.

The planning application for the largest project within the grid – the Corfe Mullen to Salisbury Transfer scheme - will be submitted in November. We are planning to start construction of this major project in late summer 2013.

In the meantime we have completed linked projects at Bulbridge near Salisbury, Corscombe near Yeovil, Lamberts Hill east of Dorchester and the construction of a service reservoir at Kingston St Mary.

In summary, once complete the projects will:

- improve the security of supply to customers, even in the event of a catastrophic source failure
- meet our customers' demands for water over the next 25 years
- meet the reductions in abstraction licences required by the Environment Agency to improve flows in some rivers and protect their ecology

- deal with deteriorating raw water quality, particularly increasing concentrations of nitrates at some of our groundwater sources.

Sewerage and sewage treatment improvements

Sewer flooding

Sewer flooding is rare but when it does happen it is one of the worst service failures our customers and the environment can experience. Substantial investment over recent years has meant that out of more than 1.1 million properties, only 84 were at risk of internal flooding more than once in 10 years because of inadequate capacity - our lowest number ever.

Through further investment we aim to keep the number at risk at around the same level, even in the face of climate change, which is causing more extreme storms. We also propose to reduce the risk of external flooding problems and newly arising flooding problems. We are currently on target to deliver the 527 flooding outputs planned in 2010-15.

The responsibility for flooding is often complex and we are working with local authorities as they produce surface water management plans to investigate these shared ownership problems. We are currently contributing towards these plans in Bournemouth, Bristol, Minehead, Taunton and Weston-super-Mare.

Private Sewer Transfer (Section 105A)

We are now one year on from the transfer of ownership of private sewers. The number of incidents attended on average each month has increased by 75%. Over the year, private sewer incidents amounted to 10,329 out of a total of 28,317 sewerage incidents (36%). We are monitoring the increase in workload and this will be built into our business plan for the next price review.

Storm Overflows

During particularly heavy rainfall storm overflows act as relief valves to ensure properties do not flood. The conditions under which they are allowed to spill are consented by the Environment Agency. We are currently ahead in our five-year programme to improve 65 unsatisfactory storm overflows to watercourses, 63 of which are in Bristol.

We have started appraisals for all these schemes and have a programme to deliver 30 by the end of the financial year.

First-time sewerage

We provide first-time sewerage to communities not connected to the public sewerage system where it can be shown that this is a cost effective solution to any public health or environmental problems.

A scheme at Greinton was successfully completed last year to allow 20 properties to connect to the public sewerage system for the first time. This year a scheme in Radstock is being constructed allowing 6 properties to connect to the public system.

The design of the Cold Harbour (Wareham) scheme, where a local nature reserve is being affected by private sewage discharges, is progressing well for construction next year. We are also appraising the viability of three other applications.

Urban Waste Water Treatment Directive

This European directive sets standards and dates for the treatment of inland and coastal waters to improve the quality of treated sewage discharges to the environment. Designation of two river systems in the Somerset Levels as Sensitive Areas means we are required to install phosphorus removal processes at six of our sewage treatment works (STWs).

In addition phosphorus removal is required at Paulton STW, where the connected population has increased above 10,000. During the first six months of this year we have progressed the design work on these schemes and commenced construction of works at Yeovil and Shepton Mallet STWs.

Revised Bathing Water Directive

The revised EU Bathing Water Directive requires that by 2015 bathing waters must meet tighter microbiological standards.

This means providing improved secondary biological treatment at Weston-super-Mare STW, together with storm storage capacity to reduce the frequency of storm sewage discharges from Black Rock pumping station. Construction of a new activated sludge plant, final settlement tanks and storm tanks began in May 2011 and is progressing well and on schedule for completion by the target date of March 2013.

Other River Quality Improvements

Improvements are required at five other STWs to meet tighter consent standards associated with increases in dry weather flows. Construction has been completed at the first of these STWs (Bishops Lydeard) and has started at Taunton and Puddletown STWs.

Coastwatch

Wessex Water was the first water company in the country to publish information that shows when storm overflows have been in use. The trial in 2011 was very successful and highly praised by local authorities and Surfers Against Sewage. The number of sites within the system doubled in 2012 and includes non-designated amenity waters, such as boating lakes and streams. Wessex Water is one of only two water companies to provide coverage of storm overflow use across all of the bathing waters within their region.

Sludge treatment

All sludge generated from the waste water treatment process is disposed of safely and in a way that meets mandatory standards. The sludge digestion process reduces the volume of sludge while generating renewable energy to minimise our costs and our carbon footprint.

We have a target for 2010-15 to extend and upgrade our sludge digestion facilities. This includes the installation of advanced anaerobic digestion at three of our major sludge

treatment centres. During the first six months of this year we have progressed design work on advanced digestion schemes at Taunton and Berry Hill (Bournemouth) sludge treatment centres and commenced construction at Trowbridge.

Biodiversity and Conservation

Like all water companies Wessex Water has a duty to protect, conserve and enhance the plants and wildlife on the land we own. In recognition of this, we have initiated two five-year projects at 15 sites of high biodiversity potential within our region. We have completed two seasons of survey work on these sites which has yielded some interesting results. The first year of active management is underway including tree surveys and the exploration of grant funding to deliver management actions.

We are working with partners and volunteers to increase the data collection and management of these sites. We are hoping to enter two of our reservoir sites into agri-environment agreements to cover management costs and deliver biodiversity benefits.

Recent government direction has raised the profile of biodiversity and land management to include payments for ecosystems services and biodiversity offsetting. Wessex Water's Partners Programme and Environmental Services Team are leading the way in these areas but there are further opportunities to include these themes in our wider working, particularly through the adoption of a catchment scale approach to deliver the company's environmental objectives.

Investigations

To address future uncertainty surrounding improvements required by European legislation a programme of investigations is taking place to plan capital investment for 2015-20. These started in 2010 and include bathing water investigations at Weston-super-Mare, Burnham and Blue Anchor, the impact of our discharges on algal growth in watercourses and more sustainable methods of phosphorus removal.

These investigations are nearing completion and the results will inform our next Business Plan. Many have been undertaken collaboratively with our environmental regulators improving our working relationships, data gathering and knowledge of environmental issues. The sustainable phosphorus removal investigation at Somerton has recently won two green innovation awards.

Waste management

Wessex Water diverted 89% of non-sludge waste from landfill in the first 6 months of the year, compared with 83% in 2011-12. Long-term pathways have been developed for landfill diversion for each waste stream, from 2013-14 to 2019-20. At the end of this period we aim to be sending virtually no waste to landfill.