United Utilities Group PLC

Full year results
Year ended 31 March 2016

Chief Executive

Steve Mogford

Good morning ladies and gentlemen and welcome to our 2015/16 full year results presentation.

You will see this morning that we have again improved underlying operational performance year-on-year, pressing on with our ambition to be the UK's best water and wastewater company, providing great service to customers. I am encouraged with this continued progress which sees us delivering a net ODI reward in the first year, ahead of our initial expectations.

I gave an overview of our 2015 to 2020 final determination at our results presentation last year. I described it as tough, but within reach, and that we had accepted Ofwat's final position on the basis that it represented a package that we felt we could accept in the round. Since then we have worked hard and been successful in restructuring our plans so that we can be confident of delivering them within our final determination totex allowance. You will see that our plans accelerate investment to secure sustainable operational benefits earlier in the five-year period and that our results underpin our confidence in delivery of our plans.

You may recall that in December there was unprecedented flooding across Cumbria, north Lancashire and Greater Manchester. Our recent investments in improved resilience and our new integrated control centre helped enormously in our handling of these incidents and our team did a tremendous job in maintaining service to customers.

I spoke about last summer's water quality incident at our half year results presentation. We are awaiting publication of the Drinking Water Inspectorate's report on the incident and so there is little more to add on this. However, in the meantime, we have implemented a number of improvements arising out of our learning from this incident.

The test of any team is how it deals with unexpected events and I am very proud of how we all responded to the challenges of last year, always with the interest of customers at the centre of our thinking and action. We have not been knocked off course and our underlying results last year demonstrate that we are on track to deliver value in this regulatory period for both customers and shareholders.

Agenda

- Operational performance
- Financial performance
- Water 2020
- Summary and outlook
- Q&A

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This is the agenda.

This morning we will give you an overview of the key value drivers over this five-year regulatory period, how we have performed in year one and our targets for the remaining four years.

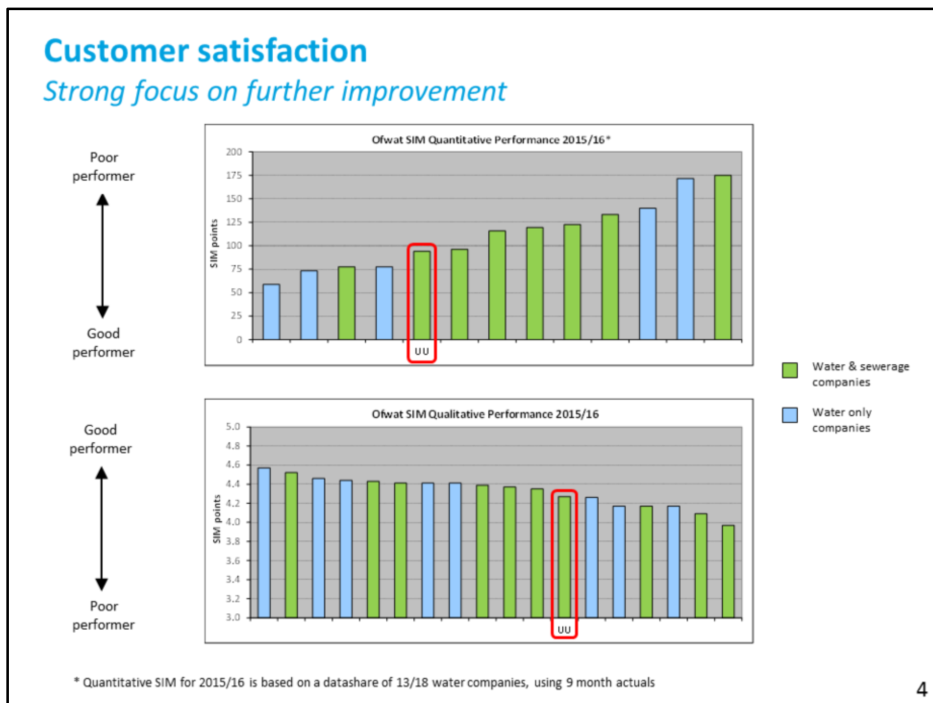
Under the current regulatory framework there are four key drivers of shareholder value - customer service as measured by SIM, totex, outcome delivery incentives or ODIs and financing. I will cover the first three and Russ will cover financing. I have also asked Steve Fraser, Managing Director of our Wholesale business, to provide more colour on our ODI performance last year.

We will also talk about our approach to market reform. As you know, we are an early mover in the development of competitive non-domestic retail services and in March we announced our latest move of a joint venture with Severn Trent.

Russ will then update you on our financial performance.

We are a constructive contributor to the development of Ofwat's Water 2020 thinking and I'll finish with a few thoughts on this and a summary and outlook for the group.

So, starting with customer satisfaction.



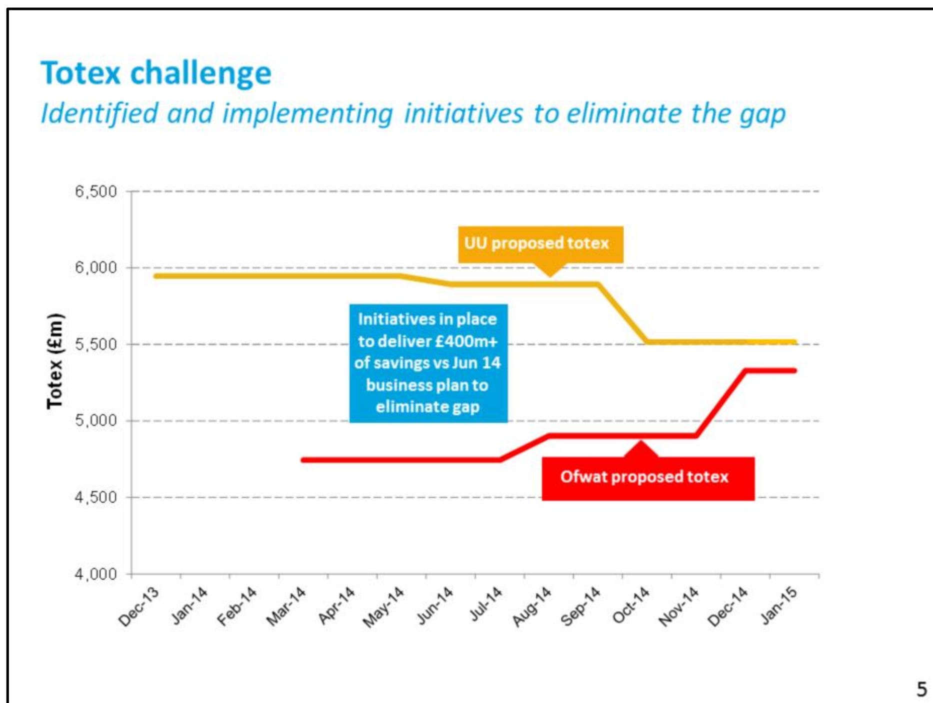
We now have the majority of companies' results for the first year under Ofwat's revised Service Incentive Mechanism, or SIM, and these two charts show companies' relative performance for 2015/16.

The top chart on this slide shows the quantitative results available so far. It is important to note that five companies have opted not to voluntarily data share for quantitative performance and the final picture will change once their data is available. We improved by 4 per cent year-on-year and by over 10 per cent on an underlying basis, adjusting for the exceptional incidents last year. As it stands, we score second amongst the water and wastewater companies and fifth in the sector.

Our qualitative result was affected by last year's incidents but we have since seen customer sentiment bounce back. We look to average the year at around 7th amongst the water and wastewater companies and 12th in sector - as shown on the bottom chart. We were delighted to learn that we scored number one on wastewater in the last qualitative wave – a real testimony to how our team handled the challenges of the floods this winter.

Analysis of our results shows us as one of the water and waste water companies with the fewest customer complaints on a normalised basis. However, our qualitative score shows that we have more to do in how we deal with complaints when we get them - and this is our focus for improvement action. Based upon progress to date, and the volatile nature of the SIM methodology, we are likely to be in the no penalty/no reward band on this measure.

Our ambition is to be held in high regard by those we serve and we continue to conduct regular surveys of customer perception, set against other companies serving our customers in the North West. We are pleased to see that across a range of perception measures, out of ten leading organisations we continue to be ranked only just behind the highly regarded brands of John Lewis and Marks and Spencer. This is important in the context of the potential opening of the domestic market to competition and building brand loyalty will continue to be important to us.



Moving on to totex, you may recall this slide from last year which shows the development of our final determination during the price review PR14. Both we and Ofwat made significant moves toward each other in arriving at our final determination and this left us with the challenge of finding over £400 million savings against our original business plan.

I said last year that we would use the first year of this AMP to develop a plan to meet this challenge and we have done so. We are now confident that we can deliver our promises to customers within our final determination totex allowance. Our performance over the last 12 months, building on the significant improvements of the previous five years, reinforces this view.

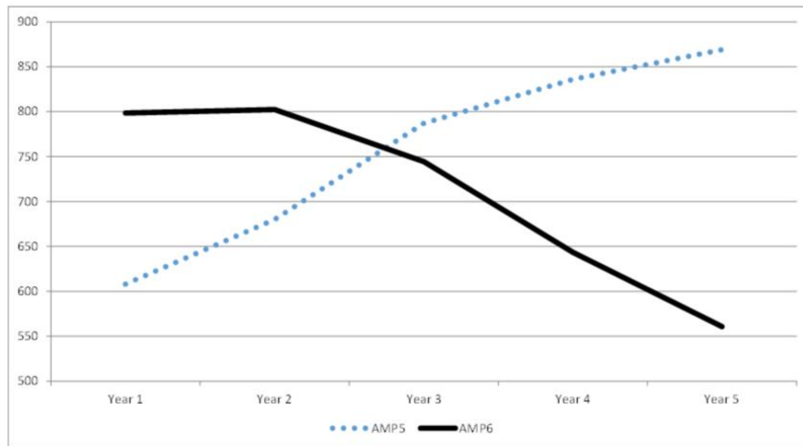
There is no single magic bullet which achieves these savings. Contributions come from a variety of management actions, including:

- our new design and construction partnerships that are delivering innovative solutions at prices that meet our upper quartile efficiency targets;
- active engineering engagement in the field to exploit flexibility between opex and capex solutions afforded by the totex regime;
- reprioritisation of projects;
- exploitation of renewables and energy efficiency to reduce power cost; and
- reduction of out of hours working and overtime through use of remote monitoring and control by our integrated control centre.

We have also accelerated investment to deliver operational benefit earlier and I will touch on this on the next slide.

Net regulatory capital spend profile

Accelerating investment programme – AMP5 vs AMP6 (£m)



NB The AMP6 investment programme shown on this chart does not constitute a forecast and is subject to change

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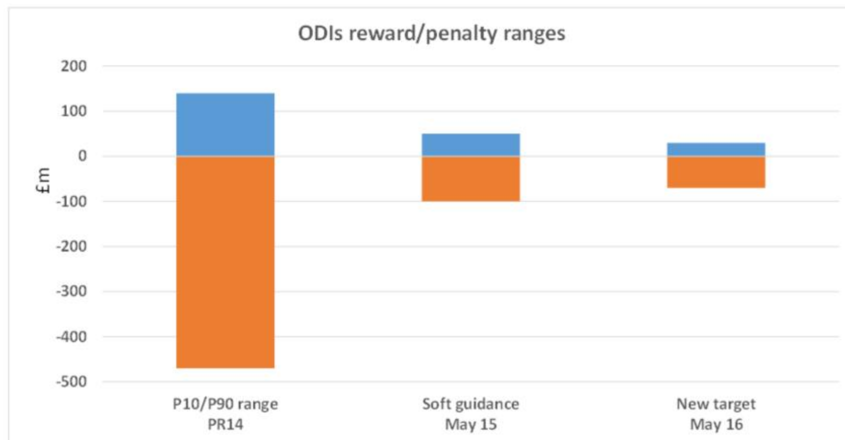
This chart shows our planned investment profile across 2015-20, compared with the last regulatory period.

As you can see, our plan accelerates investment in years one and two of the five-year period to secure earlier operational benefit, particularly in the context of our outcome delivery incentives, or ODIs. You can see that our 2015-20 plan is very different from our actual AMP5 spend profile with spend in year one being around a third higher than that for the first year of AMP5 – and continuing at a similar level in year two. We recognise that higher IRE spend in the early part of this regulatory period will impact our financial results in the first two or three years, but this reverses out in later years.

And whilst we have spent £799 million this year, this investment has been delivered effectively. Our, new tougher, Time: Cost: Quality index (TCQi) for the year remains high at 90 per cent.

Before I ask Steve to talk through our ODIs in a bit more detail, I would like to provide a high level overview of our position.



You may recall that in preparing our PR14 business plan, feedback from our customers was that they were generally satisfied with current levels of performance and unwilling to pay for better, and our ODIs are therefore weighted towards penalty. In the final stages of PR14, Ofwat imposed unfunded upper quartile targets on a number of ODIs and this made our position even more challenging. In light of this, we are very encouraged to have significantly de-risked the likely outcome as shown on the chart.

In Russ's presentation last year he explained that the 80 per cent probability range for our five year cumulative ODI performance was a £140 million net reward to a £470 million net penalty. However, these are extremes and we subsequently gave soft guidance of a more likely cumulative outcome of between a £50 million net reward and a £100 million net penalty over the five years.

As mentioned previously, the plans we have developed over the last year give significant focus to ODI performance and I have already mentioned that we have accelerated our investment profile to deliver early benefit. Steve will touch on one or two examples in a few moments. This focus is reflected in our ODI performance last year where we earned a net reward, exceeding our expectations at the beginning of the year.

Our plans and progress over the last twelve months support an improvement in our soft target range for the five-year period to between a net reward of £30 million and a net penalty of £70 million. We are sticking with a range, rather than a specific number, to reflect the fact that a number of our ODIs are volatile, often weather dependent and sensitive to single performance samples.

Now, over to Steve.

Managing Director

Steve Fraser

Thank you, Steve, and good morning everyone.

I will provide you with an overview of our ODI performance for 2015/16 and then talk through some individual ODIs to provide a bit more colour.

Outcome delivery incentives (ODIs)

Good performance in 2015/16

Water ODIs	£m reward/ (penalty)
Reliable water service index	(8.0)
Water quality service index	0.2
Average minutes lost	-
Leakage	-
Other 5 water ODIs	(0.4)
Water net (Penalty)	**(8.2)**

Wastewater ODIs	£m reward/ (penalty)
Private sewers service index	7.4
Wastewater category 3 pollution incidents	3.3
Sewer flooding index	-
Maintaining our WWTWs	-
Other 6 wastewater ODIs	-
Wastewater net reward	**10.7**

Total net reward	**2.5**

This table summarises our ODI position for 2015/16 and we have outperformed our initial expectations.

Overall, this was a good performance and we are very encouraged to have achieved a net reward of £2.5 million. We benefitted from the planned acceleration of our investment programme and early implementation of what we call 'systems thinking', something Steve will talk about later.

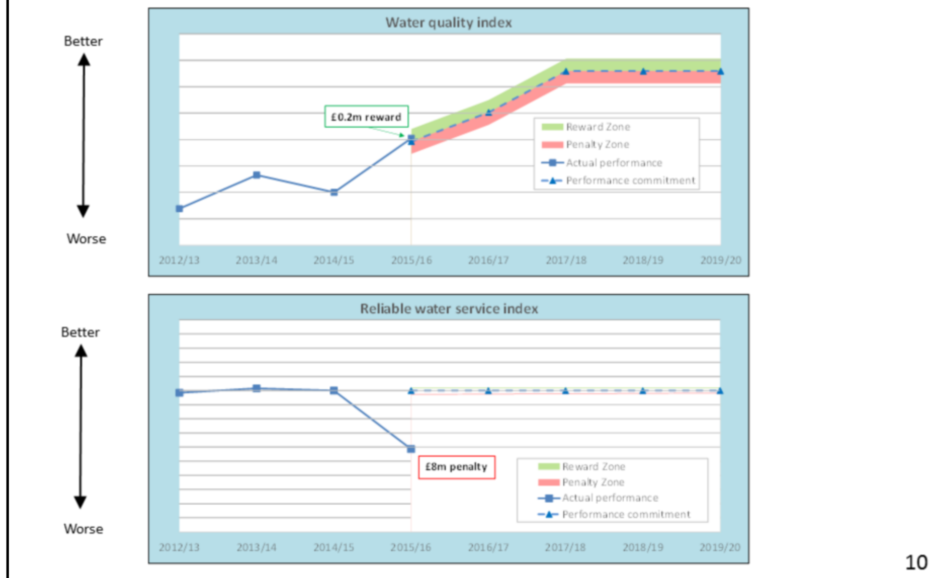
This slide shows that our main areas of reward came through good performance on private sewers and pollution, with our main penalty being on reliable water service.

Although the ODI targets generally get tougher, we are determined to maximise the opportunity. However, we will be mindful of the various trade-offs when prioritising operational investment as we look to balance performance for all of our stakeholders.

So, looking at our ODIs in a bit more detail.

Outcome delivery incentives (ODIs)

Water ODIs – main contributors to 2015/16 outcome

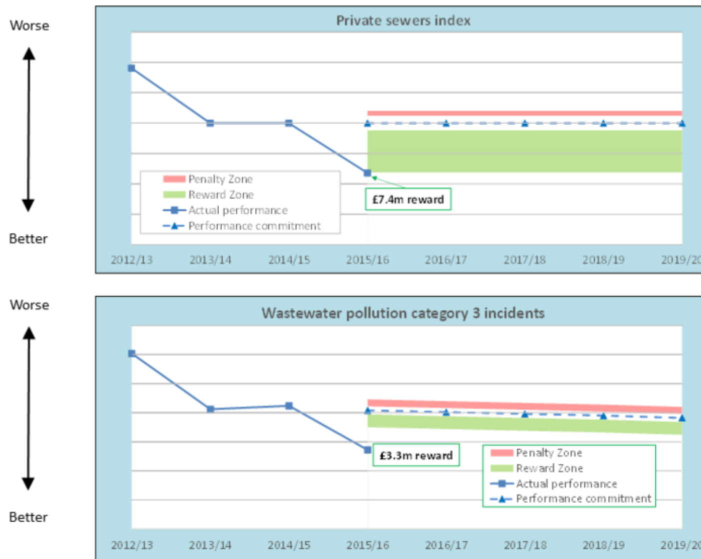


These charts show our water quality and reliable water service ODIs. These were the two main movers in our 2015/16 performance.

In recent years, we have consistently delivered high quality water and on this ODI we earned a small reward. You can see from the top chart that our regulatory targets become progressively tougher over the next couple of years, and we have plans in place to deliver further improvements.

With regard to reliable water service, we have delivered a consistent and good performance during the last three years of AMP5. However, we took a penalty of £8 million in 2015/16, reflecting water no-supply incidents, particularly those where supply was off for over 12 hours. You can see on the bottom chart that the penalty and reward band for this ODI is very narrow. And, as we are typically one of the best performers on minutes lost per customer, this was unusual for us.

I'm pleased to say that we are back on track, having delivered performance to our usual high standard during the first four months of this calendar year.

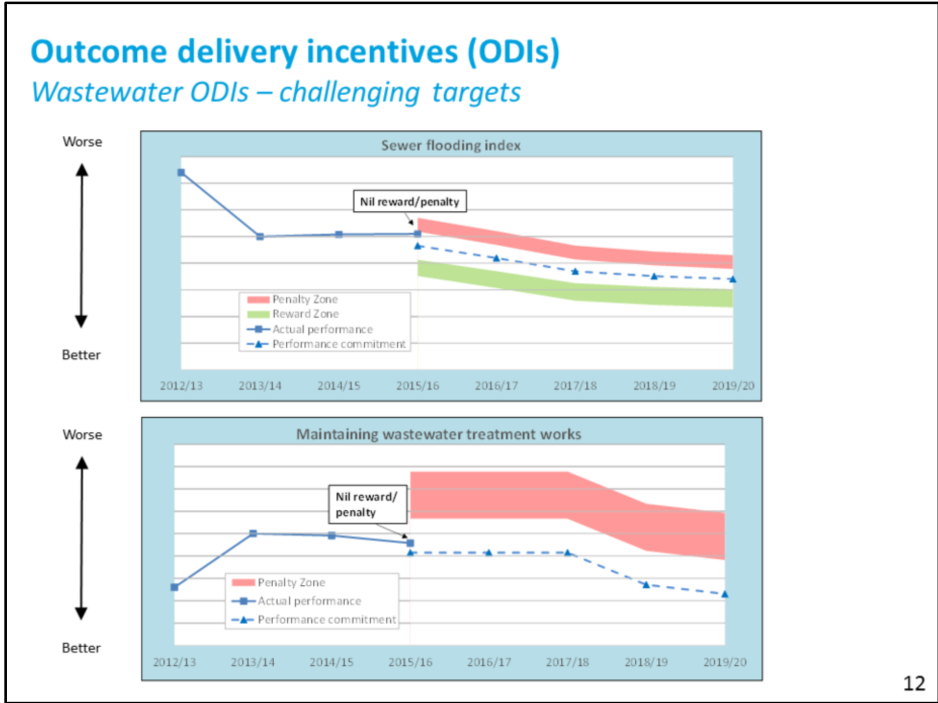


Now, looking at our private sewers and wastewater pollution ODIs, which were the main contributors to our net reward this year.

We attained the largest reward on our private sewers ODI. Our planned acceleration of investment has helped deliver customer benefits early and helped us to achieve a £7.4 million reward. As you can see from the top chart, we are in a good position. Although our investment profile will result in less capex being spent in the later years, we are focussing on achieving greater rewards in the early years whilst continuing to provide a high level of service for customers.

The bottom chart shows our wastewater pollution ODI. You can see that we are comfortably within positive territory and we achieved a £3.3 million reward. This ODI is weather dependent and we benefitted from favourable weather conditions last summer, although we have been a good performer in the area of wastewater pollution over recent years.

So, a very good performance in our wastewater business.



I'd now like to look at two of our more volatile ODIs; sewer flooding and maintaining our wastewater treatment works.

Although we were in the deadband zone on each of these for 2015/16, you can see how the targets get much tougher in future years and I will provide a few examples of some of the things we are doing to improve our performance. I will also explain how sensitive the wastewater treatment works ODI can be.

Our sewer flooding ODI was impacted by Ofwat's late decision to impose upper quartile targets. You will see from the top chart that we will have to achieve a step change in performance over the next few years to avoid a penalty. However, we are undertaking an extensive sewer cleaning programme, along with a comprehensive drainage area programme to help improve performance. We will review and make management and operational decisions on a regular basis, with the aim of reaching the optimal position overall. This ODI is also affected by rainfall and in the North West it can be very wet!

On the second chart, we look in a good position based on the last few years' performance. However, this ODI is penalty only and can be volatile based on single events at large individual works. To help mitigate this, early and targeted investment at our major treatment works, such as Davyhulme and Oldham and Royton, should help improve performance as we move through the regulatory period. At these large works, we are investing around £200 million in the early years of this AMP to re-design the specifications of the works and deliver enhanced scale and capability. This gives us a high level of confidence that in future years we will be able to meet the much more stringent permit standards that will be applied to these works.

So, overall, our ODIs tend to get tougher each year. However, we have done well this year and have managed to significantly mitigate the downside risk. And, as you can see, we are implementing a range of initiatives to improve performance levels further.

Thank you. Now, back to Steve.

Chief Executive

Steve Mogford

Thanks, Steve.

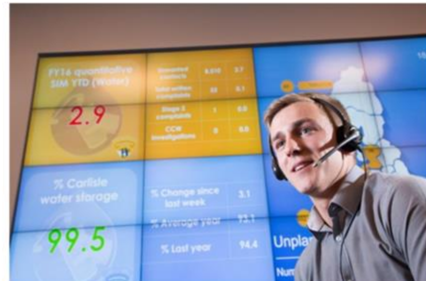
We have made good progress over the last five years in delivering improved operational performance and establishing ourselves as a leading performer in the sector. Whilst doing so we have also spent time understanding best practise in the water and other sectors with the objective of developing a future operating vision for the business.

‘Systems thinking’ operational approach

Supports drive for further improvement

- Improved operational capabilities
- Detect and fix problems before they impact the customers
- Water production planning system
  - aims for lowest cost production
  - real-time capability to respond to issues and re-schedule work
- Wastewater production planning system
  - optimise sludge treatment cost
  - optimise bio-gas production

Our Integrated Control Centre acts as the hub for our ‘data highway’ between our many sites



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In our presentation last year I outlined our new Wholesale operating model, based on what we call ‘systems thinking’. We have been progressively building our new, radically different way of working through investment in a comprehensive set of new operational capabilities. We began investing in our new operating model in the last regulatory period and so we are already benefitting from a number of new capabilities. We are also very active in finding, and exploiting innovation.

Our ambition is to detect and fix problems before they affect customer service and our new integrated control centre, opened last April, acts as the hub in which we plan, monitor and control our operations across the North West. This new capability proved critical to the effectiveness of our response to the major incidents we experienced last year and as a consequence we were able to minimise service interruption to customers.

We have around 90 water treatment works and these have historically operated largely autonomously within the context of a monthly production plan. We have implemented a real time production planning system that controls production output across our treatment works with lowest cost of production as its principal objective. The real time capability of the system has proved invaluable in re-planning production to take account of both planned and unplanned network and process issues, such as plant shutdowns or network bursts. The system proved particularly valuable during the flooding last year.

We have around 570 wastewater treatment works in our region and sludge treatment and disposal is now optimised by a production planning system that trades off transport costs, sludge quality and digester performance. This optimises sludge treatment costs and biogas production. This tool has transformed our sludge strategy. We are rationalising our digester portfolio and all this is helping us to be competition ready when the sludge value chain opens to competition post 2020.

These are just a few examples of the transformation we are undergoing and which is contributing around £100 million of totex savings within our plans for this regulatory period.

Strong operational and environmental performance

UU joint 1st position on latest metrics

	Customer experience			Environmental Impact					Serviceability, reliability and availability					
	SIM score	Internal sewer flooding incidents	Water supply interruptions (hours per total properties served)	Greenhouse gas (GHG) emissions	Pollution incidents sewerage	Serious pollution incidents sewerage	Discharge permit compliance	Satisfactory sludge disposal	Serviceability water non-infrastructure	Serviceability water infrastructure	Serviceability for sewerage non-infrastructure	Serviceability sewerage infrastructure	Leakage	Security of supply index (SoSI)
Water and sewerage companies														
ANG	G	G	G	G	A	A	A	G	G	G	G	G	G	G
WW	G	G	G	R	A	A	G	G	G	G	G	G	G	G
NWG	G	G	G	G	A	A	G	G	G	G	G	G	G	G
SVT	G	G	G	G	A	A	G	G	R	G	G	A	G	G
SWW	G	G	G	G	R	A	A	G	G	G	G	G	G	G
STN	G	G	G	G	R	R	G	G	G	G	G	G	G	G
TMS	G	A	G	R	A	A	G	G	G	G	G	R	G	G
UU	G	G	G	G	G	G	A	G	G	G	G	G	G	G
WSX	G	G	G	G	G	A	G	G	G	G	G	G	G	G
YKS	G	A	G	G	A	G	G	G	G	G	G	G	G	G

Source: Ofwat's "Companies' performance 2014-15"

This chart is Ofwat's latest comparison of water and wastewater company performance and shows us to be a top performer.

In 2014/15 we achieved upper quartile performance under the Environment Agency's metrics and we have improved on that again. We achieved leading company status last year and we were particularly pleased to deliver a reduction of around a third in environmental pollution incidents (category 3).

Our water quality performance has generally been around the sector average and, although we took an obvious setback with the incident last summer, our performance for the first four months of this year shows a significant improvement. This will continue to be an area of management focus and investment, as we embed sustainable improvement.

Now, onto business retail.

Business retail JV – Water Plus

Well positioned for full market opening

- 50:50 JV announced on 1 March 2016
- First mover advantage
- Synergies: lower cost and better service
- 2014/15 pro-forma JV financials
  - Sales: c£940m, Gross assets: c£200m, PBT: c£10m
- c400,000 customers: c25% of market
- CMA has now approved the JV

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We announced in March that we intended to form a joint venture with Severn Trent in which we would combine both business retail operations ahead of the English market opening to competition in April 2017. This represents the latest phase of our strategy for the competitive business retail market in England and Scotland, providing us with first mover advantage and economy of scale benefits. The slide gives you a few facts and figures about the joint venture.

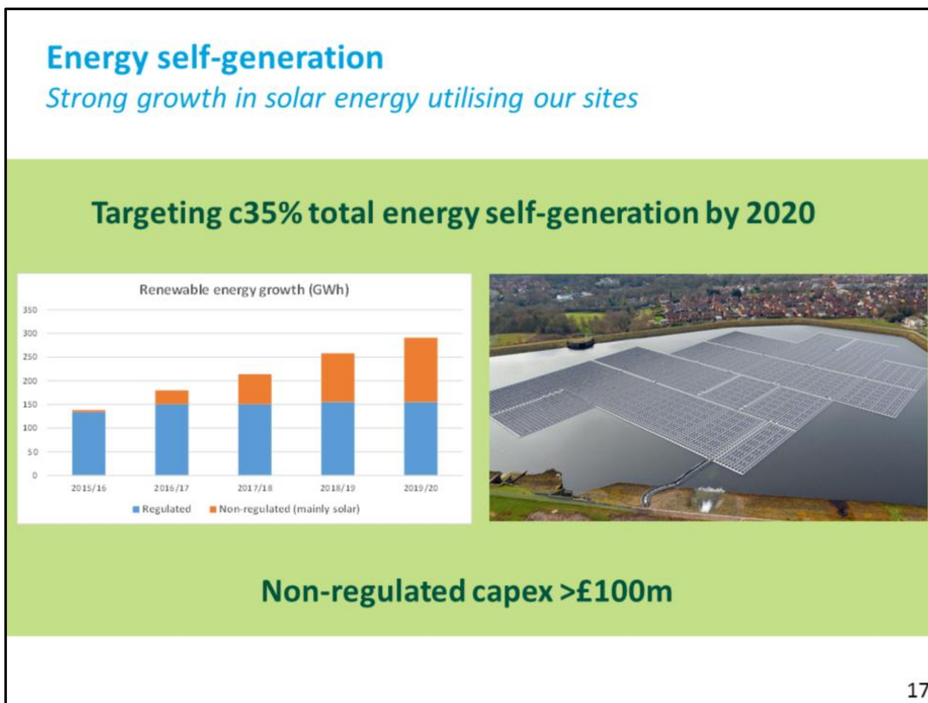
Timing is ideal.

Both companies are active in the Scottish market. We are one of the leading players having won around 3,500 sites and a net annualised revenue of around £18 million. Severn Trent started later but has also been successful in winning customers.

We had implemented a new customer relationship system for business retail at the end of 2014 and this will be the core system for the new joint venture. Severn Trent will migrate its business customers on to this platform later this year. The new joint venture will be up and running before the market opens.

Our intent is for this new company, 'Water Plus', to be a fresh, competitive operation providing customers with a very attractive choice of retail supplier. The combined business will start operations with around 400,000 business customers. It will encompass our Scottish businesses and short cycle value added services, such as water efficiency advice.

The Competition and Markets Authority has given its approval for the joint venture and so we are now targeting to complete the transaction at the beginning of June. The business will be headquartered in Stoke-on-Trent and preparations are well advanced for the start of operations this summer.



With energy as one of our biggest costs at approximately £65 million per annum, renewables represents an important area for us.

We have mentioned previously that we are targeting to produce around 35 per cent of our energy requirement from renewables by 2020, up from 17 per cent today. This chart shows the planned growth in renewables generated by our regulated and non-regulated activities.

In our regulated business, we have created a separate group within our Wholesale business with responsibility for sludge digestion and disposal and associated energy generation. In March, this team delivered our first biomethane to grid project at our biggest wastewater treatment plant in Manchester. This business area is tasked with ensuring we optimise the value we obtain from sludge and that we are ready when the sludge value chain becomes subject to competition under Ofwat's Water 2020 plans.

Our non-regulated activity is dominated by solar and, subject to acceptable returns, we plan to invest around £100 million on solar installations between 2015 and 2020. We have installed 29 mega watts of solar to date, including the first floating array in the UK at our Godley reservoir on the outskirts of Manchester. With regard to wind, long lead times and planning considerations make this a less attractive area for widespread exploitation.

Now over to Russ.

Chief Financial Officer

Russ Houlden

Thank you, Steve.

Agenda

- Operational performance
- Financial performance
- Water 2020
- Summary and outlook
- Q&A

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So, moving onto our financial performance.

Financial performance

Good set of results

- Underlying operating profit of £604m, impacted by new regulated price controls
- Underlying profit after taxation of £325m, benefiting from lower finance costs
- Underlying EPS of 47.7p pence, down 4.2p or 8%
- Final dividend of 25.64 pence per share (total for year 38.45 pence), up 2.0%
- Robust capital structure, with RCV gearing at 61%

This is a good set of results, in light of the new tough regulated price controls.

Underlying operating profit at £604 million was £60 million lower than last year impacted by these new price controls, along with an increase in IRE and operating expenses that I will discuss shortly.

Underlying profit after tax of £325 million was £29 million lower than last year, with the reduction in underlying operating profit partly offset by a decrease in underlying net finance expense and lower tax. Underlying EPS was down by 4.2p, or 8 per cent.

We have proposed a final dividend of 25.64p per share, up 2.0 per cent, reflecting the increase in RPI for the year to November 2014, which is the rate included within our price controls for 2015/16. This takes the total dividend for the year to 38.45p.

We have maintained our responsible financing policies, with RCV gearing at 61 per cent which is comfortably within our target range of 55 to 65 per cent. This supports our robust capital structure and we have solid credit ratings of A3 stable with Moody's and BBB+ positive outlook with Standard and Poor's.

And our dividend policy for AMP6, targeting growth of at least RPI each year, will keep dividends growing at a sustainable rate.

Profit after tax reconciliation

Profit benefits from one-off tax credit

£m Year ended 31 March	2016	2015
Reported profit after tax	**397.5**	**271.2**
Adjustments:		
Water quality incident	24.8	-
Flooding incident (net of insurance proceeds recognised)	(0.6)	-
Business retail market reform[1]	11.1	-
Restructuring costs	0.9	11.0
Net fair value losses on debt and derivative instruments	26.3	104.7
Interest on swaps and debt under fair value option	16.5	4.0
Net pension interest (income)/expense	(3.1)	7.0
Capitalised borrowing costs	(21.3)	(20.9)
Deferred tax credit - change in tax rate	(112.5)	-
Agreement of prior years' UK tax matters	(3.4)	(0.7)
Tax in respect of adjustments to underlying profit before tax	(10.9)	(22.2)
Underlying profit after tax	**325.3**	**354.1**
Basic earnings per share (pence)	**58.3**	**39.8**
Underlying earnings per share (pence)	**47.7**	**51.9**

[1] Relates to market reform restructuring costs incurred preparing the business for open competition in the business retail market

As usual, we have made some adjustments to reported profit to get to underlying profit, which we believe gives a more representative view of underlying performance.

We had a £26 million fair value loss in the year, largely due to losses on the swap portfolio which fixes rates for the regulatory periods. This compares with a fair value loss last year of £105 million, resulting from a decrease in medium-term sterling interest rates, meaning that there was a £79 million net movement across the two periods.

Underlying operating profit also strips out £25 million of costs associated with the water quality incident and £11 million in relation to preparations for business retail market reform, along with £1 million of restructuring costs. The net position relating to the flooding incidents was negligible, after offsetting the insurance proceeds recognised.

We have also stripped out the £112 million deferred tax credit, resulting from the UK Government's future changes to reduce the rate of corporation tax to 18 per cent.

So, whilst the reported profit after tax for the year was £126 million higher, the more meaningful underlying measure was down £29 million, at £325 million.

Income statement – underlying

Impacted by new regulated price controls

£m Year ended 31 March	2016	2015	Movement
Revenue	1,730.0	1,720.2	*+0.6%*
Operating expenses	(594.0)	(555.1)	*+7.0%*
Infrastructure renewals expenditure	(168.2)	(148.2)	*+13.5%*
EBITDA	**967.8**	**1,016.9**	***(4.8)%***
Depreciation and amortisation	(363.7)	(352.6)	*+3.1%*
Operating profit	**604.1**	**664.3**	***(9.1)%***
Net finance expense	(201.0)	(222.0)	*(9.5)%*
Share of profits of joint ventures	5.0	5.1	*(2.0)%*
Profit before tax	**408.1**	**447.4**	***(8.8)%***
Tax	(82.8)	(93.3)	*(11.3)%*
Profit after tax	**325.3**	**354.1**	***(8.1)%***
Earnings per share (pence)	**47.7**	**51.9**	***(8.1)%***
Total dividend per ordinary share (pence)	**38.45**	**37.70**	***+2.0%***

This is a summary of the underlying income statement after making the adjustments shown on the previous slide.

Revenue was up £10 million at £1.73 billion, despite the regulatory reset, as we benefitted from higher than expected volumes, increased non-regulated sales and because last year was impacted by the special discount we applied to customer bills.

Underlying operating profit at £604 million was £60 million lower than last year. This reflects the regulatory price reset and increased costs, which I'll discuss in more detail on the next two slides.

Underlying profit after tax was £325 million, down £29 million. This was due to the £60 million decrease in underlying operating profit, partly offset by the £21 million decrease in underlying net finance expense and a £10 million reduction in the underlying tax charge. The decrease in underlying finance expense was mainly due to a lower cost of debt locked-in on the group's nominal debt and the impact of lower RPI inflation on the portion of the group's index-linked debt with an eight month lag. The decrease in the tax charge was the result of lower underlying profit before tax and a lower rate of UK corporation tax.

Underlying operating costs

Movements

£m Year ended 31 March	2016	2015	Movement
Revenue	**1730.0**	**1720.2**	
Employee costs	(143.7)	(134.1)	(9.6)
Hired and contracted services	(96.8)	(93.4)	(3.4)
Property rates	(86.3)	(80.5)	(5.8)
Materials	(62.7)	(58.5)	(4.2)
Power	(65.0)	(69.1)	4.1
Bad debts	(39.2)	(52.9)	13.7
Regulatory fees	(24.9)	(29.2)	4.3
Third party wholesale charges	(15.1)	(10.8)	(4.3)
Cost of properties disposed	(10.5)	(0.6)	(9.9)
Other expenses	(49.8)	(26.0)	(23.8)
	(594.0)	**(555.1)**	**(38.9)**
Infrastructure renewals expenditure (IRE)	(168.2)	(148.2)	(20.0)
Depreciation and amortisation	(363.7)	(352.6)	(11.1)
Total underlying operating expenses	**(1,125.9)**	**(1,055.9)**	**(70.0)**
Underlying operating profit	**604.1**	**664.3**	
Adjustments:			
Water quality incident	(24.8)	-	
Flooding incidents (net of insurance proceeds)	0.6	-	
Business retail market reform[1]	(11.1)	-	
Restructuring costs	(0.9)	(11.0)	
Reported operating profit	**567.9**	**653.3**	

[1] Relates to market reform restructuring costs incurred preparing the business for open competition in the business retail market

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We have continued to maintain tight cost control, although, as is often the case, there were some special factors affecting the comparison of underlying operating expenses between the two periods.

Overall, our underlying operating expenses were up £70 million.

The main increases were IRE (£20 million, due to the planned acceleration of the investment programme), depreciation (£11 million, mainly because of the larger asset base) and employment costs (£10 million, partly due to a proportionate reduction in capitalised costs, partly due to current pension service costs and partly due to wage rises). We also sold a large property, which led to extra revenue and costs of around £10 million.

Other expenses were up £24 million, reflecting a large legal credit last year, legal and other provisions this year and an increase in the cost of sales on higher revenue within our total solutions business.

These cost increases were partly offset by reductions in bad debt costs (£14 million), power costs (£4 million) and regulatory fees (£4 million).

Bad debt and cash collection

Bad debt reduction in challenging environment

- North West is the most deprived region in England
- Bad debt reduced to 2.3% of regulated revenue, from 3.1% in 2014/15
  - reflects ongoing focus on managing bad debt; and
  - reduction in charge following review of debt processes and provisions last year
- Bad debt will continue to be challenging in difficult North West environment

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So, looking at bad debt in a bit more detail.

Deprivation remains the principal driver of our higher than average bad debt and the North West has a high proportion of customers impacted by welfare reform and claiming universal credits.

You may recall that bad debt costs increased last year to just over 3 per cent of regulated revenue. This was largely due to a review of bad debt provisions and operational debt processes last year.

Our bad debt performance for 2015/16, at 2.3 per cent, is slightly better than the 2.5 per cent guidance I gave you a year ago. We have maintained our strong focus on improving our bad debt and cash collection performance, including working with Equifax to share customers' credit data to encourage those who can pay to do so. We also have a wide range of schemes to help those who are genuinely struggling to pay.

So, we've had a good year but bad debts will remain challenging as high deprivation levels mean that we, in the North West, will continue to operate in a difficult environment.

Financial position

Robust capital structure

£m At 31 March	2016	2015
Property, plant and equipment	10,031.4	9,716.3
Retirement benefit surplus	275.2	79.2
Other non-current assets	208.7	187.7
Cash	213.6	244.0
Other current assets	412.3	393.8
Total derivative assets	765.6	682.6
Total assets	**11,906.8**	**11,303.6**
Gross borrowings	(6,978.0)	(6,645.4)
Other non-current liabilities	(1,592.5)	(1,603.8)
Other current liabilities	(369.1)	(414.8)
Total derivative liabilities	(261.7)	(205.2)
Total liabilities	**(9,201.3)**	**(8,869.2)**
TOTAL NET ASSETS	**2,705.5**	**2,434.4**
Share capital	499.8	499.8
Share premium	2.9	2.9
Retained earnings	1,878.8	1,610.7
Other reserves	324.0	321.0
SHAREHOLDERS' EQUITY	**2,705.5**	**2,434.4**
NET DEBT[1]	**(6,260.5)**	**(5,924.0)**

[1] Net debt includes cash, borrowings and derivatives (slide 42)

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Turning now to the statement of financial position.

Property, plant and equipment was up £315 million in the year to just over £10 billion, reflecting expenditure on our large capital programme.

As at March 2016, the group had an IAS 19 retirement benefit surplus of £275 million, an increase in surplus of £196 million compared with a year ago. This favourable movement mainly reflects the accounting remeasurement effect under IFRS of an increase in corporate credit spreads, reducing the IAS19 pension liability, partially offset by an increase in inflation assumptions. We believe that our pension position, and the relative differences to other companies, should be considered in analysts' equity valuations.

Cash and short term deposits were down £30 million, compared with a year ago.

Derivative assets increased by £83 million, to £766 million and derivative liabilities were up £57 million, at £262 million, both movements reflecting a decrease in market interest rates during the year.

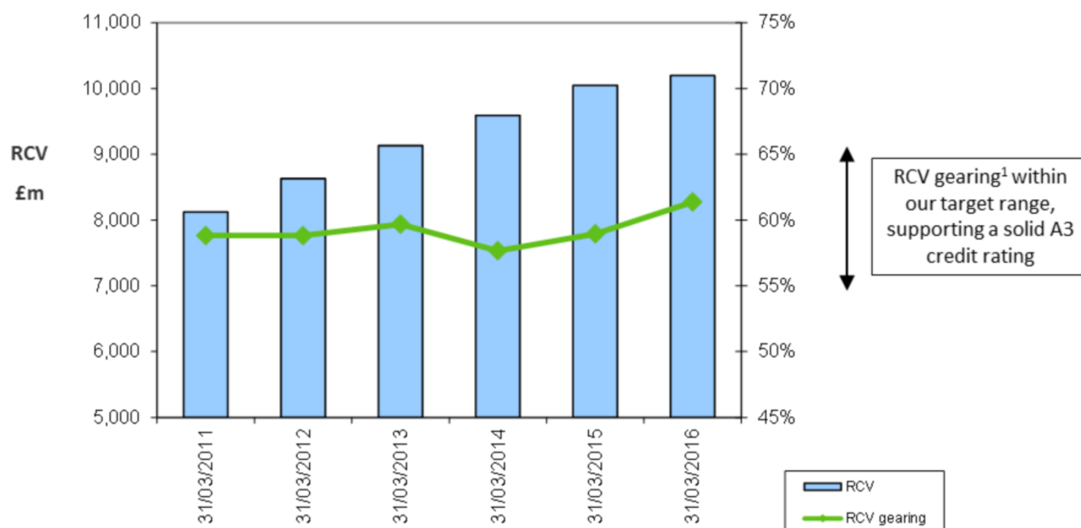
Gross borrowings increased by £333 million, to almost £7 billion, because debt raised exceeded maturities.

Retained earnings have increased by £268 million, impacted by post-tax remeasurement gains on our defined benefit pension schemes of £134 million.

Net debt was £337 million higher than the position at March 2015, mainly reflecting expenditure on our substantial capital investment programme.

RCV and gearing

RCV gearing supports robust capital structure



[1] RCV gearing calculated as group net debt / United Utilities Water's regulatory capital value (based on Ofwat's final determination, published in December 2014) and presented in outturn prices

This chart shows our RCV and gearing level.

The blue bars show the growth in our RCV, which has slowed a little over the last year mainly due to lower RPI inflation.

The green line shows the movement in RCV gearing over the last few years. Over the previous four years, our gearing had remained relatively stable, at or slightly below 60 per cent, with the growth in net debt largely offset by the growth in the RCV. This year, as expected, gearing has nudged up slightly to 61 per cent, reflecting the acceleration of our investment programme, as mentioned by Steve, and lower inflationary growth in the RCV.

Our responsible approach to financing means that gearing, at 61 per cent, is comfortably within our target gearing range of 55 to 65 per cent and supports a solid A3 credit rating.

Cash flow statement

Cash from operations covers investing activities

£m Year ended 31 March	2016	2015
Net cash generated from operating activities	685.6	706.5
Net cash used in investing activities	(676.8)	(704.9)
Net cash generated (used in)/from financing activities	(46.4)	139.2
Net movement in cash	**(37.6)**	**140.8**

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Moving on to cash flow.

Net cash generated from operating activities at £686 million was slightly lower than last year, mainly as a result of lower profit, reflecting the regulatory price reset and the impact of the additional costs associated with the operational incidents in the year.

Cash used in investing activities was down slightly, mainly reflecting lower capital investment compared with last year, as expected, as we start the new five-year regulatory period. We have achieved a smooth transition into AMP6 and our full year investment of £799 million is much higher than the £608 million we invested in the first year of AMP5.

Net cash used in financing activities was £46 million, compared with £139 million generated last year, as we repaid more borrowings this year.

Now, onto financing.

Financing

Over half of 2015-20 funding already raised

- £1.4bn of c£2.5bn 2015-20 financing requirements now raised

  Index-linked
  - £100m loan with a 10-year maturity, raised in March 2016
  - £250m EIB[1] loan with 10-year average life, still to be drawn down
  - Total of £410m raised previously

  Nominal
  - Total of £660m raised previously

- Additional £150m committed bank facilities agreed since September 2015

- Financing headroom into 2018

[1] European Investment Bank

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Over the 2015-20 regulatory period, we have financing requirements totalling around £2.5 billion. This is to meet a combination of refinancing and incremental debt, to help fund our investment programme.

We have made a very good start, having already raised around £1.4 billion.

In addition to the £1.1 billion raised prior to our half year results, we have now raised a further £100 million with an existing relationship bank, plus we have signed £250 million out of a £500 million AMP6 funding package agreed with the EIB.

Furthermore, since September, we have agreed another £150 million of committed bank facilities, bringing the total under our rolling bilateral revolving credit facilities programme to £700 million.

As a result, we now have financing headroom into 2018.

Hedging

Well placed in period of low inflation

- Debt portion of RCV remains hedged for inflation
  - index-linked debt portfolio now c£3.4bn with an average cost of 1.5% real
  - pension liabilities hedge the remaining debt portion of RCV
- Well placed in this period of low inflation
- Nominal debt portfolio fixed for 2015-20 at average rate of c3.7%[1]
- Continuing 10-year reducing balance policy post 2020
- Hedging response to Ofwat's proposed CPI transition to be considered

[1] Interest rate is inclusive of credit spreads

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And finally, a brief update on our approach to hedging.

As a reminder, we leave the equity portion of the RCV exposed to RPI inflation by hedging the debt portion of the RCV for inflation through index-linked debt and the effect of our pension scheme liabilities.

We are currently hedged in line with our policy and, as I mentioned, we have been raising an appropriate mix of index-linked and nominal debt to maintain this position.

The average cost of our £3.4 billion, long-term, index-linked debt portfolio has now reduced to 1.5 per cent real, reflecting the more recent index-linked debt we have raised which is at much more attractive rates.

Our hedging strategy keeps us more hedged for inflation than our listed competitors, but similar to our unlisted competitors. Owing to the current low level of inflation, this gives us a financial benefit relative to our listed competitors.

We are therefore well placed in this period of low inflation and this has been reflected in a £21 million reduction in underlying finance expense in the year.

In respect of our nominal debt, this is virtually all fixed for the 2015-20 period. This has been done at an average interest rate of around 3.7 per cent.

The low cost of debt we have locked-in places us in a strong positon to deliver financing outperformance up to 2020.

To help manage our exposure to the various ways in which Ofwat may choose to set the cost of debt at the next price review, we are continuing with our 10-year reducing balance policy for the post 2020 period.

Whilst we recognise that Ofwat wishes to transition from RPI to CPI inflation, we will need to know the final form of that transition before we can judge the appropriate hedging response. In the absence of a CPI-linked gilt market, we and others will find it difficult to hedge as effectively as we do now.

Summary

Key financial takeaways

- Good set of results in light of new price controls
- Lower underlying finance expense
- Robust capital structure
- Over half of 2015-20 funding requirements already raised
- Debt portfolio locked in at attractive interest rates
- Hedging policy – well placed to manage future financing costs

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So, in summary:

- this is a good set of results in light of the tough new price controls;
- we have benefitted from a reduction in underlying finance expense;
- we continue to maintain a strong balance sheet and solid credit ratings;
- we have already raised £1.4 billion of our £2.5 billion financing requirements for the five-year regulatory period;
- we have locked in a low cost of debt for 2015-20, with an appropriate mix of index-linked and nominal debt; and
- our hedging policy means we are well placed to manage future financing costs.

Now, back to Steve.

Chief Executive

Steve Mogford

Thank you, Russ.

And now, Water 2020.

Agenda

- Operational performance
- Financial performance
- Water 2020
- Summary and outlook
- Q&A

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You will probably be aware that yesterday Ofwat published its proposals following responses to its Water 2020 consultation of last December. We have been an active participant in the debate, contributing a number of papers into the 'market place for ideas' established by Ofwat and Water UK for that purpose.

Our approach is constructive, whilst also protecting customers and shareholders from any unintended consequences of such developments.

There is much yet to be done before the PR19 methodologies emerge but you will have seen there are a number of key themes to Water 2020. Ofwat intends to enable competition for new water resources, sludge processing and new enhancement projects with a total life cost of £100 million. Recent debate has centred on four key enablers to future change:

- the first is access pricing and we have been supportive of the methodology proposed by Ofwat, which is based upon the long run incremental cost, or LRIC, principle;
- next is RCV protection and we believe Ofwat's proposals will provide protection for RCV incurred up to 2020. We would support this becoming an established principle of rolling protection at each price review;
- sector cost allocation rules become important when using company cost data for efficiency comparison and multiple price caps. Non-household margins at PR14 highlighted this issue and genuine cost reflective allocation is essential if such proposed changes are to work; and
- finally, the move from RPI to CPI indexation of pricing and RCV. Ofwat has emphasised its commitment to NPV neutrality following such a change. We, like others, will pay close attention to the mechanism by which Ofwat proposes to achieve such neutrality.

We are still working through Ofwat's documents released yesterday and so we are not yet in a position to comment in detail on the proposals.

Agenda

- Operational performance
- Financial performance
- Water 2020
- **Summary and outlook**
- Q&A

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Before Russ, Steve and I take questions I would like to summarise the key points from our presentation this morning.

Summary and outlook

Strong overall performance

- Further improvements in customer satisfaction and operational performance
- Implementing plans to eliminate totex gap
- Accelerating 2015-20 investment programme: £799m capex invested in 2015/16
- Strong operational performance, with small reward achieved on ODIs
- Good financial performance, robust capital structure and low cost of debt locked-in
- Business Retail JV with Severn Trent approved by CMA: well positioned for full market opening
- Dividend growth of 2.0% in line with policy

This has been another good year for UU which has seen us:

- Deliver further improvements in customer satisfaction.
- Improve underlying operational performance, taking another step towards our vision of becoming the UK's best water and wastewater company, providing customers with great service.
- Build plans through which we can be confident of delivering our promises to customers within our final determination totex allowance.
- Accelerate our investment programme and exceed our expectations by delivering a first year ODI net reward, giving us confidence to improve our soft guidance for our cumulative net ODI performance over this regulatory period.
- Deliver financing outperformance.
- And, make our next strategic move in the non-household retail market, forming a new, competitive joint venture – 'Water Plus' – with Severn Trent.

All of this supports dividend growth in the year of two per cent, in line with our policy of an annual growth target of at least RPI inflation up to 2020.

Q&A

That concludes our presentation.
Thank you for listening.
We’d now like to take questions.

Supporting information

- Reported income statement
- Underlying profit before tax
- Finance expense
- Derivative analysis
- Movement in net debt
- Financing and liquidity
- Term debt maturity profile
- Debt structure

Income statement – reported

One-off tax credit enhances earnings

£m Year ended 31 March	2016	2015
Revenue[1]	1,730.0	1,720.2
Operating expenses	(798.4)	(714.3)
EBITDA	**931.6**	**1,005.9**
Depreciation and amortisation	(363.7)	(352.6)
Operating profit	**567.9**	**653.3**
Investment income and finance expense	(219.4)	(316.8)
Share of profits of joint ventures	5.0	5.1
Profit before tax	**353.5**	**341.6**
Taxation	44.0	(70.4)
Profit after tax	**397.5**	**271.2**
Basic earnings per share (pence)	**58.3**	**39.8**
Total dividend per ordinary share (pence)	**38.45**	**37.70**

[1] UU Water appointed: £1,680m, UU Water non-appointed: £12m, Non UU Water: £38m

Underlying profit before tax

Impacted by new regulated price controls

£m Year ended 31 March	2016	2015
Operating profit	567.9	653.3
Investment income and finance expense	(219.4)	(316.8)
Share of profits of joint ventures	5.0	5.1
Profit before tax	**353.5**	**341.6**
Adjustments:		
Water quality incident	24.8	-
Business retail market reform[1]	11.1	-
Flooding incident (net of insurance proceeds)	(0.6)	-
Restructuring costs	0.9	11.0
Net fair value losses on debt and derivative instruments	26.3	104.7
Interest on swaps and debt under fair value option	16.5	4.0
Net pension interest (income)/expense	(3.1)	7.0
Capitalised borrowing costs	(21.3)	(20.9)
Underlying profit before tax	**408.1**	**447.4**

[1] Relates to market reform restructuring costs incurred preparing the business for open competition in the business retail market

Finance expense

Underlying interest charge lower

£m Year ended 31 March	2016	2015
Investment income	5.0	1.0
Finance expense	(224.4)	(317.8)
	(219.4)	**(316.8)**
Less net fair value (gains)/losses on debt and derivative instruments	26.3	104.7
Adjustment for interest on swaps and debt under fair value option	16.5	4.0
Adjustment for net pension interest (income)/expense	(3.1)	7.0
Adjustment for capitalised borrowing costs	(21.3)	(20.9)
Underlying net finance expense	**(201.0)**	**(222.0)**
Average notional net debt	**5,853**	**5,580**
Average underlying interest rate	**3.4%**	**4.0%**
Effective interest rate on index-linked debt	2.8%	3.2%
Effective interest rate on other debt	4.2%	4.8%

Finance expense: index-linked debt

Cash benefit for the group

£m Year ended 31 March	2016	2015
Cash interest on index-linked debt	(51.2)	(50.0)
RPI adjustment to index-linked debt principal - 3 month lag[1]	(27.7)	(21.9)
RPI adjustment to index-linked debt principal - 8 month lag[2]	(10.2)	(24.7)
Finance expense on index-linked debt	**(89.1)**	**(96.6)**
Interest on other debt (including fair value option debt and swaps)	(111.9)	(125.4)
Underlying net finance expense	**(201.0)**	**(222.0)**

- Cash interest payment of £51m on c£3.4bn of index-linked debt
- Decrease in indexation charge due to lower RPI on 8 month lagged debt
- RPI impact on RCV exceeds RPI impact on debt principal

[1] Affected by movement in RPI between January 2015 and January 2016
[2] Affected by movement in RPI between July 2014 and July 2015

Derivative analysis

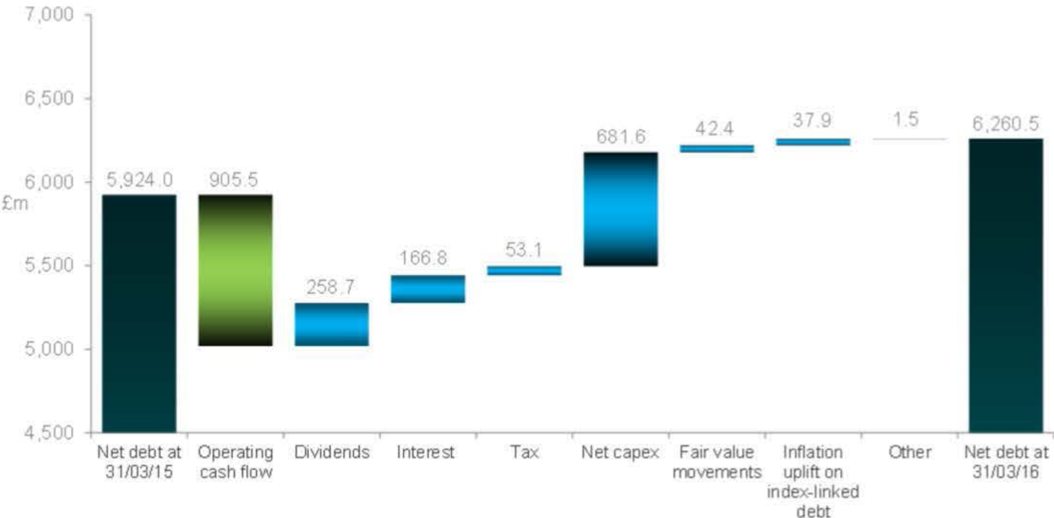
Derivatives intrinsically linked to debt

£m At 31 March	2016	2015
Derivatives hedging debt	764.5	677.6
Derivatives hedging interest rates to 2015	0.0	(6.7)
Derivatives hedging interest rates beyond 2015	(242.1)	(189.2)
Derivatives hedging commodity prices	(18.5)	(4.3)
Total derivatives assets and liabilities (slide 25)	**503.9**	**477.4**

- Derivatives hedging debt; hedge our non index-linked debt into sterling, floating interest rate debt. Typically these are designated in fair value hedge accounting relationships
- Derivatives hedging interest rates to 2015; fixed our sterling interest rate exposure out to 2015
- Derivatives hedging interest rates beyond 2015; fix our sterling interest rate exposure beyond 2015. This is in line with our strategy of fixing interest on a 10 year rolling average basis. This is supplemented by fixing substantially all remaining floating exposure across the future regulatory period around the time of the price control determination
- Derivatives hedging commodity prices; fix a proportion of our future electricity prices in line with our policy
- Derivatives are included within net debt to eliminate, to a certain extent, the fair value recognised in borrowings and thereby present a more representative net debt figure
- Further details of our group hedging strategy can be found in the Group financial statements

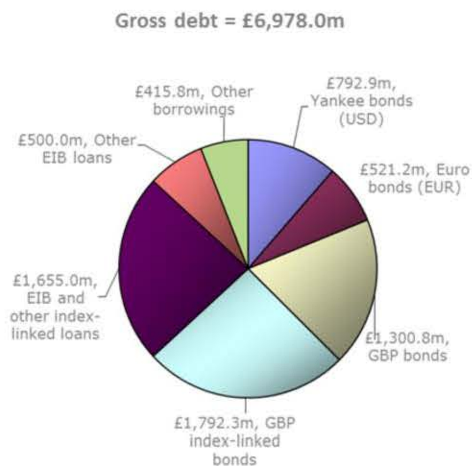
Movement in net debt*

Moderate increase in line with expectations



* Net debt includes derivatives which incorporate regulatory swaps

Financing and liquidity at 31 March 2016



Headroom / prefunding = £269.4m

	£m
Cash and short-term deposits	213.6
Medium-term committed bank facilities[1]	450.0
Undrawn EIB term loan facilities	75.0
Short-term debt	(159.0)
Term debt maturing within one year	(310.2)
Total headroom / prefunding	**269.4**

[1] Excludes £150m facilities maturing within one year

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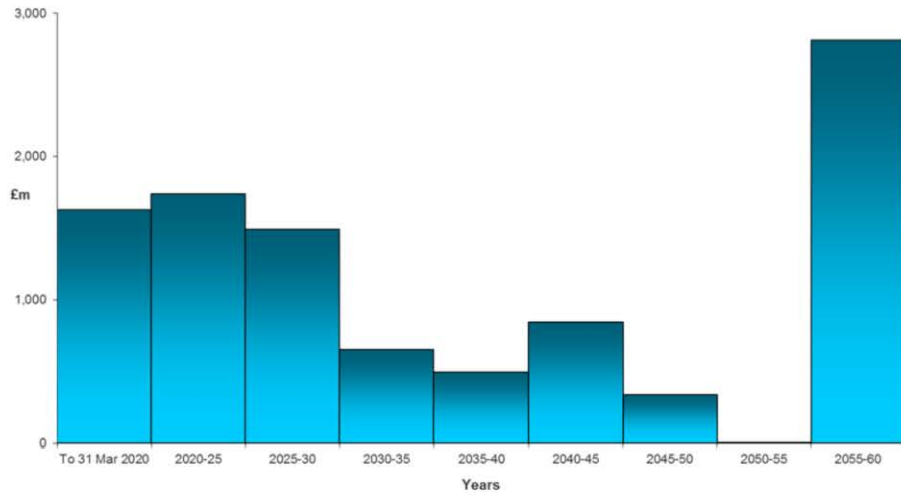
Term debt maturity profile as at 31 March 2016[1]

Average term to maturity of around 20 years



[1] Future repayments of index-linked debt include inflation based on an average annual RPI rate of 3%

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Debt structure at 31 March 2016

[1] Index-linked finance

[2] United Utilities Water Finance PLC (UUWF) is a financing subsidiary of United Utilities Water Limited (UUW) established to issue new listed debt on behalf of UUW. Notes issued by UUWF are unconditionally and irrevocably guaranteed by UUW and are rated in line with UUW's credit ratings.

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Cautionary statement

This presentation contains certain forward-looking statements with respect to the operations, performance and financial condition of the group. By their nature, these statements involve uncertainty since future events and circumstances can cause results and developments to differ materially from those anticipated. The forward-looking statements reflect knowledge and information available at the date of preparation of this presentation and the company undertakes no obligation to update these forward-looking statements. Nothing in this presentation should be construed as a profit forecast.

Certain regulatory performance data contained in this presentation is subject to regulatory audit.

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