



Good to know

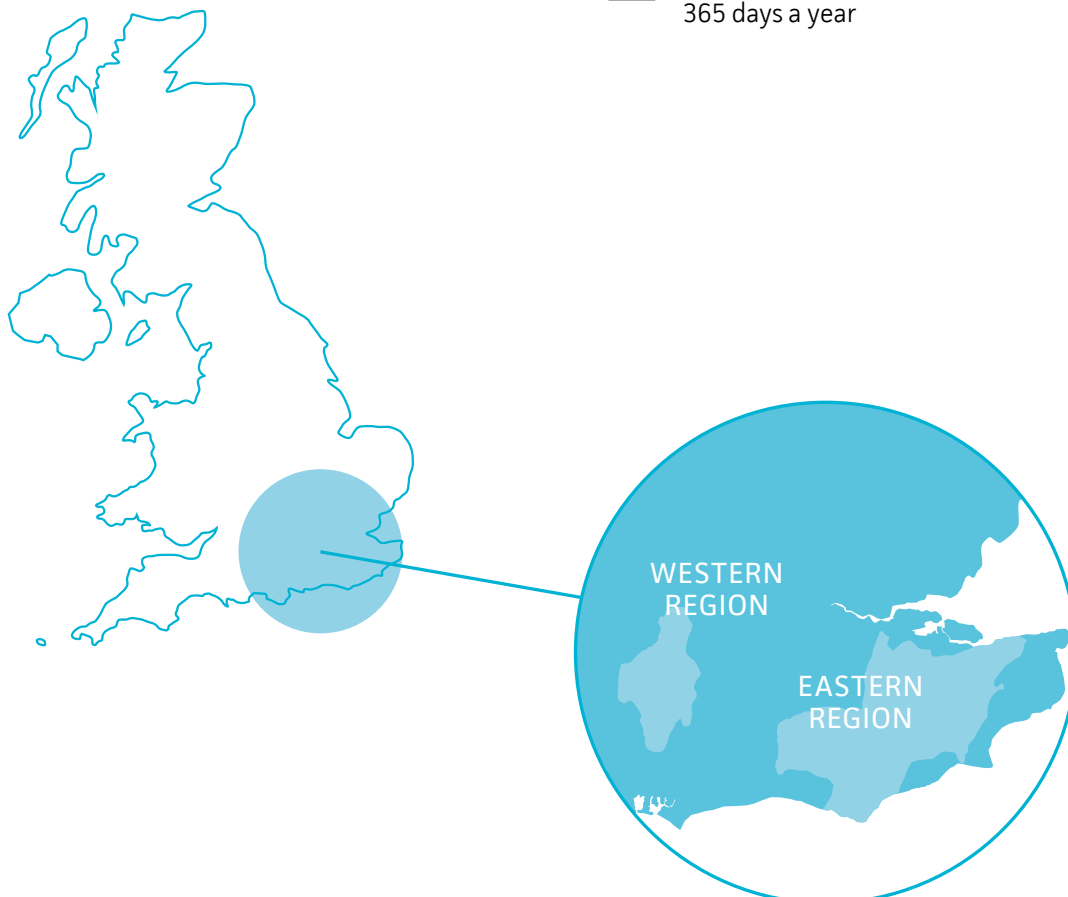
Our business

We supply top quality drinking water to **2.2 million** customers in the south east of England. Through a network of **9,000 miles** of pipe, we deliver **517 million** litres of water every day. The skill and expertise of our employees ensures our customers' water meets the highest of standards.

Our vision

Our vision is to be the water company people want to be supplied by and want to work for. Everything we do is underpinned by technical excellence.

Our supply area



Pure know h₂ow



517 million litres of water a day – that's how much water we supply to around 2.2 million people



83 water treatment works – that's how we ensure our water is of the highest quality



500,000 water quality tests each year – that's how we ensure your water meets the highest standards



9,000 miles of water mains – that's how we transfer fresh drinking water direct to your tap



983 employees – that's how we make sure your water supply runs 24 hours a day, 365 days a year

How we invest in your water

Where each £1 of your bill is spent.

Water extraction



8%

Getting the water to you



43%

Water treatment



21%

Customer service



8%

Interest & Tax



15%

Dividends



5%

Financial highlights

For the six months to 30 September 2018.

Revenue

£121.0m

Increase of 5.7 per cent on last year

Operating profit

£42.4m

Increase of 8.0 per cent on last year

Capital expenditure

£52.7m

Up from 48.9m last year

Cash generated from operating activities

£79.4m

Increase of 25.6 per cent on last year

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Chairman's introduction

I am pleased to present our interim report for the six months ended 30 September 2018.

Our vision is to be the water company people want to be supplied by and want to work for. This has been a period of intense activity for the company and its employees as we continue to strive to realise our vision and deliver on the commitments within our 2015 to 2020 business plan, deal with particular operational challenges from this summer's drought, and at the same time look to the future with the preparation of our draft Water Resources Management Plan (WRMP) and our ambitious business plan for the 2019 Price Review (PR19), which will take us through to 2025 and beyond.

Our 2015 to 2020 business plan puts customer satisfaction at the heart of everything we do. Our future plans build on this and on our commitments to both the environment and the communities in which we work, as we aim to take the lead on responsible business practice and to make a positive contribution to wider society.

Customer satisfaction, responsibly delivered

Our business plan for the 2020 to 2025 period was submitted to Ofwat in early September and simultaneously published on our website. This plan has been shaped with strong involvement of customers and community groups throughout the areas we serve and will see the company invest a further £472.0 million to improve the local water infrastructure over the five year period.

We have carried out a very extensive programme of research, discussions and consultations with some 13,000 customers, stakeholders, retailers, businesses, employees and an independent Customer Challenge Group chaired by Zoe McLeod. We would like to thank everyone who played a part in helping to shape our plans.

Our plan incorporates a comprehensive suite of ambitious commitments to improve performance in areas such as leakage and interruptions, water quality, greenhouse gas emissions, environmental impact, support for vulnerable customers and, of course, customer satisfaction. These commitments are backed by performance penalties if targets are missed, and rewards for out-performance. As an illustration of the level of ambition implicit in the plan, if we were unable to improve on our current performance levels we would incur a penalty of £35.0 million.

While delivering all these improved outcomes, the proposed average annual household bill is maintained at £204 before inflation for the next five years.

We now await Ofwat's assessment of our plan through a process which will run to the end of 2019.



Keeping water flowing whatever the weather

By the early summer we were starting to experience above average demand for water leading to the stepping up of our water efficiency messaging and a campaign encouraging customers to use water wisely during the heatwave, a recurring theme for the entirety of the summer in which the whole country experienced hotter than normal conditions for a number of weeks.

During this time our production teams geared up to produce an extra one hundred million litres of drinking water per day at the peak with employees working around the clock to produce the extra water needed.

Although the amount of untreated, raw water, available in reservoirs and aquifers was good for the time of year, and remained so throughout the hot weather, we asked customers to save water in order to help us meet demand for extra supplies of processed drinking quality water at peak times of the day.

Time to make every drop count

Christine from our Customer Care Team offers a shower timer to help make those showers a little shorter



Chairman's introduction continued



This year we became the first water company to achieve the BSI (British Standards Institution) verification certification for BS 18477, demonstrating the organisation provides a comprehensive service for identifying and responding to vulnerable customers.

We also joined forces with other water companies in the south east of the country to run a water-saving campaign in local media and radio, focussed on water-saving measures and the need for prudence when contemplating the use of such things as paddling pools and garden sprinklers. While demand was higher than normal throughout the summer, we believe the combined effects of our metering programme and customer communications helped keep the demands at manageable levels and we thank everyone who did their bit to save water.

Many of the activities we undertook during the summer, particularly in customer communications, benefited from lessons learned from the extreme freeze/thaw event we experienced at the end of 2017/18. Ofwat completed its own review into the impact of the freeze/thaw event across the whole country and the lessons to be learned. They set out where our plans worked well and where improvements could be made. We published our action plan in response to this on 28 September 2018 which included 61 actions we have agreed to. We will work closely with the industry to ensure best practice approaches are built into our emergency plans for any such future events.

Pure know h₂ow in action

In May we started construction of the company's largest ever single investment at the Keleher Water Treatment Works at Bray in Berkshire. This £21 million project will increase the capacity of the Keleher plant, which treats water extracted from the River Thames to drinking water standards from the current 45 million litres per day to 68 million litres per day.

The work got underway with a site clearance programme involving the removal of approximately 25,000 cubic metres of earthworks. Thanks to the dry summer weather this was completed ahead of schedule.

Within our water quality projects, we are seeing some really encouraging results in reducing what is known as the discolouration contact rate. This is a measure of the number of contacts we get from customers raising concerns over the appearance of their water. Such incidents can be the result of a number of factors but are largely based on the build-up over time of naturally occurring iron and manganese deposits within the distribution pipework network. This is being addressed through a pipework flushing programme and improvements to treatment work performance. In the nine months from January to September 2018 we received 1,042 discolouration contacts whereas, in the same period in 2017 we received 1,413 contacts. We expect further improvement as the programme continues.

Customer engagement and satisfaction

Between February and May 2018 we consulted on our latest draft Water Resources Management Plan, speaking to hundreds of customers and stakeholders across our supply area to gather their thoughts and opinions on our proposal which looks 60 years into the future.

After reviewing the representations alongside new data which has been made available to us we made a number of changes to our plan, including the reduction of leakage by 15 per cent by 2025, halving the amount of leakage from our current position to 44 million litres a day by 2050 and adopting a more ambitious target for water efficiency which, in the long term, could save an extra 150 million litres a day by 2080.

A national survey by the Institute of Customer Service's UK Customer Satisfaction Index (UKCSI) that measures customer satisfaction across the UK placed us eighth in the utility sector out of 28 organisations surveyed.

Based on 45,000 survey responses from across the country, the UKCSI gives a unique insight into the quality of customer service in the UK, looking at a range of satisfaction measures such as reliability and helpfulness of staff.

We were clearly very pleased our continued success in improving our customer experience has been reflected in the UKCSI. Our work is on-going to make our customer experience a smooth and positive one, and we have recently carried out a number of initiatives such as continued improvements to our responsive website services, and introducing 'One Bill' so we now also bill wastewater charges on behalf of 460,000 customers of Southern Water. This has been an important improvement for customers as many have said they wanted to be able to manage their water and wastewater bill through one account, just as our customers who have Thames Water as their wastewater service provider have done for many years.

Making a positive impact for society

The company has committed to continue to build our environment, social and governance (ESG) framework during the year and we aim to be a recognised leading responsible business. Within the new business plan we have developed a responsible business strategy and 10 new responsible business commitments to reflect the actions and behaviours customers expect a responsible business to display.

Environment

Congratulations are in order for our environmental team for scooping the Water Industry Awards prize for Water Resilience Initiative of the Year for our pioneering water and farming partnership called 'Together we knowh₂ow'. This project has also recently been shortlisted for the Utility Week Awards.

Working closely with farmers and landowners the initiatives aim is to stop soils, fertiliser and pesticides washing from fields into rivers and groundwater resources. This prevents the expense of removing these substances at the water treatment works, and means farmers and landowners benefit by losing less of these substances to waste.

We are proud of our environmental record and we continue to celebrate our many successes in conserving, protecting and developing wildlife habitats at many of our sites.

20 years of careful habitat management at our Deep Dean Water Treatment Works in East Sussex has paid off for one of Britain's most endangered insects, as the wart-biter cricket makes a successful return to the South Downs. Working alongside Natural England, Buglife, the Zoological Society of London and the South Downs National Park Authority, we carried out our third release of the rare species last year. Now, following two recent surveys, 14 new crickets have been found in the area.

The grayling butterfly, *Hipparchia semele*, one of the country's most threatened species has been spotted within the heathland restoration corridor created by South East Water after a five-kilometre strategic water main was laid through Swinley Forest near Bracknell in 2015. As part of the £6.5 million project, we formed the wide wildlife corridor to create heathland that enables species, such as the grayling butterfly, to thrive.

Social

This year we became the first water company to achieve the BSI (British Standards Institution) verification certification for BS 18477, demonstrating the organisation provides a comprehensive service for identifying and responding to vulnerable customers, something which is a priority for our business. This includes how our Customer Care Team will provide support if people are in financial difficulty, or need bottled water deliveries during a supply interruption.

As a local water supplier we aim to engage with our customers at every opportunity, a total of 2,400 people interacted with our staff at a wide range of community events during the first half of the year. These events included drop-in sessions for engineering schemes, open days at our reservoirs and water treatment works, school talks, plus fetes, fairs and attendance at other outside events with our trailer unit.

Chairman's introduction continued

In addition we issued 111,000 letters to customers about forthcoming engineering work's and kept our community leaders informed with news and updates about construction projects and incidents in their areas. Our automated emailing system allows us to track the number of emails opened and see where recipients click on links in the message for further information from the company.

We have a staff council which is a partnership between the company, employee representatives and the trade union, UNISON. This group has worked successfully for a number of years and is always well-informed of any changes taking place. We believe firmly engaged employees go the extra mile to deliver great service.

A new appraisal system entitled iReview has been introduced, which is based on self and manager assessments. The percentage of staff receiving an iReview rating was 87. This is a great start and we hope to increase engagement further.

Governance

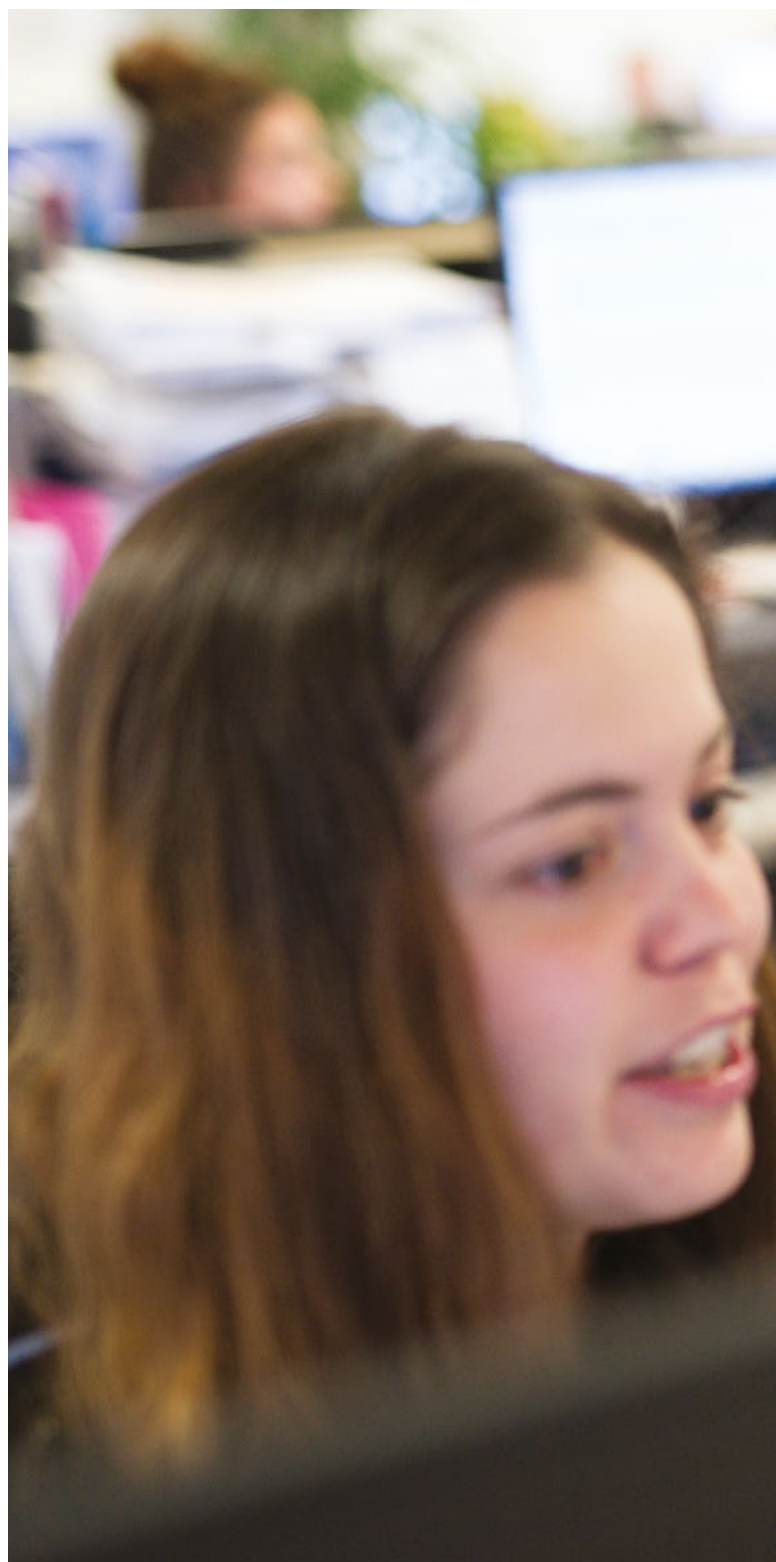
The Board is committed to maintaining the highest standards of corporate governance and transparency. We fully comply with Ofwat's defined governance requirements, including maintaining an independent Chairman and having a larger number of independent Non-executive directors (iNeds) than either shareholder representative directors or executive directors.

In July we appointed Célia Pronto as a new iNed, in anticipation of Emma Gillthorpe's retirement after completing six years of service in September. Célia brings extensive relevant experience in customer engagement and digital. I would like to formally welcome Célia to the Board and thank Emma for her contribution over the past six years.

In terms of reporting and transparency, we were pleased that our published Company Monitoring Framework was assessed by Ofwat in November 2017 as being in the highest "Self-assured" category. Only two other of the 18 water utilities were in this category and we are the only one to be assessed at this level for two years running.

Group structure

In April 2017 Ofwat introduced competition in retail activities for Non-Household Customers. This required us to separate our related retail activities into a standalone business which competes with other retailers in our supply area. On 1 July this year we completed the sale of the Non-Household business to Castle Water and hence we no longer provide Non-Household retail services. We have worked closely with Castle Water to ensure a smooth transition for customers.



A significant portion of the group's debt facilities mature in September 2019 and work has now started to put new facilities in place well ahead of that date. The amount payable on maturity will be in the region of £311 million. As part of this process the group's gearing ratio will be reduced by the injection of £54 million of equity by the group's shareholders. The balance of the repayment will be raised by new loan funding.

Results and key financial performance indicators

The results published in this statement summarise our performance for the six month period to 30 September 2018. The financial statements are prepared under International Financial Reporting Standards ("IFRS") and incorporate the performance of South East Water Limited and our subsidiary, South East Water (Finance) Limited.



Customer satisfaction

Our Customer Care Team is there to help all our customers ensure they can access the right services for their needs

Chairman's introduction continued

Revenue for the period was £121.0 million compared with £114.5 million for the same period in the previous year. The increase of £6.5 million is largely due to the change in our accounting policy for developer contributions and similar receipts following the adoption of IFRS 15 which has led to £3.1 million of additional revenue being reported in the income statement. An increase in prices averaging 4.6 per cent for the year amounted to £5.1 million of increased revenue coupled with an increase in consumption due to the hot summer weather amounted to £0.7 million. This is partially offset by the impact of metering which has reduced revenue by £2.0 million and £0.5 million less revenue from non-household customers.

Net operating costs for the period to 30 September 2018 were £84.9 million, which is some £5.9 million higher than the corresponding period last year. This was primarily due to higher contractor and staff costs due to an increase in reactive maintenance, including mains bursts on the network, of £1.8 million and the impact of IFRS 15 on the treatment of the costs and associated contributions for properties that are connected to our water supply of £1.0 million.

Additionally, increased depreciation due to the continued high investment in the company's assets of £1.3 million, additional costs of £0.8 million relating to the heatwave during the summer and £1.0 million of other inflationary costs added to the higher operation costs in the year when compared to the previous year.

Operating profit was £42.4 million for the period to 30 September 2018 which compares with £39.3 million in the prior year. Operating profit as a percentage of revenue has increased from 34.3 per cent in the first half of 2017/18 to 35.1 per cent in the current year.

Finance costs have decreased by £1.2 million from £27.0 million to £25.8 million. This reflects the lower fair value charge for our interest rate swap, as it nears maturity, of £2.6 million offset by £1.4 million of increased indexation on our other loans and bonds due to higher inflation during the period to 30 September 2018.

Profit before tax was £27.7 million compared with £14.7 million for the same period last year. This represents 22.9 per cent of revenue compared with 12.8 per cent for the corresponding period last year.

The company has incurred a tax charge of £2.7 million in the period compared to £1.7 million for the period to 30 September 2017, being £0.1 million of current tax on our ordinary operations and £2.6 million of deferred tax.

As a result of the above, profit after tax has increased from £13.0 million to £25.0 million for the first six months of the year.

Our dividend policy allows for dividends to be paid to our parent company which ensures that intercompany financial obligations are able to be settled. The increase in dividend this year of £5.0m, compared with the same period last year, relates to additional financial requirements of our parent and is in line with our dividend policy. The dividend paid by the Group's ultimate UK parent company was maintained at the same level as the prior year.

Net cash generated from operations was £79.4 million for the period to 30 September 2018 compared to £64.5 million in the same period for the previous year. This reflects a £14.9 million improvement in cash collections across the business, including £2.0 million in respect of income from commercial operations, when compared to the prior year.

Interest of £9.1 million (2017: £8.8 million) due on 30 September 2018 has been paid in October in both the current and previous financial years due to the due date falling at a weekend.

We continue to comply with the financial covenants set out in our securitisation structure and continue to hold ratings from Moody's and Standard & Poor's consistent with the requirements of both our securitisation and our instrument of appointment.

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Our 2015 to 2020 business plan puts customer satisfaction at the heart of everything we do.

Principal risks and uncertainties

The principle risks and uncertainties facing the business are set out in the Strategic Report within the group's Annual Report for the financial year 2017/18, which can be found on the South East Water website.

Going concern

The directors are satisfied that the group has sufficient resources to continue in operation for the foreseeable future; a period of not less than 12 months from the date of this report.

Looking ahead

For the rest of this year and through 2019 we will continue to focus on delivering improved customer service and successfully closing out the current business plan while devoting increasing attention to developing detailed and innovative proposals for the execution of the next five year business plan. Innovation is key to delivering these ambitious targets and we are working with staff, partners and the supply chain to drive this innovation forward.



On behalf of the Board I would like to thank all the employees and business partners at South East Water who have worked tirelessly over the last six months. It has been an exceptional start to the year and our people have worked with dedication and passion throughout in order to keep delivering great customer service in challenging operational conditions, while also planning ahead for the long-term growth of the south east region and ensuring we maintain an excellent and resilient water service and a sustainable future for the local communities we work for.

Nick Salmon

Chairman
14 December 2018

Statement of directors' responsibilities

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The directors are also responsible for the maintenance and integrity of the corporate and financial information included on the company's website.



The directors confirm that to the best of their knowledge:

- the condensed group financial statements have been prepared in accordance with IAS 34 Interim Financial Reporting as endorsed by the European Union; and
- the condensed group statements herein include a fair review of the information required by the Disclosure and Transparency Rules 4.2.7R

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the group and enable them to ensure that the group financial statements comply with the Companies Act 2006. They are responsible for safeguarding the assets of the group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The directors are also responsible for the maintenance and integrity of the corporate and financial information included on the company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Paul Butler

Managing Director
14 December 2018

Condensed group income statement

for the six months ended 30 September 2018

	Notes	Six months ended 30 September 2018 £000	Six months ended 30 September 2017 £000
Revenue	4	120,986	114,450
Group net operating costs	6	(84,900)	(79,009)
Other income	4	6,336	3,840
Group operating profit		42,422	39,281
Profit on disposal of non-household customer base	7	8,165	-
Finance costs	8	(25,765)	(26,957)
Finance income	9	2,859	2,349
Profit before taxation		27,681	14,673
Taxation	10	(2,715)	(1,662)
Profit for the period		24,966	13,011
Earnings per share			
Basic and diluted from continuing operations		50.63p	26.38p

Condensed group statement of comprehensive income

for the six months ended 30 September 2018

	Six months ended 30 September 2018 £000	Six months ended 30 September 2017 £000
Profit for the period	24,966	13,011
Items that will not be reclassified subsequently to profit or loss:		
Remeasurement of defined benefit asset/liability	1,534	(3,159)
Deferred tax on defined benefit pension schemes	(262)	537
	1,272	(2,622)
Total comprehensive income for the period attributable to owners of the company	26,238	10,389

Condensed group statement of financial position

as at 30 September 2018

	Notes	30 September 2018 £000	31 March 2018 £000	30 September 2017 £000
Non-current assets				
Intangible assets	12	11,137	10,758	10,830
Property, plant and equipment	13	1,528,087	1,501,707	1,480,018
Amount due from parent undertaking	17	189,918	190,013	190,013
Defined benefit pension surplus		25,086	21,229	8,104
		1,754,228	1,723,707	1,688,965
Current assets				
Inventories		334	236	219
Trade and other receivables	14	77,314	78,255	77,336
Cash and cash equivalents	15	26,082	6,528	27,697
		103,730	85,019	105,252
Total assets		1,857,958	1,808,726	1,794,217
Current liabilities				
Loans and borrowings	17/18	(219,782)	(20,000)	(15,000)
Derivative financial instruments	17	(105,143)	-	-
Trade and other payables	19	(119,806)	(94,379)	(110,544)
Deferred income		(6,714)	(7,593)	(7,169)
Provisions		(2,495)	(2,515)	(2,361)
		(453,940)	(124,487)	(135,074)
Non-current liabilities				
Loans and borrowings	16/17	(708,324)	(900,897)	(888,586)
Derivative financial instruments	16/17	-	(104,169)	(104,501)
Trade and other payables	16	(5,791)	(5,979)	(5,347)
Net deferred tax liabilities		(142,895)	(140,085)	(133,080)
Defined benefit pension liability		-	-	(1,378)
Deferred income	3	(3,690)	(74,471)	(72,157)
		(860,700)	(1,225,601)	(1,205,049)
Total liabilities		(1,314,640)	(1,350,088)	(1,340,123)
Net assets		543,318	458,638	454,094
Equity				
Ordinary share capital		49,312	49,312	49,312
Revaluation reserve		253,820	256,396	258,965
Retained earnings		240,186	152,930	145,817
Total equity		543,318	458,638	454,094

The notes on pages 18 to 31 are an integral part of these condensed group financial statements.

Condensed group statement of changes in equity

for the six months ended 30 September 2018

	Issued share capital £000	Revaluation reserve £000	Retained earnings £000	Total equity £000
At 31 March 2018	49,312	256,396	152,930	458,638
IFRS 15 adoption (see note 3)	-	-	72,442	72,442
At 1 April 2018	49,312	256,396	225,372	531,080
Profit for the period	-	-	24,966	24,966
Other comprehensive loss	-	-	1,272	1,272
Total comprehensive income	-	-	26,238	26,238
Dividends (see note 11)	-	-	(14,000)	(14,000)
Amortisation of revaluation reserve	-	(3,063)	3,063	-
Release revaluation on disposals	-	(34)	34	-
Deferred tax on reserve releases	-	521	(521)	-
At 30 September 2018	49,312	253,820	240,186	543,318

for the six months ended 30 September 2017

	Issued share capital £000	Revaluation reserve £000	Retained earnings £000	Total equity £000
At 1 April 2017	49,312	261,549	141,844	452,705
Profit for the period	-	-	13,011	13,011
Other comprehensive loss	-	-	(2,622)	(2,622)
Total comprehensive income	-	-	10,389	10,389
Dividends (see note 11)	-	-	(9,000)	(9,000)
Amortisation of revaluation reserve	-	(3,064)	3,064	-
Release revaluation on disposals	-	(43)	43	-
Deferred tax on reserve releases	-	523	(523)	-
At 30 September 2017	49,312	258,965	145,817	454,094

Condensed group statement of cash flows

for the six months ended 30 September 2018

	Notes	Six months ended 30 September 2018 £000	Six months ended 30 September 2017 £000
Operating activities			
Net cash flow from operating activities		79,424	64,450
Interest received		2,540	2,225
Interest paid		(9,120)	(6,337)
Group tax relief paid		(652)	(2,000)
Net cash flow before investing and financing activities		72,192	58,338
Investing activities			
Proceeds from sale of property, plant and equipment		639	103
Purchase of property, plant and equipment		(47,224)	(47,807)
Purchase of intangible assets		(1,927)	(1,414)
Sale of non-household customer base		9,665	-
Fixed asset contributions received		388	1,106
Net cash flow used in investing activities		(38,459)	(48,012)
Financing activities			
New bank loans received		-	15,000
Issue cost of listed debt		(179)	-
Dividends paid to shareholder	11	(14,000)	(9,000)
Net cash flow used in financing activities		(14,179)	6,000
Increase in cash and cash equivalents		19,554	16,326
Cash and cash equivalents at 1 April		6,528	11,371
Cash and cash equivalents at 30 September	15	26,082	27,697

Cash flow from operating activities

for the six months ended 30 September 2018

	Six months ended 30 September 2018 £000	Six months ended 30 September 2017 £000
Profit on operating activities	42,422	39,281
<i>Adjustments for:</i>		
Depreciation and impairment of property, plant and equipment	24,184	22,721
Amortisation and impairment of intangibles	1,548	1,642
Profit on disposal of fixed assets in ordinary course of business	(330)	(15)
Difference between pension contributions paid and amounts recognised in the income statement	(2,016)	(1,973)
<i>Changes in working capital:</i>		
Increase in trade and other receivables	(1,049)	(5,137)
Increase in inventory	(98)	(5)
Increase in trade and other payables	14,763	7,936
Net cash flow from operating activities	79,424	64,450

Notes to the condensed group financial statements

for the six months ended 30 September 2018

1. Basis of preparation

The condensed group financial statements for the six months ended 30 September 2018 are set out on pages 13 to 31, and have been prepared in accordance with the Disclosure and Transparency Rules of the Financial Conduct Authority and IAS 34 Interim Financial Reporting as endorsed by the European Union. The statements should be read in conjunction with the financial statements for the year ended 31 March 2018, which have been prepared in accordance with International Financial Reporting Standards ("IFRS") endorsed by the European Union.

The condensed group financial statements are presented in sterling.

These interim financial results are neither audited nor reviewed by our auditor. The information for the year ended 31 March 2018 does not comprise statutory accounts within the meaning of section 434 of the Companies Act 2006. Statutory accounts for the year ended 31 March 2018 were approved by the Board of Directors on 13 July 2018 and delivered to the Registrar of Companies. The report of the auditors on those accounts was not qualified, did not include any reference to any matters to which the auditors drew attention by way of emphasis without qualifying the report and did not contain any statement under section 498(2) or (3) of the Companies Act 2006.

2. Accounting policies

Changes in accounting policies

The accounting policies adopted are consistent with those of the financial statements for the year ended 31 March 2018 as described in those financial statements except for the changes brought about by adoption of IFRS 9 *Financial Instruments* ("IFRS 9") and IFRS 15 *Revenue from Contracts with Customers* ("IFRS 15") on 1 April 2018.

Revenue

When recognising revenue, the group applies the five criteria introduced by IFRS 15. Revenue is recognised to the extent that it is probable that the economic benefits will flow to the group, the performance obligations in the contracts with "named" customers have been met and the revenue can be reliably measured. All revenue arises within the United Kingdom and is recorded net of VAT. The company only recognises revenue in respect of "named" customers.

Infrastructure charges

Infrastructure charges represent the fees charged to property developers and others for connecting new properties and water outlets to the group's network. These fees are recognised in the income statement upon completion of the project to which they relate.

Grants and contributions

Grants and contributions are received in respect of both infrastructure and non-infrastructure assets. The receipts are recognised as deferred income on the balance sheet until completion of the work to which they relate, at which time they are released to the income statement.

Financial instruments

The group's financial instruments comprise fixed and variable rate borrowings, index linked loans, fixed rate debentures, an interest rate swap, finance leases, a loan to its parent undertaking, cash, short-term and medium-term bank deposits, trade receivables and trade and other payables.

Notes to the condensed group financial statements

for the six months ended 30 September 2018

2. Accounting policies (continued)

Recognition

Financial instruments are recognised on the statement of financial position when the group becomes party to the contractual provisions of the instrument. The group determines the classification of its financial liabilities at initial recognition.

A provision for twelve month expected credit loss is recognised in the income statement to establish a loss allowance on initial recognition.

Impairment of financial assets

At each reporting date an assessment is carried out to determine whether there is any indication that the credit risk on financial assets has increased significantly. If this is considered to be the case, full life-time expected credit loss is recognised in the income statement. Where there is objective evidence that an impairment loss has arisen, the loss is recognised in the income statement in the year in which the respective assessment takes place. Impaired debts are derecognised when they are assessed as irrecoverable.

Short term trade and other receivables

Short term trade receivables are recognised and carried at original invoice amount less an allowance for any doubtful debts. An estimate for the provision for doubtful debts is calculated by the group's management based on applying expected recovery rates to an aged debt profile and an assessment of the current and future economic conditions.

3. Transition disclosures

The group has adopted IFRS 9 and IFRS 15 in the period. Details of the impact of the adoption of these standards are provided below.

IFRS 9 Financial Instruments

IFRS 9 specifies how the group should classify and measure financial assets and liabilities. In adopting the Standard, the group has assessed the classification of its financial instruments and reclassified assets and liabilities as appropriate (see note 17). The group has also recognised an allowance for credit loss in its income statement on its relevant financial assets. A provision for this allowance has been created and offset against the carrying value of the relevant asset in the group statement of financial position.

IFRS 15 Revenue from Contracts with Customers

IFRS 15 establishes the principles the group applies when reporting information about revenue and the cash flows arising from contracts with customers. In adopting the standard the group has applied the steps for recognising revenue from customers. IFRS 15 has been adopted using the modified retrospective method which has led to the accumulated historic adjustments being made to the opening balances at 1 April 2018.

Notes to the condensed group financial statements

for the six months ended 30 September 2018

3. Transition disclosures (continued)

The impact of the adoption of IFRS 15 on the group's financial statements in the period has been:

	Six months ended 30 September 2018 £000	Adjustment for the adoption of IFRS 15 £000	Six months ended 30 September 2018 £000
Revenue			
Unmetered water income	13,433	-	13,433
Metered water income	100,754	-	100,754
Other sales	3,666	3,133	6,799
Total Revenue	117,853	3,133	120,986
Group net operating costs	(83,941)	(959)	(84,900)
Other income	6,336	-	6,336
Group operating profit	40,248	2,174	42,422
Profit on disposal of non-household customer base	8,165	-	8,165
Finance costs	(25,765)	-	(25,765)
Finance income	2,859	-	2,859
Profit before taxation	25,507	2,174	27,681
Taxation	(2,522)	(193)	(2,715)
Profit for the period	22,985	1,981	24,966

The adjustments in the current year to the financial statements as a result of the adoption of IFRS 15 are required because:

- The adjustment of £3.1 million to other sales reflects the deposits and contributions received from developers for contracts where the performance objectives have been met in the period. This has been released from non-current trade and other payables and deferred income respectively in the group statement of financial position
- The adjustment to group net operating costs reflects the contributions in the period in excess of the costs taken to fixed assets on new connections. This was previously offset against operating costs but is now included in other sales. This revenue has been taken to deferred income in the group statement of financial position
- The adjustment to taxation reflects the additional tax charged on the above adjustments. The additional tax has been relieved against losses in other companies in the HDF (UK) Holdings Limited group of companies and has been added to intercompany creditors in the group statement of financial position
- The adoption of IFRS 15 has had no impact on the group statement of changes in equity in the year other than those changes to retained earnings and total equity noted in the table above and to adjust the opening balances on retained earnings and total equity as detailed on page 15
- The adoption of IFRS 15 has had no impact on the group statement of cash flows

Notes to the condensed group financial statements

for the six months ended 30 September 2018

3. Transition disclosures (continued)

The impact of the adoption of IFRS 15 on the group's opening statement of financial position has been:

	1 April 2018 £000	Adjustment for the adoption of IFRS 15 £000	1 April 2018 £000
Non-current assets	1,723,707	-	1,723,707
Current assets	85,019	-	85,019
Total assets	1,808,726	-	1,808,726
Current liabilities	(124,487)	-	(124,487)
Non-current liabilities			
Loans and borrowings	(900,897)	-	(900,897)
Derivative financial instruments	(104,169)	-	(104,169)
Trade and other payables	(5,979)	544	(5,435)
Net deferred tax liabilities	(140,085)	-	(140,085)
Deferred income	(74,471)	71,898	(2,573)
	(1,225,601)	72,442	(1,153,159)
Total liabilities	(1,350,088)	72,442	(1,277,646)
Net assets	458,638	72,442	531,080
Equity			
Ordinary share capital	49,312	-	49,312
Revaluation reserve	256,396	-	256,396
Retained earnings	152,930	72,442	225,372
Total equity	458,638	72,442	531,080

The adjustments to non-current trade and other payables and non-current deferred income reflect the release of deposits and contributions from developers for contracts that have been completed in prior years. The revenue from these contracts has previously been amortised over the lives of the assets to which they relate.

Notes to the condensed group financial statements

for the six months ended 30 September 2018

4. Total income

	Six months ended 30 September 2018 £000	Six months ended 30 September 2017 £000
Revenue		
Unmetered water income	13,433	19,083
Metered water income	100,754	92,573
Other sales	6,799	2,794
Total revenue	120,986	114,450
Other income		
Rental income	636	566
Sundry income	5,700	3,274
Total other income	6,336	3,840
Total income	127,322	118,290

All revenue is from customers within the United Kingdom.

Notes to the condensed group financial statements

for the six months ended 30 September 2018

5. Segmental analysis

The group's revenue mainly arises from the supply of water and related activities. The activities of the group, for management purposes, fall into three operating areas being the supply of potable water on a wholesale basis, the supply of potable water and waste water services on a retail basis, both of which are governed by the Water Act 2014, and related non-regulated activities.

The group analyses results by segment to operating profits only, therefore no segmental statement of financial position or statement of cash flows are presented.

Period to 30 September 2018	Wholesale activities £000	Retail activities £000	Other activities £000	Total £000
Total income	109,665	11,099	6,558	127,322
Operating profit	37,899	1,309	3,214	42,422
Profit on disposal of non-household customer base				8,165
Finance costs				(25,765)
Finance income				2,859
Profit before taxation				27,681
Taxation				(2,715)
Profit for the period				24,966

Period to 30 September 2017				
Total income	101,921	12,329	4,040	118,290
Operating profit	36,019	1,725	1,537	39,281
Finance costs				(26,957)
Finance income				2,349
Profit before taxation				14,673
Taxation				(1,662)
Profit for the period				13,011

6. Net operating costs

	Six months ended 30 September 2018 £000	Six months ended 30 September 2017 £000
Employee benefits expenses	15,455	14,662
Asset expenses	25,402	24,348
Other operating expenses	44,043	39,999
	84,900	79,009

Notes to the condensed group financial statements

for the six months ended 30 September 2018

7. Profit on disposal of non-household customer base

On 1 May 2018, the group sold its rights to the non-household customer base to its fellow wholly owned subsidiary, Invicta Water Limited, for a consideration of £10.0 million which has resulted in a profit on disposal of £8.2 million. The rights to the non-household customer base are an internally generated intangible asset and, as per IAS 38, these were not recognised on the group's statement of financial position.

Following the sale of the rights to the non-household customer base, an additional charge for the doubtful debts of £1.5 million has been provided to reflect the increased risk of non-payment of the outstanding debt at the date of sale following the transfer of the customers to another retailer.

Subsequently Invicta Water Limited was sold to Castle Water Holdings Limited on 1 July 2018.

	Six months ended 30 September 2018 £000	Six months ended 30 September 2017 £000
Proceeds from sale	10,000	-
Legal fees	(244)	-
Provision for doubtful debts	(1,500)	-
Consultancy	(91)	-
	8,165	-

8. Finance costs

	Six months ended 30 September 2018 £000	Six months ended 30 September 2017 £000
Effective interest on listed debt	11,371	11,129
Fair value movements on interest rate swap	974	3,585
Indexation on listed debt	2,908	3,143
Interest on index linked loans	6,032	5,810
Indexation on index linked loans	4,208	3,146
Other finance costs	1,315	1,189
	26,808	28,002
Less: interest capitalised	(1,043)	(1,045)
	25,765	26,957

Notes to the condensed group financial statements

for the six months ended 30 September 2018

9. Finance income

	Six months ended 30 September 2018 £000	Six months ended 30 September 2017 £000
Interest receivable from group undertakings	2,490	2,210
Pension fund finance credit	314	124
Interest receivable on bank balances and short term deposits	55	15
	2,859	2,349

10. Taxation

	Six months ended 30 September 2018 £000	Six months ended 30 September 2017 £000
Current taxation charge	165	940
Deferred taxation charge	2,550	722
	2,715	1,662

The current tax charge is recognised based on management's estimate of the weighted average annual corporation tax rate expected for the full financial year.

11. Dividends

	Six months ended 30 September 2018 £000	Six months ended 30 September 2017 £000
Equity dividends paid during the period of 28.4p per share (2017: 18.3p)	14,000	9,000

Notes to the condensed group financial statements

for the six months ended 30 September 2018

12. Intangible assets

	£000
Net book amount	
At 1 April 2018	10,758
Additions for the period	1,908
Reclassification of assets in the period	19
Amortisation for the period	(1,548)
At 30 September 2018	11,137
Net book amount	
At 1 April 2017	11,058
Additions for the year	3,554
Amortisation for the year	(3,399)
Reclassification of assets in the period	(448)
Disposals for the year	(1)
Impairment for the year	(6)
At 31 March 2018	10,758
Net book amount	
At 1 April 2017	11,058
Additions for the period	1,953
Reclassification of assets in the period	(539)
Amortisation for the period	(1,642)
At 30 September 2017	10,830

Notes to the condensed group financial statements

for the six months ended 30 September 2018

13. Property, plant and equipment

	£000
Net book amount	
At 1 April 2018	1,501,707
Additions for the period	50,752
Reclassification of assets in the period	(13)
Disposals for the period	(173)
Depreciation for the period	(24,186)
At 30 September 2018	1,528,087
Net book amount	
At 1 April 2017	1,455,380
Additions for the year	92,410
Disposals for the year	(279)
Reclassification of assets in the period	448
Depreciation for the year	(46,233)
Impairment for the year	(19)
At 31 March 2018	1,501,707
Net book amount	
At 1 April 2017	1,455,380
Additions for the period	46,908
Reclassification of assets in the period	539
Disposals for the period	(88)
Depreciation for the period	(22,721)
Reclassification of assets in the period	-
At 30 September 2017	1,480,018

Notes to the condensed group financial statements

for the six months ended 30 September 2018

14. Trade and other receivables

	30 September 2018 £000	31 March 2018 £000	30 September 2017 £000
<i>Financial asset receivables</i>			
Trade receivables	33,630	34,463	33,580
Accrued income	36,035	35,506	36,879
Amounts due from group undertakings	378	26	273
	70,043	69,995	70,732
<i>Non-financial asset receivables</i>			
Prepayments	5,203	5,132	4,727
Other receivables	2,068	3,128	1,877
	7,271	8,260	6,604
	77,314	78,255	77,336

15. Cash and cash equivalents

	30 September 2018 £000	31 March 2018 £000	30 September 2017 £000
Cash at bank and in hand	26,082	6,528	27,697

16. Non-current financial liabilities

	30 September 2018 £000	31 March 2018 £000	30 September 2017 £000
Irredeemable debenture stock	991	991	991
Listed bonds	332,170	529,337	526,284
Index linked loans	375,163	370,569	361,311
Loans and borrowings	708,324	900,897	888,586
Derivative financial instruments	-	104,169	104,501
Trade and other payables	5,791	5,979	5,347
	714,115	1,011,045	998,434

Notes to the condensed group financial statements

for the six months ended 30 September 2018

17. Financial instruments

Fair values of financial assets and financial liabilities

Fair value is the amount at which a financial instrument could be exchanged in an arm's length transaction between informed and willing parties. In the opinion of the directors, the fair values of the financial assets and liabilities of the group (apart from the specific items shown in the fair value table below) are not materially different from the book values.

	Book Value 30 September 2018 £000	Fair Value 30 September 2018 £000	Book Value 31 March 2018 £000	Fair Value 31 March 2018 £000	Book Value 30 September 2017 £000	Fair Value 30 September 2017 £000
Measured at amortised cost						
Amounts due from parent undertaking	189,918	174,736	190,013	142,573	190,013	173,920
Current liabilities						
Bank loan	20,000	20,000	20,000	20,000	15,000	15,000
Listed bond	199,782	222,960	-	-	-	-
	219,782	242,960	20,000	20,000	15,000	15,000
Non-current liabilities						
Irredeemable debentures	991	935	991	862	991	841
Listed bonds	332,170	449,177	529,337	672,137	526,284	631,450
Index linked loans	375,163	677,802	370,569	694,765	361,311	660,655
	708,324	1,127,914	900,897	1,367,764	888,586	1,292,946

The following table details the financial instruments that are carried in the group's books at the fair value at 30 September 2018.

	Book and Fair Value 30 September 2018 £000	Book and Fair Value 31 March 2018 £000	Book and Fair Value 30 September 2017 £000
At fair value through profit or loss			
Derivative financial instruments - Interest rate swap	105,143	104,169	104,501

The book value of the interest rate swap has been adjusted to reflect its fair value.

Notes to the condensed group financial statements

for the six months ended 30 September 2018

17. Financial instruments (continued)

Fair value hierarchy

The group held the following financial instruments measured at fair value:

	Total £000	Level 1 £000	Level 2 £000	Level 3 £000
<i>Financial liabilities at fair value through profit or loss</i>				
30 September 2018				
Interest rate swap	(105,143)	-	(105,143)	-
31 March 2018				
Interest rate swap	(104,169)	-	(104,169)	-
30 September 2017				
Interest rate swap	(104,501)	-	(104,501)	-

During the reporting period ended 30 September 2018, there were no transfers between Level 1 and Level 2 fair value measurements and no transfers into and out of Level 3 fair value measurements.

The group uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation technique:

- Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities;
- Level 2: other techniques for which all inputs with a significant effect on the recorded fair value are observable, either directly or indirectly; and
- Level 3: techniques using inputs which have a significant effect on the recorded fair value that are not based on observable market data.

18. Current loans and borrowings

	30 September 2018 £000	31 March 2018 £000	30 September 2017 £000
<i>Financial liabilities</i>			
Bank loan	20,000	20,000	15,000
Listed bonds	200,000	-	-
Unamortised costs	(218)	-	-
	219,782	20,000	15,000

Notes to the condensed group financial statements

for the six months ended 30 September 2018

19. Current liabilities

	30 September 2018 £000	31 March 2018 £000	30 September 2017 £000
<i>Financial liabilities</i>			
Trade payables	11,995	13,610	10,674
Amounts due to group undertakings	15,607	9,217	10,191
Other payables	11,771	1,866	5,119
Accruals	47,525	32,556	46,088
	86,898	57,249	72,072
<i>Non-financial liabilities</i>			
Payments received in advance	31,853	36,118	37,516
Other taxes and social security	1,055	1,012	956
	32,908	37,130	38,472
	119,806	94,379	110,544

20. Post balance sheet event

On 26 October 2018, the High Court issued a judgment involving the Lloyds Banking Group's defined benefit pension schemes in relation to Guaranteed Minimum Pension (GMP) benefits being calculated differently for men and women. The judgment concluded that the schemes should be amended to equalise pension benefits for men and women in relation to GMP benefits. The issues determined by the judgment arise in relation to many other defined benefit pension schemes.

We are working with the trustees of our pension schemes and our advisers to assess the impact of the judgment on our schemes, but high level estimates based on industry expectations indicate this could be up to around 1-2 per cent of accrued liabilities. This issue is being treated as a plan amendment and the impact is expected to be recognised as a past service cost in our 31 March 2019 year-end accounts.

Overall, our pension schemes are appropriately funded and the condensed group statement of financial position shows the defined benefit schemes have a surplus of approximately £25.1m on an IAS 19 basis.

