

YORKSHIRE WATER SERVICES LTD

**INTERIM REPORT FOR THE SIX MONTHS
ENDED 30 SEPTEMBER 2008**

OVERVIEW

The first half year shows a strong operational performance and robust financial results despite the current economic climate.

KEY FINANCIAL PERFORMANCE INDICATORS for the six months to 30 September

| | 2008 | 2007 | Increase |
|--|----------------|---------|----------|
| Turnover | £425.0m | £396.9m | 7.1% |
| Regulated operating costs | £142.4m | £135.0m | 5.5% |
| Operating profit | £192.2m | £179.5m | 7.1% |
| Regulated capital investment | £160.6m | £189.0m | (15.0%) |
| Total net debt to Regulatory Capital Value (RCV) | 64.6% | 62.2% | 2.4% |

FINANCIAL PERFORMANCE

Turnover increased by 7.1% to £425.0m (2007: £396.9m), compared with an average tariff increase of 8.2%. The effects of poor summer weather and the economic climate have had an adverse impact on measured water consumption by both households and businesses leading to lower than anticipated turnover in the first half year.

Operating profit also increased by 7.1% to £192.2m (2007: £179.5m), including a 5.5% increase in regulated operating costs. Efficiencies delivered through the Clearwater and 2020 initiatives have partly offset a 20% increase in energy costs. In addition, the price of chemicals used in the treatment of water has escalated well above the level of inflation. After eliminating the impact of these items, other costs have risen by a level well below inflation due to ongoing efficiency programmes already mentioned. We still expect to outperform Ofwat's target for operating costs over the 5 year period despite the impact of energy and commodity prices.

During the period adjusted net debt increased from £2,554.2m at 30 September 2007 to £2,852.3m at 30 September 2008 with a corresponding increase in net debt to RCV from 62.2% to 64.6%, remaining in line with the 55-65% range assumed by Ofwat in the 2004 Final Determination. During the period the company increased its index linked debt profile by acceding to interest rate swaps originally entered into by Saltaire Water Ltd. These swaps enhance the link between the company's debt and revenue profile and significantly benefit cash flow.

The taxation charge of £26.3m (2007: £10.4m) includes a current tax charge of £27.7m (2007: £27.8m) and a £1.4m credit (2007: £17.4m) for deferred tax. The previous period benefited from a £16.3m credit reflecting the future effect of the change in tax rate from 30% to 28% effective from 1 April 2008. The effective tax rate is 24.0% (2007: 9.9%) of which 25.3% (2007: 26.6%) relates to current taxation.

Dividend payments of £275.0m for the period to 30 September 2008 include a special dividend of £180.1m and an interim dividend of £94.9m. No final dividend was paid in respect of 2007/08 compared with £82.9m paid in 2007 in respect of 2006/07.

OPERATIONAL PERFORMANCE

In August we submitted our draft business plan to Ofwat for the period 2010 to 2015. We plan to invest £1.9bn in the Yorkshire region to address our customers' highest priorities. These include maintaining high standards of service and water quality, reducing the number of properties affected by sewer flooding, improving the security of drinking water supplies, minimising pollution incidents and improving rivers and beaches. The plan strikes a balanced approach between customer prices, service, the environment and investor returns.

A recent report issued by the Consumer Council for Water (CCWater) confirmed that Yorkshire Water continued to receive the lowest number of complaints of any water and sewerage company in 2007/08, despite an overall 11% increase across the industry. It also recognised the success of the new billing system which was introduced without disruption to customers.

Despite the challenges arising from exceptional rainfall and flooding in the region, the company has been ranked third in Ofwat's overall performance assessment (OPA) for 2007/08. We have now remained consistently in the top four water and sewerage companies since 2001. We continue to lead the industry in a number of areas; for the 8th year running we had the lowest percentage of properties with low pressure. We also had the lowest number of unplanned interruptions to supply over 6 hours and the lowest number of serious waste water pollution incidents. We also beat the leakage target again.

Ofwat has upgraded its serviceability assessment of our waste water treatment works reflecting significant improvements achieved due to the success of our action plan and investment to address performance issues.

Following the flooding experienced in the summer of 2007 we have continued to reinstate damaged assets and have worked together with other agencies to manage the risk of future flooding and develop measures to address the risk.

PRINCIPAL RISKS AND UNCERTAINTIES

The company's risk management process aims to be comprehensive, systematic and continuous and based on constant monitoring of business risk. The board is also responsible for the company's internal control and for reviewing its effectiveness.

The company's principal risks and uncertainties include changes to the regulatory environment, changes in legislation, climatic changes, social influences and supplier markets. Final business plans for the next 5 year period will be submitted in April 2009, with draft determinations published by Ofwat in July 2009 and final determinations in November 2009. New price limits will take effect in April 2010.

Further detail on the risks and uncertainties is included in the Annual Report and Accounts for the year ended 31 March 2008.

Profit and loss account

for the 6 months ended 30 September 2008

| | | Unaudited 6 months ended 30 Sep 2008 | 30 Sep 2007 | Audited Year ended 31 Mar 2008 |
|--|------|--|-------------|--------------------------------------|
| | Note | £m | £m | £m |
| Turnover | | 425.0 | 396.9 | 795.5 |
| Operating costs | | (232.8) | (217.4) | (446.3) |
| Exceptional operating costs | | - | - | (7.0) |
| Operating profit | | 192.2 | 179.5 | 342.2 |
| Exceptional profit on disposal of fixed assets | | - | - | 17.5 |
| Profit on ordinary activities before interest | | 192.2 | 179.5 | 359.7 |
| Net interest payable | | (82.7) | (74.9) | (144.6) |
| Profit before taxation | | 109.5 | 104.6 | 215.1 |
| Tax on profit on ordinary activities | 2 | (26.3) | (10.4) | (42.2) |
| Profit for the year | | 83.2 | 94.2 | 172.9 |

All of the above results relate to continuing activities.

Exceptional operating costs in the year ended 31 March 2008 related to restructuring costs (£4.7m) and termination of long term incentive plan arrangements (£2.3m) and the exceptional profit on sale of fixed assets related to insurance proceeds received in respect of assets damaged by the 2007 floods.

Statement of total recognised gains and losses

There are no recognised gains and losses other than those included in the profit and loss account.

There is no difference between the profit before taxation and the profit for the year stated above and their historical cost equivalents.

Balance sheet

At 30 September 2008

| | Note | Unaudited At 30 Sep 2008 £m | 2007 £m | Audited At 31 Mar 2008 £m |
|--|------|--------------------------------------|------------------|------------------------------------|
| Fixed assets | | | | |
| Intangible assets | | 9.9 | 10.8 | 10.4 |
| Tangible assets | | 4,083.6 | 3,956.1 | 4,023.2 |
| Investments | | 16.7 | 16.7 | 16.7 |
| | | 4,110.2 | 3,983.6 | 4,050.3 |
| Current assets | | | | |
| Stock | | 1.0 | 0.6 | 0.7 |
| Debtors | | 487.6 | 159.9 | 140.8 |
| Cash and short term deposits | | 32.1 | - | - |
| | | 520.7 | 160.5 | 141.5 |
| Creditors: amounts falling due within one year | | | | |
| Short term borrowings | | (32.3) | (144.3) | (174.5) |
| Other creditors | | (296.0) | (380.7) | (300.3) |
| | | (328.3) | (525.0) | (474.8) |
| Net current assets (liabilities) | | 192.4 | (364.5) | (333.3) |
| Total assets less current liabilities | | 4,302.6 | 3,619.1 | 3,717.0 |
| Creditors: amounts falling due after more than one year | | | | |
| Loans and other borrowings | | (1,219.6) | (752.7) | (752.0) |
| Other creditors | | (1,764.3) | (1,717.9) | (1,760.8) |
| | | (2,983.9) | (2,470.6) | (2,512.8) |
| Provisions for liabilities and charges | | (497.3) | (184.9) | (191.2) |
| Net assets | | 821.4 | 963.6 | 1,013.0 |
| Capital and reserves | | | | |
| Called up share capital | 4 | 775.0 | 775.0 | 775.0 |
| Profit and loss account | 4 | 43.5 | 185.8 | 235.3 |
| Share-based payment reserve | 4 | 2.9 | 2.8 | 2.7 |
| Total shareholder's funds | 4 | 821.4 | 963.6 | 1,013.0 |

Cash flow statement

for the 6 months ended 30 September 2008

| | Note | Unaudited Six months ended 30 Sep 2008 £m | 30 Sep 2007 £m | Audited Year ended 31 Mar 2008 £m |
|--|------|--|-------------------|--|
| Net cash inflow from operating activities | 5 | 280.1 | 278.8 | 519.2 |
| Returns on investments and servicing of finance | | | | |
| Interest received | | 29.3 | 1.7 | 2.8 |
| Interest paid | | (61.5) | (57.9) | (99.7) |
| Interest element of finance lease rentals | | (21.8) | (15.3) | (22.1) |
| Net cash outflow from returns on investments and servicing of finance | | (54.0) | (71.5) | (119.0) |
| Taxation | | | | |
| Tax paid | | (28.8) | (44.9) | (74.2) |
| Capital expenditure and financial investment | | | | |
| Gross cost of purchase of fixed assets | | (161.7) | (201.7) | (387.0) |
| Receipt of grants and contributions | | 8.4 | 9.8 | 13.9 |
| Disposal of fixed assets | | 0.7 | 1.7 | 45.1 |
| Net cash outflow for investing activities | | (152.6) | (190.2) | (328.0) |
| Equity dividends paid | | (275.0) | (82.9) | (112.1) |
| Net cash outflow before management of liquid resources and financing | | (230.3) | (110.7) | (114.1) |
| Financing | | | | |
| New leasing finance | | - | - | 70.0 |
| Capital element of finance lease rentals | 7 | (3.3) | (2.2) | (60.8) |
| New bank loans | 7 | 446.1 | 704.9 | 730.9 |
| Repayment of bank loans | 7 | (176.2) | (594.5) | (627.9) |
| Net cash inflow from financing | | 266.6 | 108.2 | 112.2 |
| Increase/(decrease) in cash and cash equivalents | 7 | 36.3 | (2.5) | (1.9) |

Notes to the half-yearly financial information

The financial information for the year ended 31 March 2008 does not constitute the company's statutory accounts for that period but has been extracted from the statutory accounts which were prepared in accordance with UK GAAP and filed with the Registrar of Companies. The auditors' report on those accounts was unqualified and did not contain any statement under section 237 (2) or (3) of the Companies Act 1985. The financial information for the half year ended 30 September 2008 and the equivalent period in 2007 has not been audited.

The half-yearly financial information was approved for issue by the board of directors on 18 November 2008.

1. Basis of preparation

The financial information for the 6 month period ended 30 September 2008 has been prepared in accordance with UK GAAP and in accordance with pronouncements on interim reporting issued by the ASB. The accounting policies, methods of computation and presentation are consistent with those of the annual financial statements for the year ended 31 March 2008, as described in those annual financial statements. The half-yearly financial report should be read in conjunction with these annual financial statements.

No new standards, amendments or interpretations which will have a material impact on the financial statements have been adopted in the period.

2. Taxation

| | Unaudited Six months ended | | Audited Year ended |
|--------------|-------------------------------|-------------|-----------------------|
| | 30 Sep 2008 | 30 Sep 2007 | 31 Mar 2008 |
| | £m | £m | £m |
| Current tax | 27.7 | 27.8 | 53.0 |
| Deferred tax | (1.4) | (17.4) | (10.8) |
| | 26.3 | 10.4 | 42.2 |

The current tax expense comprises corporation tax calculated at the estimated effective tax rates for the year.

Deferred tax for the 6 months to 30 September 2007 includes a credit of £16.3m reflecting the future effect of the change in the rate of corporation tax from 30% to 28% from 1 April 2008 onwards.

3. Dividends

| | Unaudited Six months ended | | Audited Year ended |
|--------------------------------|-------------------------------|-------------|-----------------------|
| | 30 Sep 2008 | 30 Sep 2007 | 31 Mar 2008 |
| | £m | £m | £m |
| Prior year final dividend paid | - | 82.9 | 82.9 |
| Interim dividend paid | 94.9 | - | 29.2 |
| Special dividend paid | 180.1 | - | - |
| | 275.0 | 82.9 | 112.1 |

4. Movement in shareholder's funds

| | Unaudited 6 months ended | | | | Audited Year ended | |
|--|-----------------------------|-------------------------------------|---|--------------|-----------------------|----------------|
| | 30 Sep 2008 | | | | 30 Sep 2007 | 31 Mar 2008 |
| | Share capital £m | Profit and loss reserve £m | Share- based payment reserve £m | Total £m | Total £m | Total £m |
| At 1 April 2008 | 775.0 | 235.3 | 2.7 | 1,013.0 | 952.0 | 952.0 |
| Profit for the year | - | 83.2 | - | 83.2 | 94.2 | 172.9 |
| Dividends paid | - | (275.0) | - | (275.0) | (82.9) | (112.1) |
| Share based payments amount due to parent | - | - | 0.2 | 0.2 | 0.7 | 1.2 |
| Other | - | - | - | - | (0.4) | (1.0) |
| Shareholder's funds at end of period | 775.0 | 43.5 | 2.9 | 821.4 | 963.6 | 1,013.0 |

5. Reconciliation of operating profit to net cashflow from operating activities

| | Unaudited | | Audited |
|--|------------------|-------------|-------------|
| | Six months ended | | Year ended |
| | 30 Sep 2008 | 30 Sep 2007 | 31 Mar 2008 |
| | £m | £m | £m |
| Operating profit | 192.2 | 179.5 | 359.7 |
| Depreciation (net of amortisation of grants and contributions) | 88.5 | 86.8 | 180.3 |
| Profit on disposal of fixed assets | (0.4) | (6.3) | (10.2) |
| Profit on disposal of fixed assets- exceptional | - | - | (17.5) |
| Net movement in provisions | 308.9 | - | (0.3) |
| Non-cash movement in loan to Saltaire Water Ltd | (308.9) | - | - |
| | 280.3 | 260.0 | 512.0 |
| Working capital | | | |
| Increase in stocks | (0.3) | - | (0.2) |
| Increase in debtors | (34.0) | (21.2) | (4.7) |
| Increase in creditors | 34.1 | 40.0 | 12.1 |
| | (0.2) | 18.8 | 7.2 |
| Net cash inflow for operating activities | 280.1 | 278.8 | 519.2 |

6. Reconciliation of movement in cash to movement in net debt

| | Note | Unaudited Six months ended 30 Sep 2008 £m | Unaudited 30 Sep 2007 £m | Audited Year ended 31 Mar 2008 £m |
|--|------|--|--------------------------------|--|
| Increase/(decrease) in cash and cash equivalents in the period | 7 | 36.3 | (2.5) | (1.9) |
| Cash inflow from increase in debt and leasing finance | 7 | (266.6) | (108.2) | (112.2) |
| Non-cash loan to Saltaire Water Ltd | 7 | 308.9 | - | - |
| Indexation on index linked loans | 7 | (58.1) | (31.5) | (37.8) |
| Movement in net debt in the period | | 20.5 | (142.2) | (151.9) |
| Net debt at the beginning of the period | 7 | (2,563.9) | (2,412.0) | (2,412.0) |
| Net debt at the end of the period | 7 | (2,543.4) | (2,554.2) | (2,563.9) |

7. Reconciliation of movement in net debt

| | Audited At 31 Mar 2008 £m | Cash flow £m | Unaudited Non- cash Movements £m | Unaudited At 30 Sep 2008 £m | Unaudited At 30 Sep 2007 £m |
|--|------------------------------------|--------------------|---|--------------------------------------|--------------------------------------|
| Cash at bank and in hand | - | 21.1 | - | 21.1 | - |
| Bank overdraft | (4.2) | 4.2 | - | - | (4.8) |
| Short term deposits | - | 11.0 | - | 11.0 | - |
| Cash and cash equivalents | (4.2) | 36.3 | - | 32.1 | (4.8) |
| Loans due within one year | (164.5) | 138.1 | - | (26.4) | (133.4) |
| Finance leases due within one year | (5.8) | (0.1) | - | (5.9) | (6.1) |
| Loans due after one year | (356.4) | (432.1) | - | (788.5) | (368.8) |
| Finance leases due after one year | (395.6) | 3.5 | - | (392.1) | (383.9) |
| Index linked swaps | - | - | (39.0) | (39.0) | - |
| External net debt | (926.5) | (254.3) | (39.0) | (1,219.8) | (897.0) |
| Amounts owed to immediate parent company | (464.0) | 464.0 | - | - | (490.0) |
| Amounts owed to subsidiary company | (1,173.4) | (440.0) | (19.1) | (1,632.5) | (1,167.2) |
| | (2,563.9) | (230.3) | (58.1) | (2,852.3) | (2,554.2) |
| Amounts owed by Saltaire Water Ltd | - | - | 308.9 | 308.9 | - |
| Total net debt | (2,563.9) | (230.3) | 250.8 | (2,543.4) | (2,554.2) |

The non-cash movements of £39.0m relating to index linked swaps and £19.1m relating to amounts owed to the subsidiary company, Yorkshire Water Services Finance plc ("YWSF"), relate to an increase in net debt as a result of indexation and amortisation of issue costs. The £308.9m loan to Saltaire Water Ltd represents the fair value of interest rate swaps transferred to Yorkshire Water.

Bonds of £440.0m borrowed by Kelda and on-lent to Yorkshire Water were transferred to YWSF, £200m of which is repayable in 2010 and the remainder in 2031. The existing borrowings with YWSF are repayable on dates ranging from 2023 to 2058.

Loans due after one year totalling £788.5m include drawings under new committed facilities totalling £446.1m which expire between 26 November 2010 and 26 November 2012. Undrawn amounts under these committed facilities at 30 September 2008 amount to £455m. Also included are EIB loans repayable on dates ranging from 2012 to 2021. Finance leases due after more than one year are repayable on dates up to 2043.