United Utilities Group PLC
24 May 2018

FULL YEAR RESULTS FOR THE YEAR ENDED 31 MARCH 2018

Putting customers first

- Customers benefiting from better service, greater resilience and improved efficiency
- Delivering value through greater use of innovation and advanced technology alongside our £3.8bn AMP6 capital investment programme
- Sharing outperformance through additional investment in resilience increased from £100m to £250m
- Leading customer satisfaction scores achieved
- Supporting more than 50,000 customers in need of help through our Priority Services scheme

Strong operational performance enables improved AMP6 guidance

- Industry leading environmental and water quality performance scores achieved
- Confident of delivering totex outperformance of £100m against our AMP6 allowance
- Expect cumulative AMP6 ODI reward

Preparing well for AMP7 and beyond

- Advanced in our PR19 plans informed by extensive engagement with customers, balancing investment with affordability
- Leading performer giving us confidence heading into AMP7 and beyond

Strong financial performance

- Underlying operating profit of £645.1m (reported operating profit of £636.4m)
- Dividend in line with AMP6 growth policy
- Robust capital structure, leading pensions position and consistently responsible gearing

Key financials

	Year ended	
Continuing operations	31 March 2018	31 March 2017
Revenue	£1,735.8m	£1,704.0m
Reported operating profit	£636.4m	£605.5m
Underlying operating profit[1]	£645.1m	£622.9m
Reported profit after tax	£354.6m	£433.9m
Underlying profit after tax[1]	£304.9m	£313.4m
Total dividend per ordinary share (pence)	39.73p	38.87p
Net regulatory capital spend	£816.1m	£803.7m
RCV gearing[2]	61%	61%

[1] Underlying profit measures have been provided to give a more representative view of business performance and are defined in the underlying profit measure tables on pages 16 and 17
[2] Regulatory capital value (RCV) gearing calculated as group net debt/United Utilities Water's shadow RCV (outturn prices)

Steve Mogford, Chief Executive Officer, said:

"We continue to put customers first. Our approach to vulnerability and affordability is setting new benchmarks for the industry and our sustained improvement in customer satisfaction positions us as a leader in the sector. This year, we achieved our best ever scores against Ofwat's qualitative Service Incentive Mechanism (SIM), positioning us first in the industry in the final survey of the year. Our best practice in this area has received external recognition through several awards, many of which look beyond the water sector.

"Our approach to innovation and Systems Thinking is radically changing the way we operate and leading the way for the industry. We are using advanced technology from around the world and across different sectors to deliver better service, greater resilience and improved efficiency. This is contributing to outperformance in the current regulatory period which we are sharing with customers in the form of £250 million of additional investment in resilience projects.

"The significant progress we have made positions us well as we look towards the next regulatory period and gives us confidence that we can rise to the longer-term challenges resulting from a growing population, affordability concerns and the impact of more volatile weather. We will build on the trust our customers place in us to provide an outstanding service, invest wisely and efficiently, driving further innovation and creating value for all our stakeholders."

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A presentation to investors and analysts starts at 9.00am on Thursday 24 May 2018, at the Auditorium, Deutsche Bank, Winchester House, 1 Great Winchester Street, London, EC2N 2DB.

The presentation can be accessed via a live webcast facility at the following link:
https://edge.media-server.com/m6/p/gbgheg6d

The presentation can be accessed via a live listen only call facility by dialling:
UK toll: +44 (0) 2071 928 016 / UK toll free: +44 (0) 800 376 6220
Passcode: 2249170

The webcast will be available on demand from Friday 25 May 2018 at the following link:
https://www.unitedutilities.com/corporate/investors/financial-news/latest-financial-news/

This results announcement and the associated presentation will be available on the day at:
http://corporate.unitedutilities.com/investors.aspx

KEY OPERATIONAL PROGRESS

Our use of data and technology and our innovative Systems Thinking approach is setting new benchmarks for the sector. This is delivering continued levels of enhanced service and resilience and sustainable improvements in efficiency.

- **Sustained improvements in customer satisfaction** – achieved our best ever scores against Ofwat's qualitative Service Incentive Mechanism (SIM), positioning us first in the final wave and achieving an upper quartile position for the year overall. This performance is mirrored across other customer satisfaction metrics including an upper quartile performance and the most improved company for the utilities sector in the UK Customer Satisfaction Index and the leading listed water company against the Consumer Council for Water's customer satisfaction research. In January, we hosted the first ever North West Affordability summit, engaging with customers and key stakeholders with an interest in this topic and building on our already leading position on affordability and vulnerability.

- **Innovation through Systems Thinking** – through Systems Thinking, we have invested in the technology and infrastructure to allow us to capture huge volumes of data from our assets and the surrounding catchment. This allows us to focus on the interactions of the constituents of the system on a much larger scale, understanding the part our assets play within a catchment and the impact of other factors such as the weather, and to monitor and control the system centrally from our Integrated Control Centre. This allows us to take a much more informed and proactive approach to operations and is delivering enhanced levels of service and resilience along with sustainable improvements in efficiency. This radically different approach is on track to deliver £100 million of totex savings in the current regulatory period.

- **Efficient delivery of investment plan** – driving efficiency into the delivery of our investment programme for the 2015-20 regulatory period through changes to our delivery model, harnessing innovation and embracing the digital world. This has provided customer service, operational and environmental benefits and optimised performance under our ODIs. This significant change in approach has delivered efficiency savings contributing to regulatory outperformance whilst also maintaining highly effective capital delivery as reflected in our Time: Cost: Quality index (TCQi) score which remains high at over 90 per cent.

- **Leading performance with integrity** – in July, we retained Industry Leading Company status, as measured through the Environment Agency's (EA) annual assessment and achieved frontier performance for the sector with the lowest number of pollution incidents alongside our best-in-sector level of self-reporting. Our drinking water quality has improved and is the best it has ever been and we are leading the industry in our approach to resilience.

- **Delivering shareholder value through regulatory outperformance** – the low cost of debt we have already locked-in places us in a strong position to substantially outperform the industry allowed cost. The efficient delivery of our investment plan and our approach to innovation and Systems Thinking also gives us confidence in delivering totex outperformance of £100 million against our AMP6 allowance.

- **Sharing outperformance** – sharing net outperformance through additional investment increased from £100 million to £250 million. This is delivering industry leading, long-term resilience for the benefit of customers and helping to mitigate future bill increases.

- **Strong environmental, social and governance (ESG) credentials** – we have retained a World Class rating in the Dow Jones Sustainability Index for the tenth consecutive year, a very good achievement in light of the ever evolving standards. In addition, our best practice in the areas of affordability and vulnerability has received external recognition through several awards, many of which look beyond the water sector.

- **Preparations for AMP7 and beyond** – we approach AMP7 as a strong, high performing and responsible company in which customers can have trust and confidence. We are on track to submit our PR19 business plan in September 2018, informed by extensive engagement with customers regarding their needs and priorities, and this will set out how we intend to build on our already leading position. We are planning and preparing for the long-term challenges through our new 25-year Water Resources Management Plan. Through this, we will ensure that we remain resilient in the face of increasingly extreme weather and prepare to support a growing population in the North West.

FINANCIAL OVERVIEW

The group has delivered a strong set of financial results for the year ended 31 March 2018.

- **Revenue** – was up £32 million, at £1,736 million, reflecting our allowed regulatory revenue changes partly offset by the accounting impact of our Water Plus JV, which completed on 1 June 2016 and other regulatory adjustments as discussed in more detail on page 10.
- **Operating profit** – underlying operating profit was up £22 million, at £645 million. This reflects our allowed regulatory revenue changes and lower total costs partly offset by an increase in depreciation and amortisation and the accounting impact of our Water Plus JV. Reported operating profit was £636 million, up £31 million reflecting the movements in underlying operating profit and reduced profits last year due to costs associated with preparing the business for open competition in the business retail sector and other restructuring costs.
- **Capex** – total regulatory capital investment in the year, including £147 million of infrastructure renewals expenditure, was £816 million. As announced today, we are sharing our net outperformance by increasing the additional investment available over the remainder of the 2015-20 regulatory period to improve resilience for customers from £100 million to £250 million. This takes our five-year regulatory capex programme to c£3.8 billion. In addition, we expect to invest up to £100 million in non-regulated projects, subject to acceptable returns. In the first three years of the 2015-20 regulatory period we have invested £59 million in non-regulated projects, primarily in solar power.
- **Profit before tax** – underlying profit before tax was down £19 million to £370 million, as the increase in underlying operating profit was more than offset by a £40 million increase in the underlying net finance expense. The increase in the underlying net finance expense is mainly due to the impact of higher RPI inflation on our index-linked debt. Reported profit before tax was £432 million, reflecting fair value movements and other adjusting items as outlined in the underlying profit measures table on page 16.
- **Profit after tax** – underlying profit after tax was down by £8 million to £305 million. Reported profit after tax was £50 million higher at £355 million, reflecting the adjusting items as outlined in the underlying profit measures table on page 16.
- **Capital structure** – the group has a robust capital structure with gearing of 61 per cent as at 31 March 2018 (measured as group net debt to 'shadow' regulatory capital value). Our shadow RCV adjusts for actual spend and was £11.2 billion as at 31 March 2018. This gearing level is comfortably within our target range, of 55 per cent to 65 per cent, supporting a solid investment grade credit rating. United Utilities Water Limited (UUW) has long-term credit ratings of A3 from Moody's and A- from Standard & Poor's, both on stable outlook.
- **Financing headroom** – the group benefits from headroom to cover its projected needs into 2020, enhanced by new finance raised in the period. This headroom provides good flexibility in terms of when and how further debt finance is raised to help refinance maturing debt and support the delivery of our regulatory capital investment programme.
- **Water Plus JV** – during the year, our Water Plus joint venture with Severn Trent has experienced an increase in its working capital arising from data and billing issues following market opening. As a consequence loans owed to the group by Water Plus have increased by £17 million to £136 million.
- **Dividend** – the board has proposed a final dividend of 26.49 pence per ordinary share (taking the total dividend for 2017/18 to 39.73 pence), an increase of 2.2 per cent, in line with our policy of targeting an annual growth rate of at least RPI inflation through to 2020.

OUTLOOK

Our use of data and technology and our innovative Systems Thinking approach is helping deliver our leading operational performance and is supported by a robust financing position. We are outperforming the regulatory contract for the 2015-20 regulatory period allowing us to fund additional investment for the benefit of customers. We have plans in place to improve yet further giving us confidence heading into AMP7 and beyond and deliver long-term value for customers, the environment and for shareholders.

OPERATIONAL PERFORMANCE

United Utilities aims to deliver long-term shareholder value by providing:

- The best service to customers;
- At the lowest sustainable cost;
- In a responsible manner.

Our operational performance is presented under each of these strategic themes.

Best service to customers

Customer service – sitting at the core of everything we do, our strong focus on customer service has helped us deliver substantial improvements in recent years, becoming the most improved company in the 2010-15 regulatory period with a reduction of around 75 per cent in the overall number of customer complaints.

This year, we have seen another step change in our customer satisfaction performance. We achieved our highest ever scores against Ofwat's qualitative Service Incentive Mechanism (SIM) measure, finishing first in the final survey of the year and third for the year overall. This performance is mirrored in the number of complaints that we receive. These have reduced by over 34 per cent in two years and the number of repeat complaints have reduced by 63 per cent over the same period.

We have added to our already leading position on affordability and vulnerability. We are now supporting more than 50,000 customers in need of help through our Priority Services scheme, providing more targeted support for customers experiencing short or long-term personal or financial difficulties in their lives, with tailored assistance. In January we hosted the first ever North West Affordability summit, engaging with customers and key stakeholders with an interest in this topic.

We have an industry leading digital capability informed by customers with more than 750,000 customers now registered for our online customer portal, My Account, and we have launched the sector's first truly integrated mobile app allowing customers to complete a variety of interactions with us using their preferred channel.

Improving customer service will continue to be a key area of focus, and we have identified a range of opportunities to deliver further benefits for customers.

Leading North West service provider – we are consistently ranked third out of ten leading organisations in the North West, through an independent brand tracker survey which is undertaken quarterly. This covers key attributes such as reputation, trustworthiness and customer service. We are behind only Marks & Spencer and John Lewis, and ahead of seven other major organisations covering utilities, telecoms, media and banking services.

Robust water supply – our customers benefit from our robust water supply and demand balance, along with high levels of water supply reliability. Our overall water quality continues to be good, and although our water quality service index has slightly deteriorated compared with the prior year, it remains above our historical average and we have plans in place to deliver improved performance going forward. We have consistently delivered a reliable water service, although we have experienced some water no-supply incidents in the 2015-20 regulatory period. Whilst this is disappointing, our Systems Thinking approach is helping us to respond to these events and avoid them in future.

Reducing sewer flooding – we have continued to invest heavily in schemes, projects and programmes of work designed to reduce the risk of flooding of our customers' homes, including incidence based targeting on areas more likely to experience flooding and defect identification through CCTV sewer surveys and other innovative technologies. Our plan for the 2015-20 regulatory period includes a target of reducing sewer flooding incidents by over 40 per cent, in line with customers' affordability preferences, and we are making good progress. We have achieved our best ever five-year performance on our repeat flooding and internal operational flooding measures. Our wastewater network will continue to benefit from significant investment going forward and we will continue to seek to work in collaboration with other external lead flood authorities and associated partners to address the widespread flooding events that hit our region, as we aim to help mitigate changing weather patterns likely to result from climate change.

Key performance indicators:

- **Outcome delivery incentives (ODIs)** – we have 19 wholesale financial ODIs and as was supported by customers, the risk is skewed to the downside with only ten providing the potential to earn a reward in the 2015-20 regulatory period.

  Our performance for 2017/18 has resulted in a £7.0 million net penalty. Overall, performance was again good against our wastewater measures but we recognise that there are still areas in which we can improve against our water measures, and we are committed to achieving this.

  We are pleased with our cumulative performance over the first three years of the current regulatory period resulting in a net reward of £2.2 million, exceeding our initial expectations. Whilst a number of our ODI measures are susceptible to one-off events and, on the whole, our ODI targets get tougher each year, our strong performance to date coupled with continued targeted investment alongside our Systems Thinking and innovative approach to the way we operate, gives us confidence that we will achieve a cumulative net ODI outcome over the 2015-20 regulatory period in positive reward territory.

  Our main areas of reward to date have come through our performance in the areas of private sewers, pollution and leakage, with our main penalty being on reliable water service and water quality service.

- **Service incentive mechanism (SIM)** – we have previously stated our target was to move towards the upper quartile in the medium-term, and we are particularly pleased with the progress we have made this year, ending the year as a leading company in our peer group.

  Qualitative: Ofwat has undertaken the four surveys for 2017/18 and United Utilities has improved its score to 4.49 points, compared with 4.42 points in 2016/17, putting us in third position for the year out of the 18 water companies, and also third position out of the 10 companies providing both water and wastewater services. We ended the year with our highest ever score of 4.61 in wave 4, which placed us in first position in this wave for the sector overall. In particular, customers scored us highly for our billing and wastewater services.

  Quantitative: the quantitative assessment measures customer contacts and performance is assessed on both an absolute and relative basis. Whilst relative performance can only be assessed in full following the end of each financial year when the other companies publish their respective results, on absolute performance for 2017/18, our score of 71 points represents a marked improvement on our 2016/17 score of 77 points. For the first nine months of the year, of the companies that share data on quantitative SIM, we were first of the seven water and wastewater companies and fourth of the 11 water companies.

<u>**Lowest sustainable cost**</u>

Power and chemicals – our asset optimisation programme continues to provide the benefits of increased and more effective use of operational site management to optimise power and chemical use and the development of more combined heat and power assets to generate renewable energy. In addition to the electricity we generate from bioresources, we are developing other renewable energy facilities. This is primarily in the area of solar, where we have invested £53 million in the first three years of the 2015-20 regulatory period and contributing towards our expected investment of up to £100 million across the five-year period. We have also substantially locked-in our power commodity costs across 2015-20, providing greater cost certainty for the regulatory period.

Proactive network management – through our Systems Thinking approach we are more proactive in the management of our assets and networks. We have improved our predictive modelling and forecasting through better use of sensors in our network and better analysis of other data, such as weather forecasting, enabling us to address more asset and network problems before they affect customers. This reduces the level of reactive work and improves our performance and efficiency.

Debt collection – our region suffers from high levels of income deprivation and we offer wide-ranging schemes to help customers struggling to pay. We now have over 100,000 customers on affordability schemes, almost double the commitment we made at the start of AMP6. Notwithstanding our industry-leading debt management

processes, deprivation remains the principal driver of our higher than average bad debt and cost to serve and we expect this to continue to be a challenging area for us.

Reflecting our ongoing focus on bad debt through initiatives such as our affordability schemes, our household bad debt expense has reduced to 2.3 per cent of regulated revenue from 2.5 per cent last year.

Pensions – United Utilities has taken progressive steps to de-risk its pension provision. The group had an IFRS retirement benefit surplus of £344 million as at 31 March 2018, compared with a surplus of £248 million as at 31 March 2017. Further details of the group's pension provision are provided in the pensions section on page 15.

From 1 April 2018, the majority of active members in the defined benefit sections of the group's pension schemes transitioned to a hybrid section incorporating both defined benefit and defined contribution elements. The changes have had no impact on the financial statements for the year ended 31 March 2018 as they have only taken effect for pensionable service from 1 April 2018.

Capital delivery and regulatory commitments – we are strongly focused on delivering our commitments efficiently and on time, and have a robust commercial capital delivery framework in place. Across the 2015-20 regulatory period, we are working with a single engineering partner and four design and construction partners to deliver our regulatory capital investment programme of around £3.8 billion. We are involving our partners much earlier in project definition and packaging projects by type, geography and timing in order to deliver efficiencies. Projects are allocated on an incentive or competitive basis leading to our partners presenting a range of solutions, innovations and pricing.

We have accelerated our 2015-20 investment programme in order to improve services for customers and deliver early operational and environmental benefits. Regulatory capital investment in 2017/18, including £147 million of infrastructure renewals expenditure, was £816 million, including additional investment that we have committed to, sharing our overall regulatory outperformance with customers. This, combined with £1.6 billion invested in the first two years of the regulatory period, brings our total spend to around £2.4 billion of our planned £3.8 billion capital investment across the 2015-20 regulatory period.

We are also driving more effective and efficient delivery of our capital programme and applying a tougher measurement mechanism to our Time: Cost: Quality index (TCQi) score for this regulatory period. Despite this tougher approach, our TCQi score remains high at 93 per cent, representing very good performance.

Key performance indicators:

- **Total expenditure (totex) performance** – our totex allowance for the 2015-2020 regulatory period represented a significant challenge compared with the costs we originally submitted as part of our business plan. We have not only closed the gap to our allowance but we are now also confident of outperforming that allowance by £100 million. This has been achieved through a combination of driving efficiency into our capital programme and also through Systems Thinking.

- **Financing outperformance** – the low cost of debt we have already locked-in places United Utilities in a strong position to deliver significant outperformance for the 2015-20 regulatory period compared with the industry allowed cost.

- **Household retail cost to serve** – we continue to deliver against a challenging benchmark set for AMP6. Our target is to minimise our costs compared with our revenue allowance and we have delivered a good performance in 2017/18, outperforming this year's revenue allowance by around £9 million. By 2020, we are forecasting a cost to serve in line with the regulatory cost allowance and we are hopeful that our cost plans will move us towards upper quartile performance in AMP7.

<u>**Responsible manner**</u>

Behaving responsibly is fundamental to the manner in which we undertake our business, and the group has for many years included corporate responsibility factors in its strategic decision making. Our environmental, social and governance performance across a broad front has received external recognition. Earlier in the 2017/18 financial

year, United Utilities retained a World Class rating in the Dow Jones Sustainability Index for the tenth consecutive year, again achieving industry leading performance status in the multi-utility/water sector. Retaining 'World Class' status for this length of time is a significant achievement, particularly as the assessment standards continue to increase and evolve.

Leakage – we have continued our strong operational focus on leakage, alongside our network resilience improvements and a range of initiatives such as active pressure management, satellite technology and the UK's first leakage sniffer dog specially trained to pinpoint the exact location of leaks. This has delivered good performance against our leakage targets in 2017/18. Encouraging our customers to save water through water efficiency programmes not only enables them to help preserve this precious resource but can also save money on their water bill.

Environmental performance – this is a high priority for United Utilities and we were delighted to have retained our Industry Leading Company status in the Environment Agency's latest performance metrics, as described in the KPIs section below. This is a result of our approach to managing our assets in an integrated way and has resulted in reduced environmental incidents. We still don't always get it right and this year we delivered the obligations under our first enforcement undertakings, investing in catchment schemes rather than accepting formal prosecutions.

Carbon footprint – by 2020, we aim to reduce our carbon footprint by 50 per cent compared with a 2005/06 baseline and we are on track to do so. This year our carbon footprint has reduced to 391,640 tonnes of carbon dioxide equivalent, a reduction of one-third since 2005/06, helped by a 4 per cent reduction in electricity use. In addition, we generated more renewable energy than ever before, at 167 gigawatt hours, up 12 per cent on the previous year. This illustrates good progress in the company's energy strategy to use less and generate more renewable energy.

Employees – we continue to work hard to engage all of our employees in the transformation of the group's performance. Employee engagement was at 79 per cent this year, higher than the UK norm. We remain focused on maintaining high levels of employee engagement.

We have been successful in attracting and retaining people and have continued to expand our apprentice and graduate programmes for 2017/18. We now have a total of 55 graduates and 118 apprentices across the business. Our investment in recruiting graduates and apprentices is already benefiting the company with 153 employees securing permanent roles across our business, having previously been on either the graduate or apprentice scheme.

Over the last year, we have continued our sustained focus on health, safety and wellbeing. In this period we retained our Gold award status with the Royal Society for the Prevention of Accidents and our status under the UK workplace wellbeing charter. Our employee accident frequency rate for 2017/18 reduced to 0.101 accidents per 100,000 hours, compared with a rate of 0.196 in 2016/17. For the same period, our contractor accident frequency rate increased slightly to 0.092 per 100,000 hours, compared with a rate of 0.087 in 2016/17. We recognise that there is always more to do, and health, safety and wellbeing will continue to be a significant area of focus as we strive for continuous improvement.

Communities – we continue to support partnerships, both financially and in terms of employee time through volunteering, with other organisations across the North West. Our approach to integrated catchments helps to tackle water quality issues in lakes, rivers and coastal waters across the North West, and our LoveMyBeach contribution includes employees volunteering to help to keep our region's beaches tidy. We continue to support local communities through contributions and schemes such as providing debt advisory services and , our work with Youth Focus North West engages the region's young people, and our future customers, with our business planning process.

Key performance indicators:

- **Leakage** – Although leakage is included within our outcome delivery incentives, we intend to continue publishing our leakage position separately, with it being an important measure from a corporate responsibility perspective. In 2017/18 we have again met our regulatory leakage target of 463 megalitres per day.

- **Environmental performance** – On the Environment Agency's latest annual assessment, published in July 2017, we were awarded Industry Leading Company status across the range of operational metrics for the second year running and were one of only two companies to achieve this status. This aligns with our medium-term goal of being a first quartile company on a consistent basis.

- **Corporate responsibility** – United Utilities has a strong focus on operating in a responsible manner and is the only UK water company to have a World Class rating as measured by the Dow Jones Sustainability Index. In 2017/18, United Utilities retained its World Class rating for the tenth consecutive year.

FINANCIAL PERFORMANCE

United Utilities delivered a strong set of financial results for the year ended 31 March 2018.

Revenue

Revenue was up £32 million, at £1,736 million, reflecting our allowed regulatory revenue changes, partly offset by the impact of our Water Plus JV, which completed on 1 June 2016 and the below regulatory adjustments.

With regard to Ofwat's revenue correction mechanism relating to the 2014/15 financial year, we have around £9 million to return to customers. As we have previously indicated, we have begun to return this to customers with a revenue reduction of around £3 million in 2017/18, with further revenue reductions proposed of around £3 million in both of 2018/19 and 2019/20. This approach has been adopted to help aid a smoother bill profile.

Separately, consistent with Ofwat's annual wholesale revenue forecasting incentive mechanism (WRFIM), revenue has also been reduced in 2017/18 by £10 million as actual volumes in 2015/16 were higher than our original assumptions. We will further be reducing revenues in 2018/19 by £4 million as actual volumes in 2016/17 were also higher than our original assumptions.

Operating profit

Reported operating profit increased by £31 million, to £636 million, reflecting the increase in underlying operating profit, along with a reduction in adjusted items. Adjusted items for 2017/18 amounted to £9 million, £6 million of which related to restructuring costs. Adjusted items in the prior year amounted to £17 million, £10 million of which related to restructuring costs.

Underlying operating profit at £645 million was £22 million higher than last year. This reflects our allowed regulatory revenue changes, partly offset by an expected increase in depreciation and the accounting impact of our Water Plus JV. The JV completed on 1 June 2016 and, from that date, its contribution is no longer included within operating profit and is, instead, included within the share of profits of joint ventures line in the income statement.

Investment income and finance expense

Reported net finance expense of £207 million was higher than the £189 million expense in 2016/17. This £18 million increase principally reflects the increased indexation charge in the year of £57 million which has been partly offset by an increase in the fair value gains on debt and derivative instruments, from a £24 million gain in 2016/17 to a £47 million gain in 2017/18.

The underlying net finance expense of £277 million was £40 million higher than last year, mainly due to the impact of higher RPI inflation on the group's index-linked debt, particularly on the portion of index-linked debt with a three-month lag. Interest on non index-linked debt of £92 million was £17 million lower than last year, due to the lower rates locked in on our interest rate swaps and the re-couponing of a portion of our regulatory swap portfolio. The indexation of the principal on our index-linked debt amounted to a net charge in the income statement of £138 million, compared with a net charge of £81 million last year. As at 31 March 2018, the group had approximately £3.7 billion of index-linked debt at an average real rate of 1.3 per cent.

The higher RPI inflation charge compared with last year contributed to the group's average underlying interest rate of 4.2 per cent being higher than the rate of 3.8 per cent for the year ended 31 March 2017. The average underlying interest rate represents the underlying net finance expense divided by average debt.

The group has fixed the substantial majority of its non index-linked debt for the 2015-20 regulatory period.

Profit before tax

Reported profit before tax was £432 million, £10 million lower than last year due to the increase in operating profit being more than offset by fair value movements, as outlined in the underlying profit measures tables on pages 16 and 17 and the £22 million profit in 2016/17 on disposal of the non-household business.

Underlying profit before tax was £370 million, £19 million lower than last year, primarily reflecting the £22 million increase in underlying operating profit more than offset by the £40 million increase in underlying net finance expense. This underlying measure reflects the adjusting items, as outlined in the operating profit section above, and other items such as fair value movements in respect of debt and derivative instruments, as outlined in the underlying profit measures table on page 16.

Tax

In addition to corporation tax, the group pays significant other contributions to the public finances on its own behalf as well as collecting and paying over further amounts for its 5,000 strong workforce. The total payments for 2017/18 were around £242 million and included business rates, employment taxes, environmental taxes and other regulatory service fees such as water abstraction charges as well as corporation tax.

In 2017/18, we paid corporation tax of £36 million, which represents an effective cash tax rate on underlying profits of 10 per cent, which is 9 per cent lower than the headline rate of corporation tax of 19 per cent. Consistent with prior years, the key reconciling item to the headline rate was allowable tax deductions on capital investment. We have expressed the effective cash tax rate in terms of underlying profits as this measure excludes fair value movements on debt and derivative instruments and thereby enables a medium-term cash tax rate forecast. We would expect the average cash tax rate on underlying profits through to the end of the current regulatory period in March 2020 to be around 12 per cent. The key risk to sustaining this rate is any unexpected changes in tax legislation or practice and, as necessary, we would actively engage with the relevant authorities in order to manage this risk.

The current tax charge was £25 million in 2017/18, compared with £54 million in the previous year; the main differences being timing in nature with a corresponding equal and opposite adjustment to deferred tax. There were current tax credits of £7 million in 2017/18 and £23 million in 2016/17, following agreement of prior years' tax matters; in addition to UK tax, the prior year figure also included the release of a provision in relation to agreed historic overseas tax matters.

For 2017/18, the group recognised a deferred tax charge of £52 million, compared with a charge of £28 million for 2016/17. In addition, the group recognised a deferred tax charge of £7 million in both 2016/17 and 2017/18 relating to prior years' tax matters. In 2016/17, the group also recognised a deferred tax credit of £58 million relating to the enacted reduction in the headline rate of corporation tax from 18 per cent to 17 per cent from 1 April 2020.

The total tax charge for 2017/18 was £78 million as compared to a total tax charge of £9 million for 2016/17, the main differences being the £58 million deferred tax credit relating to changes in tax rates in 2016/17 together with the higher current tax credit in 2016/17 in respect of prior years. For both periods, the total underlying tax effective rate was in line with the headline rate (currently at 19 per cent) and subject to any legislative or tax practice changes, we would expect this to continue for the medium-term.

Profit after tax

Reported profit after tax was £355 million, compared with £434 million in the previous year, due to the £10 million reduction in reported profit before tax and the £69 million higher tax charge as 2016/17 included a deferred tax credit of £58 million relating to changes in the Government's future planned tax rate and a further tax credit of £16 million relating to prior years' tax matters.

Underlying profit after tax of £305 million was £8 million lower than last year, principally reflecting the £19 million decrease in underlying profit before tax partly offset by lower underlying tax on lower profits and the reduction in the headline rate of corporation tax.

Earnings per share

Basic earnings per share decreased from 63.6 pence to 52.0 pence, for the same reasons that decreased profit after tax.

Underlying earnings per share decreased from 46.0 pence to 44.7 pence. This underlying measure is derived from underlying profit after tax which decreased by £8 million.

Dividend per share

The board has proposed a final dividend of 26.49 pence per ordinary share in respect of the year ended 31 March 2018. Taken together with the interim dividend of 13.24 pence per ordinary share, paid in February, this produces a total dividend per ordinary share for 2017/18 of 39.73 pence. This is an increase of 2.2 per cent, compared with the dividend relating to last year, in line with the group's dividend policy of targeting a growth rate of at least RPI inflation each year through to 2020. The inflationary increase of 2.2 per cent is based on the RPI element included within the allowed regulated revenue increase for the 2017/18 financial year (i.e. the movement in RPI between November 2015 and November 2016).

The final dividend is expected to be paid on 3 August 2018 to shareholders on the register at the close of business on 22 June 2018. The ex-dividend date is 21 June 2018.

Our dividend policy targets a growth rate of at least RPI inflation each year through to 2020, with further details set out below.

- ***Policy period*** – the dividend policy aligns with the five-year regulatory period which runs from 1 April 2015 to 31 March 2020.

- ***Policy approval process*** – the dividend policy was considered and approved by the United Utilities Group Board in January 2015, as part of a comprehensive review of the 2015-20 regulatory final determination in the context of a detailed business planning process, with due regard for the group's financial metrics, credit ratings and long-term financial stability, and is reviewed at least annually.

- ***Distributable reserves*** – as at 31 March 2018, the company had distributable reserves of £3,163 million. The total external dividends relating to the 2017/18 financial year amounted to £271 million. The company distributable reserves support over 11 times this annual dividend.

- ***Financing headroom*** – supporting the group's cash flow, United Utilities adopts a funding/liquidity headroom policy of having available resources to cover the next 15-24 months of projected cash outflows on a rolling basis.

- ***Cash flows from subsidiaries*** – the directors consider that the group's principal operating subsidiary, United Utilities Water Limited, has sufficient resources to pay dividends to United Utilities Group PLC for the duration of the current dividend policy period to support the external payment of dividends to shareholders.

- ***Financial stability*** – the water industry has invested significant capital since privatisation in 1989 to improve services for customers and provide environmental benefits, a large part of which is driven by legislation. Water companies have typically raised borrowings to help fund the capital investment programme. Part of total expenditure is additive to the regulatory capital value, or RCV, on which water companies earn a return allowed by the economic regulator, Ofwat. RCV gearing is useful in assessing a company's financial stability in the UK water industry and is one of the key credit metrics that the credit rating agencies focus on. United Utilities has had a relatively stable RCV gearing level over the last seven years, always comfortably within its target range of 55 per cent to 65 per cent, supporting a solid A3 credit rating for UUW with Moody's. RCV gearing at 31 March 2018 was 61 per cent and the movement in net debt is outlined in the cash flow section below.

- ***Dividend sustainability*** – in approving the policy, the board is satisfied that across the current regulatory period, the projected dividend is adequately covered by underlying profit after tax. Separately, the executive directors' long-term remuneration plan is directly linked to a measure of sustainable dividends. Whilst specific targets are not disclosed in advance, for commercial sensitivity reasons, there is a major focus on the creation of strong earnings that ensure the sustainability of dividends.

- ***Viability statement*** – the dividend policy is underpinned by the group's long-term viability statement (contained within the group's annual report and financial statements). Assurance supporting this statement is provided by the review of: the group's key financial measures; the key credit financial metrics; the group's liquidity position; the contingent liabilities of the group; and the key risks of the group together with the associated mitigating actions.

- ***Annual dividend approval process*** – the group places significant emphasis on strong corporate governance, and before declaring interim and proposing final dividends, the United Utilities Group board undertakes a comprehensive assessment of the group's key financial metrics.

- ***Policy sustainability***

  2015-20

  - the policy is considered by the board to be robust to reasonable changes in assumptions, such as inflation, opex, capex and interest rates;

  - extreme economic, regulatory, political or operational events, which could lead to a significant deterioration in the group's financial metrics during the policy period, may present risks to policy sustainability;

  2020-25

  - a dividend policy for the 2020-25 regulatory period will be formulated after Ofwat announces the outcome of the regulatory price review (currently expected in December 2019).

Cash flow

Net cash generated from continuing operating activities for the year ended 31 March 2018 was £816 million, and therefore broadly consistent with £821 million in the previous year. The group's net capital expenditure was £710 million, principally in the regulated water and wastewater investment programmes. This excludes infrastructure renewals expenditure which is treated as an operating cost under IFRS. Cash flow capex differs from regulatory capex, since regulatory capex includes infrastructure renewals expenditure and is based on capital work done in the period, rather than actual cash spent.

Net debt including derivatives at 31 March 2018 was £6,868 million, compared with £6,579 million at 31 March 2017. This increase reflects regulatory capital expenditure, payments of dividends, interest and tax, the inflationary uplift on index-linked debt and loans to joint ventures, partly offset by operating cash flows.

Fair value of debt

The group's gross borrowings at 31 March 2018 had a carrying value of £7,912 million. The fair value of these borrowings was £9,052 million. This £1,140 million difference principally reflects the significant fall in real interest rates, compared with the rates at the time we raised a portion of the group's index-linked debt. This difference has decreased from £1,218 million at 31 March 2017 due primarily to an increase in credit spreads.

Debt financing and interest rate management

Gearing, measured as group net debt divided by UUW's shadow (adjusted for actual spend) regulatory capital value, was 61 per cent at 31 March 2018. This is the same gearing as at 31 March 2017 and remains comfortably within our target range of 55 per cent to 65 per cent.

UUW has long-term credit ratings of A3/A- and United Utilities PLC (UU PLC) has long-term credit ratings of Baa1/BBB from Moody's Investors Service (Moody's) and Standard & Poor's (S&P) Ratings Services respectively. The split rating for UU PLC reflects differing methodologies used by the credit rating agencies. Both Moody's and S&P have the group's ratings on a stable outlook.

The group has access to the international debt capital markets through its €7 billion euro medium-term note (EMTN) programme. The EMTN programme does not represent a funding commitment, with funding dependent on the successful issue of the notes.

Cash and short-term deposits at 31 March 2018 amounted to £510 million. Over 2015-20 we have financing requirements totalling around £2.5 billion to cover refinancing and incremental debt, supporting our five-year investment programme, and we have now raised over £2.2 billion of this requirement.

In April 2016, UUW signed a £250 million index-linked term loan facility with the European Investment Bank (EIB) to support the delivery of UUW's AMP6 investment programme. In October 2017 the final £75 million was drawn down such that as at 31 March 2018, the full £250 million had been drawn down. This is an amortising facility with an average loan life of 10 years and a final maturity of 18 years from draw down.

In December 2017, UUW's financing subsidiary, United Utilities Water Finance PLC (UUWF), raised around £23 million of term funding, via the issue of €26 million private placement notes, with a 15-year maturity, off our EMTN programme. In January 2018, UUWF raised around £27 million of term funding, via the issue of €30 million private placement notes, with a 15-year maturity, off our EMTN programme. In February 2018, UUWF raised around £68 million of term funding, via the issue of HKD739 million private placement notes, with an 8-year maturity, off our EMTN programme. Also in February 2018, UUWF issued £300 million fixed rate notes in the public bond market, with a 7-year maturity. This was the group's first public bond issue since 2009 and was well received by the market with good investor participation generating an order book in excess of £600 million. Notwithstanding a degree of market volatility at the time of issuance, we were pleased to price the bond at a very satisfactory level.

We remain the sector leader in the issuance of CPI-linked debt having previously raised £165 million, in response to Ofwat's decision to transition away from RPI inflation linkage.

In addition, since September 2017, the group has renewed £100 million of committed bank facilities.

Long-term borrowings are structured or hedged to match assets and earnings, which are largely in sterling, indexed to UK retail price inflation and subject to regulatory price reviews every five years.

Long-term sterling inflation index-linked debt provides a natural hedge to assets and earnings. At 31 March 2018, approximately 54 per cent of the group's net debt was in index-linked form, representing around 33 per cent of UUW's regulatory capital value, with an average real interest rate of 1.3 per cent. The long-term nature of this funding also provides a good match to the company's long-life infrastructure assets and is a key contributor to the group's average term debt maturity profile, which is just under 20 years.

Recognising Ofwat's intention to transition to the use of CPIH as part of its PR19 methodology, the group has undertaken a review of its inflation hedging policy. This review involved a balanced assessment across a range of factors including maintaining an appropriate economic hedge of the RCV and associated cash flows, the availability and costs of hedging instruments, the impact of different hedging strategies on key financial indicators including income statement metrics, along with a consideration of broader sector positioning. Taking account of these factors, along with the intention of the group's defined benefits pension schemes to implement further de-risking by increasing their hedges of RPI inflation with a corresponding reduction/removal of the pension Inflation Funding Mechanism, has resulted in a revised inflation hedging policy whereby the group intends to maintain around half of net debt in index-linked form.

Where nominal debt is raised in a currency other than sterling and/or with a fixed interest rate, the debt is generally swapped to create a floating rate sterling liability for the term of the debt. To manage exposure to medium-term interest rates, the group fixes underlying interest costs on nominal debt out to ten years on a reducing balance basis. Historically, this has been supplemented by fixing substantially all remaining floating rate exposure across the forthcoming regulatory period around the time of the price control determination. In line with this, the group has fixed interest costs for substantially all of its floating rate exposure over the 2015-20 regulatory period, locking in an average annual interest rate of around 3.2 per cent nominal (inclusive of credit spreads).

Recognising Ofwat's intention to apply debt indexation for new debt raised during the 2020-25 regulatory period, we will retain the hedge to fix underlying interest costs on nominal debt out to ten years on a reducing balance basis, but we will no longer supplement this with the additional 'top up' hedge at the start of each new regulatory period.

Liquidity

Short-term liquidity requirements are met from the group's normal operating cash flow and its short-term bank deposits and supported by committed but undrawn credit facilities. The group's €7 billion EMTN programme provides further support.

Available headroom at 31 March 2018 was £435 million based on cash, short-term deposits and committed bank facilities, net of short-term debt as well as committed facilities and term debt falling due within 12 months.

United Utilities believes that it operates a prudent approach to managing banking counterparty risk. Counterparty risk, in relation to both cash deposits and derivatives, is controlled through the use of counterparty credit limits. United Utilities' cash is held in the form of short-term money market deposits with prime commercial banks.

United Utilities operates a bilateral, rather than a syndicated, approach to its core relationship banking facilities. This approach spreads maturities more evenly over a longer time period, thereby reducing refinancing risk and providing the benefit of several renewal points rather than a large single refinancing requirement.

Pensions

As at 31 March 2018, the group had an IAS 19 net pension surplus of £344 million, compared with a net pension surplus of £248 million at 31 March 2017. This £97 million increase mainly reflects the impact of a decrease in credit spreads and the favourable impact of updating mortality assumptions. The scheme specific funding basis does not suffer from volatility due to inflation and credit spread movements as it uses a fixed inflation assumption via a blend of the inflation market hedge and the Inflation Funding Mechanism and a prudent, fixed credit spread assumption. Therefore, any inflation and credit spread movements have not had a material impact on the deficit calculated on a scheme specific funding basis or the level of deficit repair contributions.

Further detail on pensions is provided in note 11 ('Retirement benefit surplus') of these condensed consolidated financial statements.

Underlying profit

The underlying profit measures in the following table represent alternative performance measures (APMs) as defined by the European Securities and Markets Authority (ESMA). These measures are linked to the group's financial performance as reported under International Financial Reporting Standards (IFRSs) as adopted by the European Union in the group's consolidated income statement, which can be found on page 26. As such, they represent non-GAAP measures.

These APMs have been presented in order to provide a more representative view of business performance. The group determines adjusted items in the calculation of its underlying measures against a framework which considers significance by reference to profit before tax, in addition to other qualitative factors such as whether the item is deemed to be within the normal course of business, its assessed frequency of reoccurrence and its volatility which is either outside the control of management and/or not representative of current year performance.

Adjusted item	Rationale
Flooding incidents	Two significant flooding incidents in the year ended 31 March 2016 caused extensive damage to localised parts of our infrastructure, resulting in significant levels of remedial operating expenditure and a large claim under the group's insurance cover. Management's view is that these were significant and infrequent events and, as such, were not part of the normal course of business.
Non-household retail market reform	The group has incurred significant costs since the year ended 31 March 2015 relating to the non-household retail market opening to competition in April 2017. This represents a one-off event and as such, is not considered part of the normal course of business.
Restructuring costs	The group has incurred restructuring costs in the past in relation to a number of discrete events which can cause volatility in the reported results. Management adjusts internally for these costs to provide an underlying view of performance which it views as being more representative of the normal course of business and more comparable period to period.
Net fair value (gains)/losses on debt and derivative instruments	Fair value movements on debt and derivatives can be both very significant and volatile from one period to the next. These movements are determined by macro-economic factors which are outside the control of management and these instruments are purely held for funding and hedging purposes (not for trading purposes). Taking these factors into account, management believe it is useful to adjust for this to provide a more representative view of performance.
Interest on swaps and debt under fair value option	Net fair value losses on debt and derivative instruments includes interest on swaps and debt under fair value option. In adjusting for the former, it is appropriate to add back interest on swaps and debt under fair value option to provide a view of the group's cost of debt which is better aligned to the return on capital it earns through revenue.
Net pension interest (income)/ expense	This item can be very volatile from one period to the next and it is a direct function of the extent to which the pension scheme is in an accounting deficit or surplus position. Management believe it is useful to adjust for this to provide a more representative view of performance which is better aligned to the return on capital it earns through revenue.
Capitalised borrowing costs	Accounting standards allow for the capitalisation of borrowing costs in the cost of qualifying assets. Management believe it is appropriate to adjust for these significant costs to provide a representative cost of borrowings and current year performance which is better aligned to the return on capital it earns through revenue.
Profit on disposal of business	This relates to the disposal of the group's non-household retail business during the year ended 31 March 2017 which represents a significant one-off event and, as such, is not considered part of the normal course of business.
Deferred tax credit-change in tax rate	The deferred tax impact from changes to the corporation tax rate announced by the UK Government represent both significant and volatile impacts which are outside the control of management. Management adjust for this to provide a more representative view of current year performance.
Agreement of prior years' tax matters	The agreement of prior years' tax matters can be significant, volatile and often related to final settlement with tax authorities of numerous prior year periods. Management adjust for this to provide a more representative view of the tax charge/credit in relation to current year performance.
Tax in respect of adjustments to underlying profit before tax	Management adjust for the tax impacts of the above adjusted items to provide a more representative view of current year performance.

Operating profit	**Year ended 31 March 2018**	**Year ended 31 March 2017**
	£m	**£m**
Operating profit per published results	**636.4**	**605.5**
Flooding incidents (net of insurance proceeds)	1.7	1.5
Non-household retail market reform	1.0	5.8
Restructuring costs	6.0	10.1
Underlying operating profit	**645.1**	**622.9**

Net finance expense		
	£m	**£m**
Finance expense	(218.6)	(202.7)
Investment income	12.0	13.7
Net finance expense per published results	**(206.6)**	**(189.0)**
Adjustments:		
Net fair value (gains)/losses on debt and derivative instruments	(47.3)	(24.3)
Interest on swaps and debt under fair value option	23.5	15.4
Net pension interest (income)/expense	(7.1)	(10.2)
Capitalised borrowing costs	(39.7)	(29.2)
Underlying net finance expense	**(277.2)**	**(237.3)**

Profit before taxation		
	£m	**£m**
Share of profits of joint ventures	**2.3**	**3.8**
Profit before taxation per published results	**432.1**	**442.4**
Adjustments:		
Flooding incidents	1.7	1.5
Business retail market reform	1.0	5.8
Restructuring costs	6.0	10.1
Net fair value (gains)/losses on debt and derivative instruments	(47.3)	(24.3)
Interest on swaps and debt under fair value option	23.5	15.4
Net pension interest (income)/expense	(7.1)	(10.2)
Capitalised borrowing costs	(39.7)	(29.2)
Profit on disposal of business	-	(22.1)
Underlying profit before taxation	**370.2**	**389.4**

Profit after taxation		
	£m	**£m**
Underlying profit before taxation	370.2	389.4
Reported tax credit/(charge)	(77.5)	(8.5)
Deferred tax credit - change in tax rate	-	(58.2)
Agreement of prior years' UK tax matters	0.4	(15.5)
Taxation in respect of adjustments to underlying profit before taxation	11.8	6.2
Underlying profit after taxation	**304.9**	**313.4**

Earnings per share		
	£m	**£m**
Profit after taxation per published results (a)	354.6	433.9
Underlying profit after taxation (b)	304.9	313.4
Weighted average number of shares in issue, in millions (c)	681.9m	681.9m
Earnings per share per published results, in pence (a/c)	52.0p	63.6p
Underlying earnings per share, in pence (b/c)	44.7p	46.0p
Dividend per share	39.73p	38.87p

Underlying operating profit reconciliation

The table below provides a reconciliation between group underlying operating profit and United Utilities Water Limited (UUW) historical cost regulatory underlying operating profit (non-GAAP measures) as follows:

Continuing operations
Underlying operating profit

	Year ended 31 March 2018 £m	Year ended 31 March 2017 £m
Group underlying operating profit	**645.1**	**622.9**
Underlying operating (profit) / loss not relating to UUW	(2.3)	1.0
UUW statutory underlying operating profit (unaudited)	**642.8**	**623.9**
Revenue recognition	(2.8)	5.4
Capitalised borrowing costs	4.1	3.6
Reclassification of regulatory other income (not included in UUW operating profit)	(29.1)	(30.5)
Other differences (including non-appointed business)	(3.9)	(5.0)
UUW regulatory underlying operating profit (unaudited)	**611.1**	**597.4**

Return on Regulated Equity (RoRE)

Whilst RoRE has been evolving as a measure for the last few years, Ofwat has helpfully clarified the definition to reduce the risk of any material inconsistencies.

UUW's RoRE, presented on a real return basis, for both the year ended 31 March 2018 and the cumulative position for the first three years of AMP6 are as below:

	Year ended 31 March 2018	AMP 6 to date
Base return	5.5%	5.6%
Totex performance	(0.5%)	(0.2%)
Retail performance	0.0%	0.0%
ODI performance	(0.2%)	0.0%
SIM performance	0.0%	0.0%
Financing performance	2.8%	1.7%
RoRE[1]	**7.7%**	**7.1%**

[1] Calculated in accordance with RAG 4.07, published in November 2017

[2] Total RoRE for the year ended 31 March 2018 differs to the sum of the lines above due to roundings.

PRINCIPAL RISKS AND UNCERTAINTIES

We continue to focus on creating sustainable value by delivering a high quality customer service, at the lowest sustainable cost, while acting in a responsible manner at every level within our organisation. In our day-to-day operations we encounter a wide variety of risks which can challenge the quality, cost-effectiveness and timescales for the delivery of our aims and ambitions. We identify and plan for mitigation of these risks under our established risk management framework which includes:

- An enterprise-wide approach to risk management;
- Oversight and control of risk through a well-established governance and reporting process;
- A risk assessment and management process which aligns to ISO 31000:2018; and
- Training materials, accessible policies and guidance to help our people to identify and manage risk in a consistent manner.

Our individual business areas and functions take responsibility for identifying, quantifying, communicating and controlling the risks relevant to their own business activities. We also use a forward looking approach to take into account new and emerging areas of concern and the long-term impact of risk. The identified risks cover a very wide range of potential events including regulatory, legal, core operations, service and hazard risks. They are reviewed and scored for likelihood as well as for financial and reputational impact should the identified event occur. Initially we use the gross position when assessing risk, i.e. we assume that any controls over the risk are absent or have failed. We then assess the current position of the risk including considering existing controls and their effectiveness. This is then followed by a targeted risk position which introduces further mitigating controls where the current state does not fully align with objectives and/or obligations.

Our governance and reporting process includes twice-yearly reports to our group board on the character of the group's risk profile, informed by the above risk identification and assessment approach. Individual event-based risks are identified and then categorised within ten inherent risk areas known as principal risks (see below). We also build on this overview in the board report, highlighting two key categories of risk: i) the most significant group-wide business risks; and ii) wholesale operational risks. These are represented by the 10 highest ranked risks (based on the scores awarded for likelihood x 'full life' financial impact) for each of the two categories plus a further five risks with potentially very high impact severity in their current state (net of control effectiveness). In addition, the report also identifies risks that could create potentially significant reputational impacts or are associated with potentially significant emerging topics but have not already been covered by the other reported categories.

Our approach aligns with the UK Corporate Governance Code and includes reports to the group board for every full and half year statutory accounting period so that the board is in a position to:

- Determine the nature and extent of the principal risks it is willing to take in achieving its strategic objectives;
- Oversee the management of those risks and provide challenge to executive management where appropriate;
- Express an informed opinion on the long-term viability of the company; and
- Monitor risk management and internal control systems and review their effectiveness.

Key developments

Key developments in the last 12 months include a maturing of and increased formalisation of our risk appetite framework. Our framework supports our assessment of the extent of risk we are willing to take based on obligations, stakeholders' requirements and the company's capacity and capability to manage risk. By doing this we aim to influence the target position for individual risks underpinning the principal risks through improved consistency. This approach also enables better benchmarking of individual risks against the appetite limits and boundaries. We have also sought to make an incremental governance improvement in our sign-off processes for all risks and also in relation to the wholesale risk and resilience board and the core risk team meetings which focus on long-term resilience. Associated with this is a focus on asset health and operational hazard risk assessment in advance of and beyond PR19. This supports our understanding of the long-term risk profile of our asset base and improves our capability to deliver the most cost-effective and proportionate risk management response as a result.

Profile features
Our risk profile currently consists of around 200 event-based risks. By their nature, these will include all combinations of high to low likelihood and high to low impact. Heat maps are typically used in various managerial and group reports either as a method to evaluate the extent of multiple risks within a certain profile or to evaluate the effectiveness of mitigation for a single risk relative to the initial gross position.

Political and regulatory risk and uncertainty feature prominently within the profile, notably with the outcome of PR19 which is expected to be even tougher than previous price reviews. The possibility of 'Renationalisation' is a key area of uncertainty as is the opening up to competition of wholesale operations (including the current focus on possible competition in bioresources and water abstraction) and the potential for competition covering domestic retail activities.

Our operations continue to be substantially UK-based, but the potential impacts of 'Brexit' remain under review and have been reported to the group board. In common with other UK companies, a significant issue is the uncertainty surrounding the effects of the Brexit deal that the UK Government ultimately delivers. Our review has considered the availability of European funding, the price of goods and services, exchange rate impacts, possible impacts on our ability to collect cash were there to be an economic downturn and the effect of any potential inflationary shift outside current predicted parameters. We continue to keep this area under review.

Following the launch of non-household retail competition in April 2017, we have continued to monitor our operations within the market to review compliance risks and ensure that we continue to operate in a manner that complements and promotes the 'level playing field'.

From an operational risk perspective, the dominance of the penalty element of Ofwat's outcome delivery incentive mechanism and the effect following changes to the Environmental Sentencing Guidelines are key features of evolving exposure. Reputationally, our core operations/service provision (notably water service) and health, safety and environmental risks have the highest focus for monitoring and reviewing control effectiveness based on the potential impact should the risk event occur.

We continue to adapt to and plan for climate change and its significant and permanent impacts on the water cycle, our operations and the broader operating environment. This includes consideration of the long-term viability of water and wastewater services such as water abstraction, drinking water supply and treatment capability, drainage and sewer capacity, wastewater treatment and its discharge efficiency and effectiveness. The recommendations of the Task Force on Climate-related Financial Disclosures (TCFD) support and reinforce the need to consider climate-related risks and uncertainties. These continue to be factored into risk management and the likely effects of future changes are a critical consideration in our long and medium-term risk, operational and financial planning. Our water service and wastewater service risks summarised below also reflect current key risks including the potential for extreme weather and climate change.

The principal risks (combinations of event-based risks), which have been set out below reflect the categories of risks that define business activity or contributing factors where value can be lost or gained and could have a material impact on the business model, future performance, solvency or liquidity of the group. In each case the nature and the extent of exposure is highlighted together with the extent of management/mitigation. To ensure relevance with the current environment, issues or areas of uncertainty are also illustrated.

1. **Political and regulatory risk -** potential change in the political and regulatory environment and/or frameworks

Principal/significant impacts could include:

- A potential increase in costs of administration, reduced income, margin and greater variability of returns;
- A potential loss of confidence of equity investors and challenging debt market conditions creating funding pressures given the need to raise finance and refinance debt on an on-going basis; and
- The possibility on a potential Renationalisation that the business is acquired below fair value.

To manage and mitigate this risk we engage in relevant government and regulatory consultations which may affect policy and regulation in the sectors where we operate. We also consult with customers to understand their requirements and proactively consider all the opportunities and threats associated with any potential change; exploiting opportunities and mitigating risks where appropriate. We keep customers and the public informed. We also provide information to the government, regulators, customers and the public as appropriate to help them to make informed decisions.

Current key risks, issues or uncertainties include: potential Renationalisation of the water sector; market reform including upstream competition and, further ahead, the potential for the introduction of domestic competition; change from using the retail prices index to the consumer prices index for regulatory indexation; and Brexit.

2. **Compliance risk** - failure to meet all legal and regulatory obligations and responsibilities

Principal/significant impacts could include the potential to receive penalties of up to ten per cent of relevant turnover and ultimately revocation of our licence or the appointment of a special administrator.

To manage and mitigate this risk we continually monitor legislative and regulatory developments and the governance framework utilised by the group. Risk-based training of employees is undertaken and we participate in consultations to influence legislative and regulatory developments. Allowance for any material additional compliance costs in the regulated business is sought as part of the price determination process. The group also robustly defends litigation where appropriate and seeks to minimise its exposure by establishing provisions and seeking recovery wherever possible.

Current key risks, issues or uncertainties include: competition law and regulatory compliance while preparing for and operating within a changing competitive market; level playing field requirements in relation to the non-household retail market; current material litigation; higher fine levels for environmental offences; and the introduction of material pieces of legislation e.g. the General Data Protection Regulation.

3. and 4. **Water service and wastewater service risks** - A failure to provide a secure supply of clean, safe drinking water and the potential for negative impact on public confidence in water supply or a failure to remove and treat wastewater

Principal/significant impacts could include:

- The potential for public health issues associated with poor water quality;
- The potential for supply interruptions that could affect large populations within the region for long durations; and
- The potential for serious pollution (including sewer flooding) leading to disruption to the public, businesses and the environment (wildlife, fish and natural habitats) resulting in fines and reputational damage.

We manage and mitigate these risks through core business processes, including centralised planning and control, quality assurance procedures, risk assessments and rigorous sampling/testing regimes. Optimisation of operational and maintenance tasks together with targeted capital interventions help to ensure services to customers are maintained. Our 25-year Water Resources Management Plan defines our strategy to achieve a long-term, best-value and sustainable plan for water supplies in the North West including consideration of over 20 different climate change scenarios including a 2°C or lower global warming scenario (assessing systems resilience). We continue to develop innovative solutions and invest in resilience to further support the delivery of water and wastewater services in the long-term.

Current key risks, issues or uncertainties include: population growth; extreme weather and climate change; meeting infrastructure investment requirements; expected change to the abstraction licensing regime; catchment management; raw water quality; drinking water safety and security; critical asset failure; and drought.

5. **Retail and commercial risk** - Failing to provide good and fair service to domestic customers and third party retailers

Principal/significant impacts could include:

- The potential for significant regulatory penalties and long-term reputational damage associated with poor customer satisfaction; and
- The potential for a significant increase in the bad debt charge, reducing profitability.

To manage and mitigate this risk we have a wide range of initiatives and activities focused on improving customer satisfaction, including proactive incident communication, complaints handling and use of appropriate tariffs. Bad debt risk is managed through the adoption of best practice collection techniques, segmentation of customers based on their credit risk profile and the use of data sharing to better understand customers' circumstances to determine the most appropriate collection and support activities. Our wholesale business maintains processes, systems, data and organisational capacity and capability to deal fairly with market participants and the central market operator in the Business Retail market in order to generate and collect revenue.

Current key risks, issues or uncertainties include: socio-economic deprivation in the North West; welfare reform and the impact on domestic bad debt; competition in the water and wastewater market and competitor positioning; Brexit; and non-household retail competition and the ability to treat other participants equally.

6. **Financial risk** - Potential inability to finance the business appropriately

Principal/significant impacts could include:

- The potential for worse credit ratings, associated funding costs or reduced access to debt capital markets leading to lower liquidity and adversely impacting the economic return on the regulatory capital value (RCV); and
- The potential for a worsening of the pension scheme funding position leading to a requirement for the group to make additional contributions.

To manage and mitigate this risk refinancing is long-term with staggered maturity dates to minimise the effect of short-term downturns. Counterparty credit exposure and settlement limits exist to reduce any potential future impacts. These are based on a number of factors, including the credit rating and the size of the asset base of the individual counterparty. The group also employs hedging strategies to manage the impact of market fluctuations for inflation, interest rates and energy prices. Sensitivity analysis is carried out as part of the business planning process, influencing the various financial limits employed. Continuous monitoring of the markets takes place including movements in credit default swap prices and movements in equity levels.

Current key risks, issues or uncertainties include: stability of financial institutions and the world economy; economic uncertainty; inflation/deflation; financial market conditions, interest rates and funding costs; and Brexit.

7. **Supply chain and programme delivery risk** - Potential ineffective delivery of capital, operational and change programmes/processes

Principal/significant impacts could include the potential failure to meet our obligations and customer outcomes resulting in an impact at future price reviews, negative reputational impact with customers and regulators.

To manage and mitigate this risk supply chain management is utilised to deliver an end-to-end contract management service, including contract strategy, tendering and category management, which provides a risk-based approach and relationship management programmes for suppliers. We prioritise our investment programmes, projects and integrated business and asset plans. We have created better alignment and integration between our capital delivery partners and engineering service providers including alignment with our operating model. Our programme and project management capabilities are well-established with strong governance and embedded processes to support delivery, manage risks and achieve business benefits. We utilise a time, cost and

quality index (TCQi) as a key performance indicator and enhance our performance through a dedicated programme change office to deliver change in a structured and consistent way.

Current key risks, issues or uncertainties include: security of supply; delivery of solutions, technical quality and innovation; and Brexit.

8. **Resources Risk** - Failing to provide appropriate resources (human, technological or physical resource) required to support business activity

Principal/significant impacts could include:

- The potential inability to recruit and retain knowledge/expertise; and
- The potential inability to respond and recover due to ineffective non-resilient business activity.

Manage and mitigation of this risk includes developing our people to have the right skills and knowledge, combined with delivering effective technology to support the business to meet its objectives. Employees are kept informed regarding business strategy and progress through various communication channels. Training and personal development programmes exist for all employees in addition to talent management programmes and apprentice and graduate schemes. We focus on change programmes and innovative ways of working to deliver better, faster and more cost-effective operations.

Current key risks, issues or uncertainties include: delivering required employee engagement; personal development and talent management; technological innovation; and asset management.

9. **Security risk** - Potential for malicious activity (physical or technological) against people, assets or operations

Principal/significant impacts could include:

- The potential for loss of data / information and the consequent effect on service provision; and
- The potential for catastrophic damage to UU property, infrastructure and non-infrastructure and the consequent effect on service provision.

To manage and mitigate this risk we utilise physical and technological security measures and awareness training combined with strong governance and inspection regimes which aim to protect infrastructure, assets and operational capability. Externally, we work closely with our industry peers, the Centre for the Protection of National Infrastructure (CPNI), the National Cyber Security Centre (NCSC) and Defra to shape the sector approach to security, particularly cyber security, and to understand how we can best deliver the appropriate levels of protection to our business. Ongoing system and network integration improves operational resilience and we maintain robust incident response, business continuity and disaster recovery procedures. We also maintain insurance cover for loss and liability and the licence of the regulated business also contains a 'shipwreck' clause that, if applicable, may offer a degree of recourse to Ofwat/customers in the event of a catastrophic incident.

Current key risks, issues or uncertainties include: cybercrime; terrorism; fraud; and ownership of Critical National Infrastructure and National Infrastructure.

10. **Health, safety and environmental risk** - Potential harm to people (employees, contractors or the public) and the environment

Principal/significant impacts could include:

- The potential for serious injury or loss of life in remote, extreme circumstances;
- The potential for catastrophic damage to private, public or commercial property / infrastructure including the consequent effect on water and wastewater service provision; and
- The potential for serious impact to wildlife, fish or natural habitats resulting in significant fines and reputational damage.

To manage and mitigate this risk we have developed a strong health and safety culture where 'nothing we do at United Utilities is worth getting hurt for', supported by strong governance and management systems certified to OHSAS 18001. We actively seek to improve health, safety and wellbeing across the group through targeted improvements and benchmarking against our peers. Also certified to ISO 14001, we seek to protect and improve the environment through the responsible delivery of our services. This includes helping to support rare species and habitats through targeted engagement and activity and commitment to reducing our carbon emissions by designing out waste from our operations, generating our own energy and looking at ways to reduce our use of raw materials. We also recognise the impact the environment can have on our service provision with extreme weather and climate change being integrated into our risk, planning and decision-making processes.

Current key risks, issues or uncertainties include: impounding reservoirs containing significant volumes of water; other critical asset failure; process safety; excavation, tunnelling and construction work; working with chemicals; and fluvial and coastal flooding.

Material Litigation

The group robustly defends litigation where appropriate and seeks to minimise its exposure by establishing provisions and seeking recovery wherever possible. Litigation of a material nature is regularly reported to the group board. While our directors remain of the opinion that the likelihood of a material adverse impact on the group's financial position is remote, based on the facts currently known to us and the provisions in our statement of financial position, the following two cases are worthy of note:

- In February 2009, United Utilities International Limited (UUIL) was served with notice of a multiparty 'class action' in Argentina related to the issuance and payment default of a US$230 million bond by Inversora Eléctrica de Buenos Aires S.A. (IEBA), an Argentine project company set up to purchase one of the Argentine electricity distribution networks which was privatised in 1997. UUIL had a 45 per cent shareholding in IEBA which it sold in 2005. The claim is for a non-quantified amount of unspecified damages and purports to be pursued on behalf of unidentified consumer bondholders in IEBA. UUIL has filed a defence to the action and will vigorously resist the proceedings given the robust defences that UUIL has been advised that it has on procedural and substantive grounds. There have been no material developments in this matter over the last 12 months; and
- In March 2010, Manchester Ship Canal Company (MSCC) issued proceedings seeking, amongst other relief, damages alleging trespass against United Utilities Water Limited (UUW) in respect of UUW's discharges of water and treated effluent into the canal. While the matter has not reached a final conclusion, the Supreme Court has found substantively in UUW's favour on a significant element of the claim and the High Court has upheld UUW's position on the remainder of the proceedings. MSCC have now instigated further heads of claim against UUW in order that they may continue to challenge UUW's rights to discharge water and treated effluent into the canal.

CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

This financial report 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 financial report and the company undertakes no obligation to update these forward-looking statements. Nothing in this financial report should be construed as a profit forecast.

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

This announcement contains inside information, disclosed in accordance with the Market Abuse Regulation which came into effect on 3 July 2016 and for UK Regulatory purposes the person responsible for making the announcement is Simon Gardiner, Company Secretary.

LEI 2138002IEYQAOC88ZJ59
Classification – Full Year Results

Consolidated income statement

	Year ended 31 March 2018 £m	Year ended 31 March 2017 £m
Revenue	**1,735.8**	1,704.0
Employee benefit expense (note 3)	**(153.5)**	(151.9)
Other operating costs (note 4)	**(423.4)**	(435.1)
Other income	**3.8**	4.2
Depreciation and amortisation expense	**(376.8)**	(364.9)
Infrastructure renewals expenditure	**(149.5)**	(150.8)
Total operating expenses	**(1,099.4)**	(1,098.5)
Operating profit	**636.4**	605.5
Investment income (note 5)	**12.0**	13.7
Finance expense (note 6)	**(218.6)**	(202.7)
Investment income and finance expense	**(206.6)**	(189.0)
Profit on disposal of business	**-**	22.1
Share of profits of joint ventures (note 10)	**2.3**	3.8
Profit before tax	**432.1**	442.4
Current tax charge	**(18.7)**	(31.5)
Deferred tax charge	**(58.8)**	(35.2)
Deferred tax credit - change in tax rate	**-**	58.2
Tax (note 7)	**(77.5)**	(8.5)
Profit after tax	**354.6**	433.9

All of the results shown above relate to continuing operations.

Earnings per share (note 8)		
Basic	**52.0p**	63.6p
Diluted	**51.9p**	63.5p
Dividend per ordinary share (note 9)	**39.73p**	38.87p

Consolidated statement of comprehensive income

	Year ended 31 March 2018 £m	Year ended 31 March 2017 £m
Profit after tax	**354.6**	433.9
Other comprehensive income		
Remeasurement gains/(losses) on defined benefit pension schemes (note 11)	**50.2**	(76.7)
Tax on items taken directly to equity (note 7)	**(8.5)**	17.3
Foreign exchange adjustments	**0.2**	3.7
Total comprehensive income	**396.5**	378.2

Consolidated statement of financial position

	31 March 2018 £m	31 March 2017 £m
ASSETS		
Non-current assets		
Property, plant and equipment	**10,790.5**	10,405.5
Intangible assets	**197.7**	187.7
Interests in joint ventures (note 10)	**75.2**	75.2
Investments	**7.1**	9.0
Trade and other receivables	**141.1**	112.3
Retirement benefit surplus (note 11)	**344.2**	247.5
Derivative financial instruments	**297.8**	731.0
	11,853.6	11,768.2
Current assets		
Inventories	**16.8**	22.4
Trade and other receivables	**260.9**	303.9
Current tax asset	**24.5**	7.1
Cash and short-term deposits	**510.0**	247.8
Derivative financial instruments	**337.7**	76.7
	1,149.9	657.9
Total assets	**13,003.5**	12,426.1
LIABILITIES		
Non-current liabilities		
Trade and other payables	**(642.7)**	(589.3)
Borrowings (note 12)	**(7,072.8)**	(7,058.4)
Deferred tax liabilities	**(1,098.8)**	(1,031.5)
Derivative financial instruments	**(96.8)**	(235.5)
	(8,911.1)	(8,914.7)
Current liabilities		
Trade and other payables	**(275.7)**	(323.0)
Borrowings (note 12)	**(839.5)**	(326.1)
Provisions	**(22.1)**	(26.5)
Derivative financial instruments	**(4.2)**	(14.2)
	(1,141.5)	(689.8)
Total liabilities	**(10,052.6)**	(9,604.5)
Total net assets	**2,950.9**	2,821.6
EQUITY		
Share capital	**499.8**	499.8
Share premium account	**2.9**	2.9
Cumulative exchange reserve	**(1.8)**	(2.0)
Merger reserve	**329.7**	329.7
Retained earnings	**2,120.3**	1,991.2
Shareholders' equity	**2,950.9**	2,821.6

Consolidated statement of changes in equity

Year ended 31 March 2018

	Share capital £m	Share premium account £m	Cumulative exchange reserve £m	Merger reserve £m	Retained earnings £m	Total £m
At 1 April 2017	**499.8**	**2.9**	**(2.0)**	**329.7**	**1,991.2**	**2,821.6**
Profit after tax	**-**	**-**	**-**	**-**	**354.6**	**354.6**
Other comprehensive income/(expense)						
Remeasurement gains on defined benefit pension schemes (note 11)	**-**	**-**	**-**	**-**	**50.2**	**50.2**
Tax on items taken directly to equity (note 7)	**-**	**-**	**-**	**-**	**(8.5)**	**(8.5)**
Foreign exchange adjustments	**-**	**-**	**0.2**	**-**	**-**	**0.2**
Total comprehensive income	**-**	**-**	**0.2**	**-**	**396.3**	**396.5**
Dividends (note 9)	**-**	**-**	**-**	**-**	**(267.0)**	**(267.0)**
Equity-settled share-based payments	**-**	**-**	**-**	**-**	**3.2**	**3.2**
Exercise of share options - purchase of shares	**-**	**-**	**-**	**-**	**(3.4)**	**(3.4)**
At 31 March 2018	**499.8**	**2.9**	**(1.8)**	**329.7**	**2,120.3**	**2,950.9**

Year ended 31 March 2017

	Share capital £m	Share premium account £m	Cumulative exchange reserve £m	Merger reserve £m	Retained earnings £m	Total £m
At 1 April 2016	499.8	2.9	(5.7)	329.7	1,878.8	2,705.5
Profit after tax	-	-	-	-	433.9	433.9
Other comprehensive income/(expense)						
Remeasurement losses on defined benefit pension schemes (note 11)	-	-	-	-	(76.7)	(76.7)
Tax on items taken directly to equity (note 7)	-	-	-	-	17.3	17.3
Foreign exchange adjustments	-	-	3.7	-	-	3.7
Total comprehensive income	-	-	3.7	-	374.5	378.2
Dividends (note 9)	-	-	-	-	(263.1)	(263.1)
Equity-settled share-based payments	-	-	-	-	3.4	3.4
Exercise of share options - purchase of shares	-	-	-	-	(2.4)	(2.4)
At 31 March 2017	499.8	2.9	(2.0)	329.7	1,991.2	2,821.6

Consolidated statement of cash flows

	Year ended 31 March 2018 £m	Year ended 31 March 2017 £m
Operating activities		
Cash generated from operations (note 14)	**989.8**	1,018.1
Interest paid	**(144.6)**	(161.0)
Interest received and similar income	**5.9**	4.9
Tax paid	**(35.5)**	(42.4)
Tax received	**-**	1.2
Net cash generated from operating activities	**815.6**	820.8
Investing activities		
Purchase of property, plant and equipment	**(698.6)**	(672.4)
Purchase of intangible assets	**(36.1)**	(52.4)
Proceeds from sale of property, plant and equipment	**1.1**	4.1
Grants and contributions received	**23.7**	29.0
Loans to joint ventures	**(26.5)**	(109.0)
Investment in joint ventures	**-**	(13.5)
Proceeds from disposal of business	**8.9**	3.3
Dividends received from joint ventures	**3.3**	5.4
Proceeds from investments	**1.0**	0.9
Net cash used in investing activities	**(723.2)**	(804.6)
Financing activities		
Proceeds from borrowings	**801.0**	736.2
Repayment of borrowings	**(345.9)**	(448.7)
Dividends paid to equity holders of the company (note 9)	**(267.0)**	(263.1)
Exercise of share options – purchase of shares	**(3.4)**	(2.4)
Net cash generated from financing activities	**184.7**	22.0
Net increase in cash and cash equivalents	**277.1**	38.2
Cash and cash equivalents at beginning of the year	**220.3**	182.1
Cash and cash equivalents at end of the year	**497.4**	220.3

NOTES

1. Basis of preparation and accounting policies

The condensed consolidated financial statements for the year ended 31 March 2018 have been prepared in accordance with the Disclosure and Transparency Rules of the Financial Conduct Authority.

The accounting policies, presentation and methods of computation are consistent with those applied in the audited financial statements of United Utilities Group PLC for the year ended 31 March 2017 and are prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union (EU).

The condensed consolidated financial statements do not include all of the information and disclosures required for full annual financial statements and do not comprise statutory accounts within the meaning of section 434 of the Companies Act 2006, but are derived from the audited financial statements of United Utilities Group PLC for the year ended 31 March 2018, for which the auditors have given an unqualified opinion.

The comparative figures for the year ended 31 March 2017 do not comprise the group's statutory accounts for that financial year. Those accounts have been reported upon by the group's auditor and delivered to the registrar of companies. The report of the auditor was unqualified and did not include a reference to any matters to which the auditor drew attention by way of emphasis without qualifying their report and did not contain a statement under section 498(2) or (3) of the Companies Act 2006.

Going concern

The directors have a reasonable expectation that the group has adequate resources for a period of at least 12 months from the date of approval of the condensed consolidated financial statements and have therefore assessed that the going concern basis of accounting is appropriate in preparing the condensed financial statements and that there are no material uncertainties to disclose. This conclusion is based upon a review of the resources available to the group, taking account of the group's financial projections together with available cash and committed borrowing facilities as well as consideration of the group's capital adequacy and any material uncertainties. In reaching this conclusion, the board has considered the magnitude of potential impacts resulting from uncertain future events or changes in conditions, the likelihood of their occurrence and the likely effectiveness of mitigating actions that the directors would consider undertaking.

2. Segmental reporting

The board of directors of United Utilities Group PLC (the board) is provided with information on a single segment basis for the purposes of assessing performance and allocating resources. The group's performance is measured against financial and operational key performance indicators which align with our three strategic themes to deliver the best service to customers, at the lowest sustainable cost, in a responsible manner. The board reviews revenue, operating profit, and gearing, along with operational drivers, at a consolidated level. In light of this, the group has a single segment for financial reporting purposes and therefore no further detailed segmental information is provided in this note.

3. Employee benefits expense

Included within employee benefits expense were £6.0 million (31 March 2017: £10.1 million) of restructuring costs.

Employee benefits expense is stated net of £nil (31 March 2017: £4.0 million) costs recharged to Water Plus at £nil margin under transitional service agreements.

4. Other operating costs

	Year ended 31 March 2018 £m	Year ended 31 March 2017 £m
Hired and contracted services	**97.7**	101.5
Property rates	**90.5**	91.6
Power	**70.4**	68.7
Materials	**67.3**	67.7
Regulatory fees	**29.7**	28.6
Charge for bad and doubtful receivables	**20.8**	29.9
Cost of properties disposed	**9.8**	8.6
Loss on disposal of property, plant and equipment	**6.8**	3.3
Legal and professional expenses	**5.8**	6.5
Operating leases payable	**4.2**	4.4
Third party wholesale charges	**-**	3.0
Impairment of property, plant and equipment	**-**	0.2
Compensation from insurers	**(3.6)**	(12.3)
Amortisation of deferred grants and contributions	**(6.4)**	(6.7)
Other expenses	**30.4**	40.1
	423.4	435.1

As a result of two significant flooding incidents caused by Storms Desmond and Eva in December 2015, there were £5.3 million (31 March 2017: £13.8 million) of expenses incurred, comprising £2.9 million (31 March 2017: £11.1 million) of operating costs, £2.4 million (31 March 2017: £2.5 million) of infrastructure renewals expenditure, and a £nil (31 March 2017: £0.2 million) impairment of property, plant and equipment. Insurance compensation of £3.6 million (31 March 2017: £12.3 million) relating to the flooding incidents has been recognised as part of a final settlement of the insurance claim. The group does not expect there to be any further costs or insurance receipts in respect of the flooding incidents.

In addition, there were £1.0 million (31 March 2017: £5.8 million) of market reform restructuring costs relating to the non-household retail market opening to competition in April 2017.

Total other operating costs are stated net of £1.4 million (31 March 2017: £14.5 million) of costs recharged to Water Plus at nil margin under transitional service agreements.

5. Investment income

	Year ended 31 March 2018 £m	Year ended 31 March 2017 £m
Interest receivable	**4.9**	3.5
Net pension interest income (note 11)	**7.1**	10.2
	12.0	13.7

6. Finance expense

	Year ended 31 March 2018 £m	Year ended 31 March 2017 £m
Interest payable	**265.9**	227.0
Net fair value gains on debt and derivative instruments	**(47.3)**	(24.3)
	218.6	202.7

Interest payable is stated net of £39.7 million (31 March 2017: £29.2 million) borrowing costs capitalised in the cost of qualifying assets within property, plant and equipment and intangible assets during the year. Interest payable includes a £137.8 million (31 March 2017: £80.7 million), non-cash inflation uplift expense repayable on maturity in relation to the group's index-linked debt.

Net fair value gains on debt and derivative instruments includes £23.5 million income (31 March 2017: £15.4 million) due to net interest on swaps and debt under fair value option.

7. Tax

During the year ended 31 March 2018 there was a current tax credit of £6.7 million (31 March 2017: £22.5 million) and a deferred tax charge of £7.1 million (31 March 2017: £7.0 million) relating to agreed matters in relation to prior years; the prior year figure includes the release of a provision in relation to agreed historic overseas tax matters. During the prior year there was also a deferred tax credit of £58.2 million reflecting the substantive enactment of the reduction in the headline rate of corporation tax to 17 per cent from 1 April 2020.

After adjusting for the above tax credits, the total effective tax charge for the current and prior years was in line with the headline rate of corporation tax, currently 19 per cent (31 March 2017: 20 per cent). The split of the total tax charge between current and deferred tax relates to ongoing timing differences in relation to tax deductions on pension contributions, capital investment, and unrealised gains and losses on treasury derivatives.

The tax adjustments taken to equity primarily relate to remeasurement movements on the group's defined benefit pension schemes.

8. Earnings per share

Basic and diluted earnings per share are calculated by dividing profit after tax by the weighted average number of shares in issue during the year. The weighted average number of shares in issue as at 31 March 2018 for the purpose of the basic earnings per share was 681.9 million (31 March 2017: 681.9 million) and for the diluted earnings per share was 683.1 million (31 March 2017: 683.0 million).

9. Dividends

	Year ended 31 March 2018 £m	Year ended 31 March 2017 £m
Dividends relating to the year comprise:		
Interim dividend	**90.3**	88.3
Final dividend	**180.6**	176.8
	270.9	265.1
Dividends deducted from shareholders' equity comprise:		
Interim dividend	**90.3**	88.3
Final dividend	**176.7**	174.8
	267.0	263.1

9. Dividends (continued)

The proposed final dividends for the years ended 31 March 2018 and 31 March 2017 were subject to approval by equity holders of United Utilities Group PLC as at the reporting dates, and therefore have not been included as liabilities in the consolidated financial statements as at 31 March 2018 and 31 March 2017 respectively.

At March 2017, the proposed final dividend was £176.8 million although the final dividend amount actually paid was £176.7 million. This difference is due to a higher than anticipated number of shares purchased cum dividend to satisfy the dividend reinvestment plan. Dividends in relation to these shares are waived.

The final dividend of 26.49 pence per ordinary share (2017: 25.92 pence per ordinary share) is expected to be paid on 3 August 2018 to shareholders on the register at the close of business on 22 June 2018. The ex-dividend date for the final dividend is 21 June 2018.

The interim dividend of 13.24 pence per ordinary share (2017: 12.95 pence per ordinary share) was paid on 1 February 2018 to shareholders on the register at the close of business on 22 December 2017.

10. Joint ventures

	Year ended 31 March 2018 £m	Year ended 31 March 2017 £m
At the start of the year	**75.2**	35.1
Additions	**-**	39.1
Share of profits of joint ventures	**2.3**	3.8
Dividends received from joint ventures	**(3.3)**	(5.4)
Currency translation differences	**1.0**	2.6
At the end of the year	**75.2**	75.2

The group's interests in joint ventures mainly comprise its interests in Water Plus Group Limited (Water Plus) and AS Tallinna Vesi (Tallinn Water). Water Plus is jointly owned and controlled by the group and Severn Trent PLC under a joint venture agreement. Joint management of Tallinn Water is based on a shareholders' agreement.

Tallinn Water has disclosed a new contingent liability of EUR 26.5 million in its latest financial statements relating to possible third-party claims. If this contingent liability materialises in the future this would impact the group's share of profits of the joint venture and the joint venture's carrying value under the equity method of accounting.

Details of transactions between the group and its joint ventures are disclosed in note 17.

11. Retirement benefit surplus

The main financial assumptions used by the company's actuary to calculate the defined benefit surplus of the United Utilities Pension Scheme (UUPS) and the United Utilities PLC Group of the Electricity Supply Pension Scheme (ESPS) were as follows:

	Year ended 31 March 2018 %pa	Year ended 31 March 2017 %pa
Discount rate	**2.60**	2.55
Pensionable salary growth and pension increases	**3.35**	3.40
Price inflation - RPI	**3.35**	3.40
Price inflation - CPI	**1.95**	-

11. Retirement benefit surplus (continued)

At both 31 March 2018 and 31 March 2017, mortality in retirement is assumed to be in line with the Continuous Mortality Investigation's (CMI) S2PA year of birth tables, with scaling factor of 108 per cent for males and 102 per cent for females, reflecting actual mortality experience. At 31 March 2018, mortality in retirement is based on CMI 2016 (31 March 2017: CMI 2015) long-term improvement factors, with a long-term annual rate of improvement of 1.75 per cent (31 March 2017: 1.75 per cent).

The net pension expense before tax in the income statement in respect of the defined benefit schemes is summarised as follows:

	Year ended 31 March 2018 £m	Year ended 31 March 2017 £m
Current service cost	**27.3**	19.7
Curtailments/settlements	**2.3**	3.1
Administrative expenses	**2.6**	2.7
Pension expense charged to operating profit	**32.2**	25.5
Net pension interest credited to investment income (note 5)	**(7.1)**	(10.2)
Net pension expense charged before tax	**25.1**	15.3

The reconciliation of the opening and closing net pension surplus included in the statement of financial position is as follows:

	Year ended 31 March 2018 £m	Year ended 31 March 2017 £m
At the start of the year	**247.5**	275.2
Expense recognised in the income statement	**(25.1)**	(15.3)
Contributions paid	**71.6**	64.3
Remeasurement gains/(losses) gross of tax	**50.2**	(76.7)
At the end of the year	**344.2**	247.5

The closing surplus at each reporting date is analysed as follows:

	31 March 2018 £m	31 March 2017 £m
Present value of defined benefit obligations	**(3,498.7)**	(3,615.5)
Fair value of schemes' assets	**3,842.9**	3,863.0
Net retirement benefit surplus	**344.2**	247.5

In the year ended 31 March 2018 the discount rate has increased by 0.05 per cent, which includes a 0.05 per cent decrease in credit spreads and a 0.1 per cent increase in swap yields over the year. The £50.2 million remeasurement gain has largely resulted from the impact of the decrease in credit spreads during the year, partially offset by the reduction in gilt-swap spreads, growth asset gains, and the favourable impact of changes in mortality during the year. Further details on the approach to managing pension scheme risk are set out in the audited consolidated financial statements of United Utilities Group PLC for the year ended 31 March 2018.

Member data used in arriving at the liability figure included within the overall IAS 19 surplus has been based on the finalised actuarial valuation as at 31 March 2016 for the group's UUPS and ESPS schemes.

12. Borrowings

New borrowings raised during the year ended 31 March 2018 were as follows:

- On 21 July 2017 the group drew down £100.0 million and on 2 October 2017 the group drew down the remaining £75.0 million against its £250.0 million term loan facility signed in April 2016 with the European Investment Bank. These floating rate loans are structured on an amortising basis with final repayments due in July and October 2035 respectively.
- On 4 October 2017 the group issued HKD 830.0 million fixed interest rate notes due October 2027.
- On 5 October 2017 the group issued £32.0 million CPI index-linked notes due October 2048 and £33.0 million CPI index-linked notes due October 2057. The issue of these notes is connected to the partial close out of £50.0 million RPI index-linked notes due April 2043 with a nominal value of £30.0 million (carrying value £41.3 million) at a fair value of £64.4 million. The purchase of the RPI index-linked notes resulted in a £23.1 million fair value loss.
- On 6 October 2017 the group issued EUR 28.0 million fixed interest rate notes due October 2032.
- On 6 December 2017 the group issued EUR 26.0 million fixed interest rate notes due December 2032.
- On 23 January 2018 the group issued EUR 30.0 million fixed interest rate notes due January 2033.
- On 14 February 2018 the group issued £300.0 million fixed interest rate notes due February 2025.
- On 23 February 2018 the group issued HKD 739.0 million fixed interest rate notes due February 2026.

The notes were issued through private placement under the Euro medium-term note programme.

13. Fair values of financial instruments

The fair values of financial instruments are shown in the table below.

		31 March 2018		31 March 2017
	Fair value £m	Carrying value £m	Fair value £m	Carrying value £m
Available for sale financial assets				
Investments	7.1	7.1	9.0	9.0
Financial assets at fair value through profit or loss				
Derivative financial assets - fair value hedge	455.7	455.7	591.1	591.1
Derivative financial assets - held for trading	179.8	179.8	216.6	216.6
Financial liabilities at fair value through profit or loss				
Derivative financial liabilities - fair value hedge	(24.2)	(24.2)	-	-
Derivative financial liabilities - held for trading	(76.8)	(76.8)	(249.7)	(249.7)
Financial liabilities designated as fair value through profit or loss	(347.7)	(347.7)	(375.5)	(375.5)
Financial instruments for which fair value does not approximate carrying value				
Financial liabilities in fair value hedge relationships	(2,905.9)	(2,895.3)	(2,544.6)	(2,522.4)
Other financial liabilities at amortised cost	(5,798.4)	(4,669.3)	(5,682.8)	(4,486.6)
	(8,510.4)	**(7,370.7)**	**(8,035.9)**	**(6,817.5)**

A decrease in underlying interest rates on index-linked debt during the year is the principal reason for the reduction in the difference between the fair value and carrying value of the group's borrowings.

The group has calculated fair values using quoted prices where an active market exists, which has resulted in 'level 1' fair value liability measurements under the IFRS 13 'Fair value measurement' hierarchy of £2,192.4 million (31 March 2017: £1,766.1 million) for financial liabilities in fair value hedge relationships and £2,425.6 million (31 March 2017: £937.9 million) for other financial liabilities at amortised cost.

13. Fair values of financial instruments (continued)

The £1,914.0 million increase (31 March 2017: £755.4 million reduction) in 'level 1' fair value liability measurements is largely due to an increase in the number of observable quoted bond prices in active markets at 31 March 2018. In the absence of an appropriate quoted price, the group has applied discounted cash flow valuation models utilising market available data which are classified as 'level 2' valuations. More information in relation to the valuation techniques used by the group and the IFRS 13 hierarchy can be found in the audited financial statements of United Utilities Group PLC for the year ended 31 March 2018.

14. Cash generated from operations

	Year ended 31 March 2018 £m	Year ended 31 March 2017 £m
Operating profit	**636.4**	605.5
Adjustments for:		
Depreciation of property, plant and equipment	**348.4**	336.2
Amortisation of intangible assets	**28.4**	28.7
Impairment of property, plant and equipment	**-**	0.2
Loss on disposal of property, plant and equipment	**6.8**	3.3
Loss on disposal of intangible assets	**-**	0.5
Amortisation of deferred grants and contributions	**(6.4)**	(6.7)
Equity-settled share-based payments charge	**3.2**	3.4
Other non-cash movements	**(3.3)**	(3.0)
Changes in working capital:		
Decrease in inventories	**5.6**	6.9
Decrease in trade and other receivables	**27.5**	71.1
Decrease in trade and other payables	**(13.0)**	(0.6)
(Decrease)/increase in provisions	**(4.4)**	11.4
Pension contributions paid less pension expense charged to operating profit	**(39.4)**	(38.8)
Cash generated from operations	**989.8**	1,018.1

15. Net debt

	Year ended 31 March 2018 £m	Year ended 31 March 2017 £m
At the start of the year	**6,578.7**	6,260.5
Net capital expenditure	**701.0**	691.7
Dividends (note 9)	**267.0**	263.1
Interest	**138.7**	156.1
Inflation uplift on index-linked debt (note 6)	**137.8**	80.7
Tax	**35.5**	41.2
Loans to joint ventures	**26.5**	109.0
Other	**(0.7)**	4.4
Fair value movements	**(26.9)**	(9.9)
Cash generated from operations (note 14)	**(989.8)**	(1,018.1)
At the end of the year	**6,867.8**	6,578.7

Net debt comprises borrowings, net of cash and short-term deposits and derivatives. As such, movements in net debt during the year reflected in the above reconciliation are impacted by net cash generated from financing activities as disclosed in the consolidated statement of cash flows.

15. Net debt (continued)

Fair value movements includes net fair value gains on debt and derivative instruments of £47.3 million (31 March 2017: £24.3 million net fair value gains) less net receipts on swaps and debt designated at fair value of £20.4 million (31 March 2017: £14.4 million).

Notional net debt totals £6,830.2 million as at 31 March 2018 (31 March 2017: £6,385.2 million). Notional net debt is calculated as the principal amount of debt to be repaid at the 31st March 2018 net of interest related mark-to-market adjustments.

16. Commitments and contingent liabilities

At 31 March 2018 there were commitments for future capital expenditure contracted but not provided for of £432.9 million (31 March 2017: £336.9 million).

The group has determined that the possibility of any outflow in respect of performance guarantees issued is remote and, as such, no contingent liabilities are disclosed (31 March 2017: none).

17. Related party transactions

The related party transactions with the group's joint ventures during the period and amounts outstanding at the period end date were as follows:

	Year ended 31 March 2018 £m	Year ended 31 March 2017 £m
Sales of services	**496.3**	404.3
Purchases of goods and services	**0.7**	0.7
Costs recharged at nil margin under transitional service agreements	**1.4**	18.5
Interest income and fees recognised on loans to related parties	**3.4**	2.6
Amounts owed by related parties	**179.7**	163.5
Amounts owed to related parties	**1.4**	12.1

Sales of services to related parties during the year mainly represent non-household wholesale charges and were on the group's normal trading terms.

At 31 March 2018 amounts owed by joint ventures, as recorded within trade and other receivables in the statement of financial position, were £179.7 million (31 March 2017: £163.5 million), comprising £42.5 million (2017: £41.5 million) of trade balances, which are unsecured and will be settled in accordance with normal credit terms, and £137.2 million (2017: £122.0 million) relating to loans. Included within these loans receivable were the following amounts owed by Water Plus:

- £100.0 million outstanding on a £100.0 million revolving credit facility provided by United Utilities Water Limited, which is guaranteed by United Utilities PLC, with a maturity date of 30 September 2019, bearing a floating interest rate of LIBOR plus a credit margin;
- £9.3 million receivable being the fair value of amounts owed in relation to a £12.5 million unsecured loan note held by United Utilities PLC, with a maturity date of 28 March 2027. This is an interest-free shareholder loan with a total amount outstanding at 31 March 2018 of £12.5 million, comprising the £9.3 million receivable held at fair value, and £3.2 million recorded as an equity contribution to Water Plus recognised within interests in joint ventures; and
- £26.5 million outstanding on a £32.5 million revolving credit facility provided by United Utilities PLC, with a maturity date of 30 September 2019, bearing a floating interest rate of LIBOR plus a credit margin.

17. Related party transactions (continued)

A further £1.4 million of non-current receivables (31 March 2017: £3.3 million) was owed by other related parties at 31 March 2018.

No expense or allowance has been recognised for bad and doubtful receivables in respect of the amounts owed by related parties (31 March 2017: £nil).

During the year, United Utilities PLC provided guarantees in support of Water Plus in respect of certain amounts owed to wholesalers. The aggregate limit of these guarantees was £42.5 million (31 March 2017: £42.5 million), of which £24.0 million (31 March 2017: £24.0 million), related to guarantees to United Utilities Water Limited.

At 31 March 2018, amounts owed to joint ventures were £1.4 million (31 March 2017: £12.1 million). The amounts outstanding are unsecured and will be settled in accordance with normal credit terms (31 March 2017: same).

18. Events after the reporting period

There were no events arising after the reporting date that required recognition or disclosure in the financial statements for the year ended 31 March 2018.

STATEMENT OF DIRECTORS' RESPONSIBILITIES

The responsibility statement below has been prepared in connection with the group's full annual report for the year ended 31 March 2018. Certain parts thereof are not included within this announcement.

Responsibilities Statement

We confirm that to the best of our knowledge:

- the financial statements have been prepared in accordance with IFRS as adopted by the European Union, give a true and fair view of the assets, liabilities, financial position and profit or loss of the company and the undertakings included in the consolidation taken as a whole; and
- the strategic report includes a fair review of the development and performance of the business and the position of the issuer and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face.

We consider the annual report, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the group's position and performance, business model and strategy.

The directors of United Utilities Group PLC at the date of this announcement are listed below:

Dr John McAdam
Steve Mogford
Stephen A Carter
Mark Clare
Steve Fraser
Alison Goligher
Russ Houlden
Brian May
Paulette Rowe
Sara Weller

This responsibility statement was approved by the board and signed on its behalf by:

Steve Mogford
23 May 2018
Chief Executive Officer

Russ Houlden
23 May 2018
Chief Financial Officer