

Chairman's statement I am pleased to report on a year of sound achievement. The financial results, standards of service and quality and overall environmental performance continue to improve, reflecting the benefits of our strategic focus on water and waste water interests.

Financial results:-

- before tax, profit, including exceptionals at £197.1m, increased 26.0% on prior year.
- after adjustment for non operating exceptional items, profit increased 15.8% to £162.7m.
- adjusted earnings per share increased 11.7% to 35.3p per share.
- full year dividend increased 2.8% to 25.5p.

In the UK, Yorkshire Water:-

- continued to make gains in efficiency and service levels.
- further improved drinking water quality and environmental standards, including the delivery of its "CoastCare" programme.
- is on target to fully deliver the AMP3 capital plan.

In the US, Aquarion:-

- improved results from water operations.
- finalised the acquisition of the adjacent American Water Works companies in April 2002, increasing the customer base by 50%.
- completed its land sale which has realised a £60.3m exceptional gain.

Progress on the focus strategy has included:-

- completion of the UK non core business disposal programme with the sale of First Renewables.
- continued strengthening of management at all levels and further reductions in corporate costs.

Financial results

The main drivers of the annual profit growth from continuing operations were a strong performance from Yorkshire Water, increased operating results from water operations in the US and good growth in associated company operating profits from Waste Recycling Group (WRG). The performance of First Renewables in the UK and the Timco timber operations in the US were below expectations. The sale of First Renewables has been completed and the sale of the Timco operations is in progress.

There was an exceptional profit of £60.3m made from the completion of the land sale in the US. This was partly offset by a full provision of £25.9m against the disposal of First Renewables.

Corporate costs continued to reduce on a year to year basis. The balance sheet remains strong, due to the benefits of business disposal proceeds, although borrowing has increased slightly with the significant capital investment programme.

Operational results

The results of Yorkshire Water reflect the full year's impact of the major reductions in operating costs completed early last financial year and a fundamental review of management and operations which included the internal separation of asset and operations management. These actions, allied to continuing improvement in management standards and further investment in operational systems, have delivered further cost efficiencies and service improvements.

There has been good second year outperformance compared to the regulatory determination due to the early implementation of plans and enhanced management performance, which is creditable. Outperformance does not mean, however, that the regulatory settlement was appropriate to the longer term needs of the company and the industry.

In addition to important improvements in service standards Yorkshire Water has also increased compliance on drinking water quality and waste water discharge.

The company has also performed well on capital delivery objectives. These are a different challenge as there is a significant change in contract mix with a much higher proportion of low value schemes compared to the major projects which were typical of the previous capital programme. The "CoastCare" programme, which has raised bathing water quality standards of the principal Yorkshire east coast resorts, has now been largely completed and should help give those areas a major tourist boost.

In the US, Aquarion benefited from a dry summer with increased usage, which helped increase profits in water operations. In addition to a continuing emphasis on quality and service standards, there were two other main areas of management focus. The first related to the finalisation of the land sale, which was satisfactorily completed with the state of Connecticut and The Nature Conservancy, the international conservation organisation. The result was the largest land deal for open space preservation in the history of the company and Connecticut. The second was to expand operations with the acquisition of the American Water Works' operations in Connecticut, Massachusetts, New Hampshire and New York. This achieved regulatory approval in April 2002, in record time, and has increased the US customer base by approximately 50%.

The smaller businesses, KeyLand Developments and Loop Customer Management, had satisfactory years. KeyLand plays an important role in developing surplus property assets on an agreed arms length basis with the regulated Yorkshire Water activity. Loop operates a call centre and customer access unit supporting Yorkshire Water. It has gained a number of third party contracts, which include the National Blood Service, the Wales Tourist Board and the Merseyside Fire and Civil Defence Authority.

The results from First Renewables were below expectations due to delays in the operational development of the Arbre renewable energy plant. The performance of the minority investment in Fibrowatt improved on a year to year basis. The sale of First Renewables (which includes the Arbre plant and the investment in Fibrowatt) has now been completed.

Outlook

The company has contributed to the industry debate with the government and regulator on the conditions necessary to enable it to fulfil its responsibility and obligations to customers and secure essential investment capital on a long term sustainable basis. There has been an important recognition of the performance and contribution that all water companies have made in delivering service, quality and environmental improvements. This needs to influence government and regulatory thinking in the longer run with the objective of increasing the attractiveness of the water sector to capital and equity markets generally.

The establishment of the Glas Cymru structure, and the sales of Wessex and Southern Water utilising some aspects of highly leveraged financing at close to their regulatory asset value, has helped restore some of the shareholder value significantly eroded by the last regulatory settlement. This has combined with what appears to be a greater market recognition of the counter cyclical strengths of water company shares. The public acknowledgement of the performance of water companies by the government and regulator has also given some encouragement to the sector, as has the welcome clarification of the industry competitive situation which has helped reduce longer term uncertainty.

Although regulatory uncertainties still remain, they have been reduced by a more constructive dialogue between the regulator, government and industry. The realisation of an increased need for continuing high levels of investment, partly driven by environmental and quality improvement demanded by European legislation and essential infrastructure replacement, is now more apparent. It should give a more positive emphasis to future price determinations, if this necessary investment is to be financed from equity and debt markets.

Whilst accepting that there are issues outside our control, our objective remains to continue to focus on water and waste water and to drive for further service and quality enhancements on a sustainable basis in both the UK and US. There is the scope for further controlled growth in the US. The significant improvement in water company valuations in the US has helped enhance the value of existing operations.

Management and staff

In parallel with the strategic focus of the company, there has been an ongoing drive on all aspects of management and employee performance. My thanks to all staff who have responded to the challenges needed to improve performance and achieve these results.

Following the management buyout of Foseco led by Jamie Pike, he is to stand down at the annual general meeting. Jamie, who joined the Kelda Board on the same day as myself, has been supportive of the strategy and management of the company, and I would like to thank him, and my fellow directors, for their contribution and support.



John Napier
Executive Chairman