



DŴR CYMRU
WELSH WATER

June Return 2003



Overview

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Introduction

This report provides an overview of Dŵr Cymru's performance in the year to 31 March 2003. It is addressed to the Director General of Ofwat and accompanies our annual June Return.

It covers levels of service and outputs for our water and sewerage activities, environmental performance, financial performance and overall progress against targets established at the last price review in 1999 and at the Interim Determination (IDOK) in 2000.

Highlights for the year

Customer service delivery

- Overall compliance with drinking water quality standards "at the tap" as measured by the Operational Performance Index (OPI) best ever at 99.79%
- Compliance with bacteriological drinking water quality standards "at the tap" maintained at 99.75%
- Leakage targets achieved and water abstractions now 10% lower than in 1998
- Properties at risk of low pressure (DG2) reduced to 0.03%, down from 0.06% in 2001/02
- Unplanned interruptions to supply (DG3) reduced to 0.08%, down from 0.14% in 2001/02
- Properties at risk of sewage flooding (DG5) reduced to 297, down from 395 in 2001/02
- Best ever performance in meter reading (DG8) and steady improvement in customer contact centre performance.
- Compliance with environmental quality standards at wastewater treatment works maintained at 99.5%
- Number of "Category 1 and 2" pollution incidents reduced to 13 in 2002, down from 22 in 2001

- Best ever results for bathing water quality; 100% compliance with "mandatory" standard and 83% with tighter "guideline" standard leading to 33 Blue Flag beach awards in 2003, 7 more than in 2002 and a third of the UK total.

Financial performance

- Key financial measures ahead of the targets published at the time of the Glas bond issue in May 2001
- Earnings before interest, tax, depreciation and amortisation (EBITDA) up 4% at £260 million
- Net debt of £2,014 million now 85% of Regulatory Capital Value (RCV), down from 89%
- Customer bill rebates worth £11 million in 2003/04 implemented
- Overall, £1.2 billion AMP3 capital investment programme on track to deliver key outputs by 2005 on time and within budget
- On course to meet or exceed target for Financial Reserves (RCV less net debt) of £400 million by March 2005
- Water service operating costs are 5% lower, sewerage operating costs 3% higher than in 2001/02. Total operating costs were

£10.8m behind the assumptions, included in the 1999 Final Determination. However, overall base operating costs have reduced by some 5% over the reporting year.

- Capital investment for the year was £267m, some £28m more than assumed in the 1999 Final Determination.

AMP3 improvement outputs

- 433km of water mains renewed or relined in the year to improve water quality (S19 Undertaking on target).
- 35 Water Treatment Works schemes completed.
- 22 Wastewater Treatment Works improvement schemes completed.
- 205 CSO schemes completed
- Capital maintenance expenditure in line with Ofwat 1999 Final Determination.

Competitive Procurement Plan

In 2001 we implemented a competitive procurement policy under which specialist service providers now carry out under contract much of the day to day operation of assets and service delivery. We also out-sourced customer billing and call centre operation.

As reported last year, following a highly competitive process in accordance with EU Procurement Rules, United Utilities and Thames Water remain our service providers for operations and customer billing and contact centre services respectively.

Our procurement strategy is designed to bring significant benefits to Welsh Water and its customers, including the best combination of value for money and quality of service from the most capable and competitive operators in the marketplace for each distinct area of activity.

Preparations have commenced for the competitive re-tendering of the main service delivery contracts, namely, asset operations, asset investment, income and billing, IT and sampling and laboratories.

The new arrangements will take effect from 1 April 2005.

The procurement process will support the development of the Company's Strategic Business Plan by establishing and demonstrating cost efficient delivery of the "Final SBP" and as such will provide additional information for Regulators when they are judging Dwr Cymru's relative cost efficiency and as a result reduce possible concerns about "regulatory risk".

Progress against Monitoring Plan

In our Monitoring Plan, published in December 2000, we set out the minimum service standards we expected to achieve over the AMP3 period and the target levels we are aiming to achieve by 2005. This Overview provides a summary of our progress against these targets.

Performance against the Monitoring Plan

Water Service

Performance Measure	Units	The 2005 Monitoring Plan Target	Previous Performance 2001/02	Actual Performance 2002/03
DG2 Properties below reference level for low pressure	No.	1,828	748	410
DG2 Properties at risk of receiving low pressure	%	0.14	0.06	0.03
DG3 Overall performance score (interruption to supply)	No.	0.66	0.14	0.08
DG4 Restrictions on water supply	No.	0	0	0
Trend in burst mains per 1,000km of main	No.	194	203	208
Distribution input not covered by S19 undertakings	%	98	80.75	95.57
Compliance with water quality regulations "at the tap"	%	99.8	99.60	99.83
Iron compliance "at the tap"	%	97.7	98.78	98.81

Sewerage Service

Performance Measure	Units	The 2005 Monitoring Plan Target	Previous Performance 2001/02	Actual Performance 2002/03
Properties flooded internally – excluding extreme / severe weather	No.	310	169	169
Total props subject to internal flooding (excluding extreme / exceptional weather)	%	0.023	0.013	0.013
Properties at risk of flooding	No.	315	395	297
Trend in sewer collapses per 1,000km of sewer	No.	27	36	25.4
Wastewater treatment works complying with numeric consents	%	100	98.2	98.0*
Combined sewer overflows satisfactory	%	81	71	77

* Performance is based on a revised definition (Ofwat reporting requirements 2002/03).

Quality and Environmental Compliance

Performance Measure	Units	The 2005 Monitoring Plan Target	Previous Performance 2001/02	Actual Performance 2002/03
Percentage population equivalent served by compliant works (LUT)	%	>90	99.97	99.97
Sewage sludge disposed of satisfactorily	%	100	100	100
Bathing waters – compliance with mandatory standards	%	100	93.3	100
Bathing waters – compliance with guideline standards	%	Stable	60.0	83
Number pollution incidents at CSOs and sewers (cat 1 & 2)	no.	9 +/- 30%	11	6

Customer Service

Performance Measure	Units	The 2005 Monitoring Plan Target	Previous Performance 2001/02	Actual Performance 2002/03
DG6 Billing contacts responded to within 5 days	%	99.2	99.99	99.99
DG7 Written complaints responded to within 10 days	%	99.46	99.1	99.7
DG8 Bills based on company or customer meter readings	%	99.7	99.9	99.96
DG9 Received telephone calls answered within 30 seconds*	%	94.6	98.45	95.12*

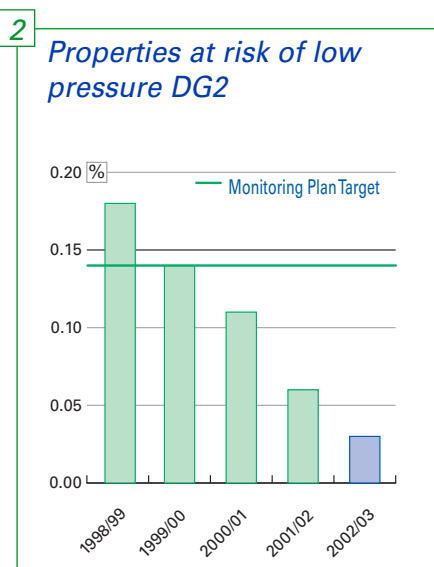
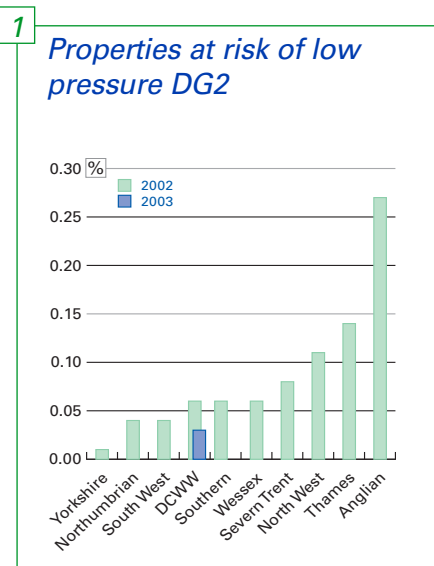
* Actual DG9 performance reported for 2002/03 reflects performance without the use of a front-line call answering system and reflects the % of calls answered by a company agent in accordance with revised Ofwat reporting requirements.

CHAPTER 1

Key Outputs and Service Delivery

Over the last year we have made further improvements to our levels of service to customers and overall we are meeting our targets for water and wastewater quality improvement.

We carry out regular research with customers to understand their satisfaction with the services provided by Dŵr Cymru. Latest research shows that overall satisfaction with the Company's levels of service remains high.



Water Service

Low pressure DG2

In 1999 the company set itself a challenging DG2 target of 0.14% by 2005. By the end of the 2002/03 reporting year 410 properties or 0.03% received a supply below the reference level for low pressure. This compares with 748 properties in 2001/02 and 1,439 properties in 2000/01.

Our performance continues to be well above the average for the sector (0.03% of properties compared with the industry average of 0.09% for 2001/02).^[1]

In total 1,764 properties have been removed from the DG2 register as a result of company action; this has involved targeted mains replacement and a continued focus on a rolling programme of pressure monitoring.

DG2 additions resulting from asset deterioration show a downward (improving) trend with 996 property additions in 2002/03 as compared with 1,078 in the previous year, reflecting positive outputs from the Company's maintenance programme.^[2]

Interruptions to supply DG3

During the year 678 properties experienced unplanned supply interruptions lasting more than 6 hours, compared with 1,501 in the previous year. Correspondingly, Company performance as measured by Ofwat's "overall performance score" has improved this year to 0.08% (2002/03) from 0.14% in the previous year, continuing the trend of year on year improvement delivered since 1999.^[3]

The number of unplanned supply interruptions lasting more than 12 hours has also reduced with 170 properties affected in 2002/03 as compared to 331 properties in the previous year.

During the year we have invested significantly on a programme of mains renewal and maintenance and continued to focus on reducing response times to asset breakdown and on pressure management. Despite this, the number of bursts per km of water main has increased this year. In addition, we have again reported an increase in the number of planned interruptions

reflecting the relatively high level of mains refurbishment activities that has been undertaken on the network.

Despite the increase in activity levels our DG3 performance on all measures continues to be well above the sector average. ⁴

Delivering the drinking water compliance programme

The company achieved a high level of water quality compliance during 2002 with performance against a number of key measures being best ever. This performance reflects both the continued improvements at Water Treatment Works, the substantial ongoing investment on water mains rehabilitation and improvements in operational procedures defined in the Company's Quality Management System.

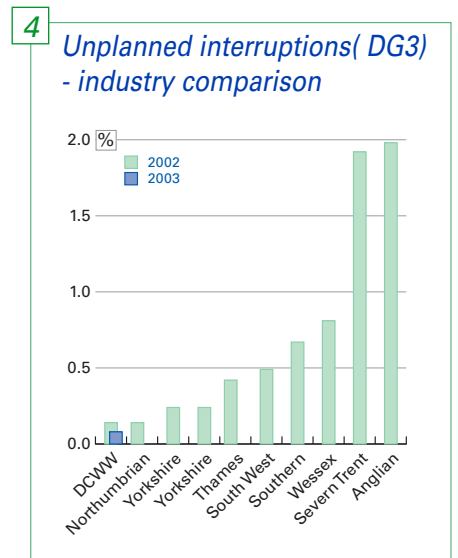
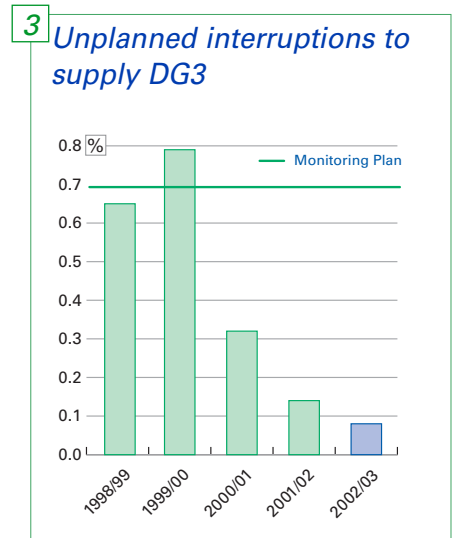
In the reporting year we have renovated some 433km of unlined iron mains to meet the DWI S19 Undertakings (411 km in calendar year 2002) and we remain on track to achieve key Milestones for the revised programme agreed with DWI following delays, in the early part of AMP3, to the original programme caused by the Foot and Mouth Disease outbreak.

The revised standard on lead (reduction from 50ug/l to 25 ug/l by 2004 and to 10ug/l by 2014) is likely to require replacement of a considerable number of lead communication pipes. Both Ofwat and DWI advocate that companies should adopt a policy of treatment

for plumbosolvency at works to meet the interim standard before committing to a programme of lead pipe replacement. Since the start of AMP3 we have taken steps to comply with the interim standard by providing plumbosolvency treatment and control at 38 water treatment works. In addition, we have introduced a policy of replacing lead communication pipes in zones where the water mains are being replaced (rather than relined) as part of the quality improvement programme. In the reporting year we replaced a total of 1,064 lead communication pipes, down from 3,901 in 2001/02 reflecting the overall shape of the S19 programme and against a nil allowance for this work included in the IDOK.

Overall compliance with drinking water quality standards "at the tap" improved to 99.79%, up from 99.60%. Compliance with bacteriological drinking water standards "at the tap" was broadly stable at 99.75% in the reporting year as compared to 99.81 % in the previous year.

The "Operational Performance Index" ("OPI") covers six water quality parameters which reflect operational performance of water treatment works and distribution networks. Compliance on this measure improved from 99.49% to 99.79%, mainly as a result of much higher compliance against the quality standard for trihalomethanes which improved from 95.30% to 99.85% following capital investment improvement schemes at all the affected water



treatment works.

Compliance with the drinking water quality standards for iron and manganese, the usual cause of discoloured water at customers' taps and also part of the OPI measure, was 98.81% and 99.85% respectively.

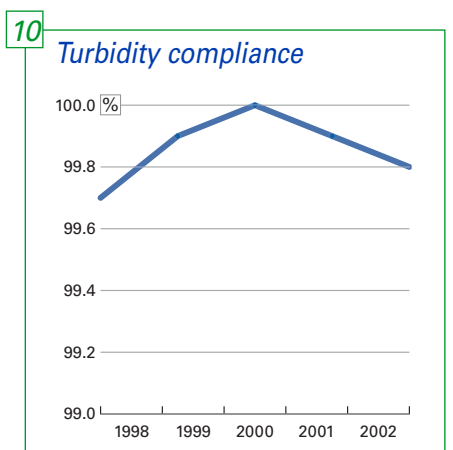
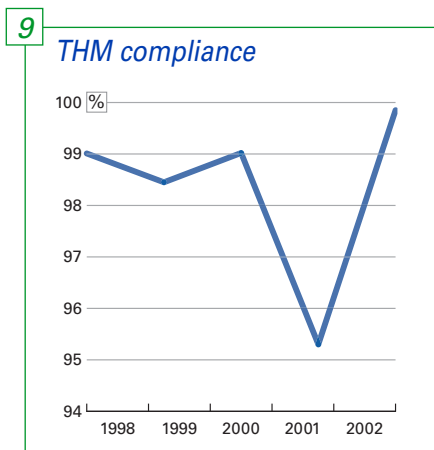
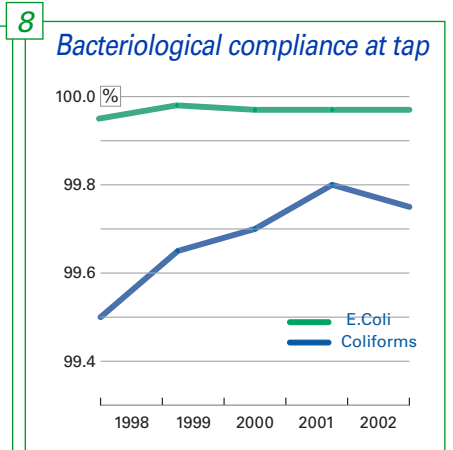
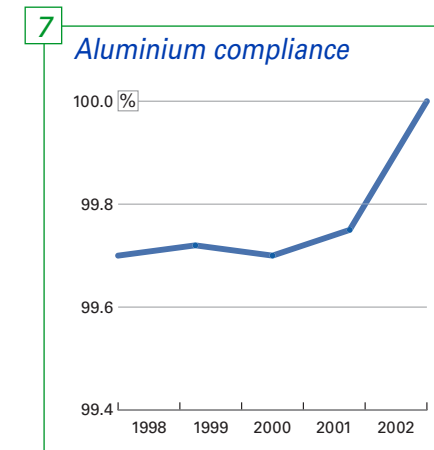
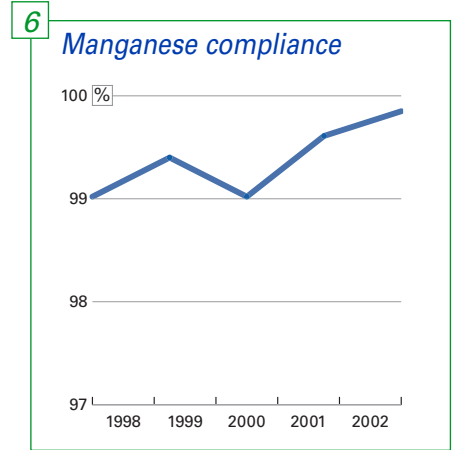
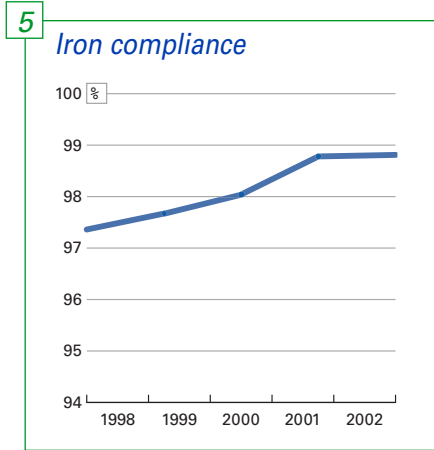
There has been no recurrence of the problems of geosmin, experienced in 2001. Two incidents of discoloured water occurred in the Swansea Valley affecting customers fed from the Crai Water Treatment Works. We will be replacing 66km of Trunk Mains during 2003 to prevent a repeat of these discolouration incidents.

Performance against the six main parameters which comprise the OPI measure is shown in the charts opposite. [5][6][7][8][9][10]

Compliance for coliforms at water treatment works has remained high in the reporting year, with only 0.04% of Water Treatment Works samples containing coliforms in 2002. We have also reported improvements in compliance in Service Reservoirs and this continues the trend of year on year improvement since 1997/98. [11]

Bacteriological Compliance - 2002

	Coliforms	E.Coli
WTW	99.96%	100%
Service Reservoirs	99.92%	99.99%
Zones	99.75%	99.97%



Maintaining serviceability to customers

Despite continued improvement in customer levels of service we have reported an increase in the number bursts on our mains network. This is despite experiencing a mild and frost free winter and a relatively high rate of renewal for unlined iron water mains.

In 2002/03 the mains burst rate (per km) was some 2.5% higher than in 2001/02, with a total of 208 bursts per 1,000km. The Company's monitoring plan target for burst reduction was 15% over the 5 year period from the 1999/00 baseline (228). Over the first three years of this regulatory period the burst rate has been reduced by some 9%. [12](#) [13](#)

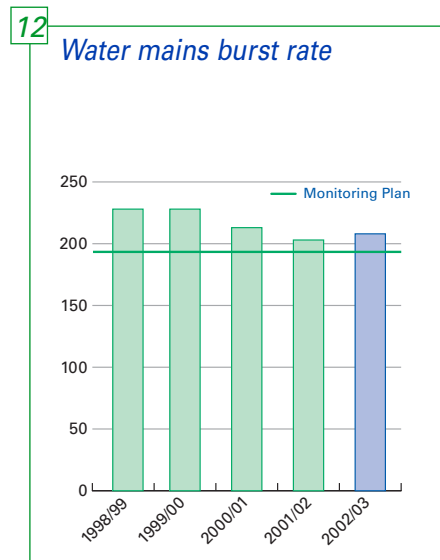
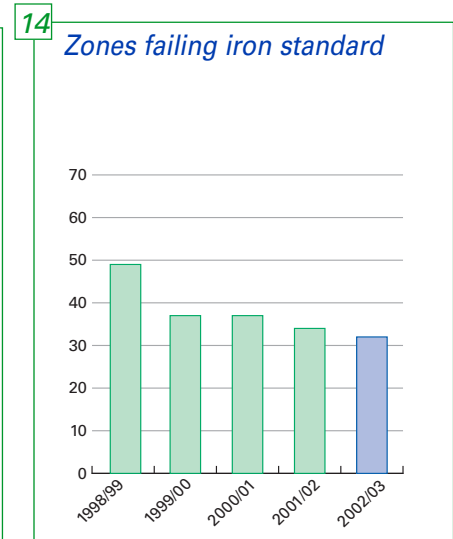
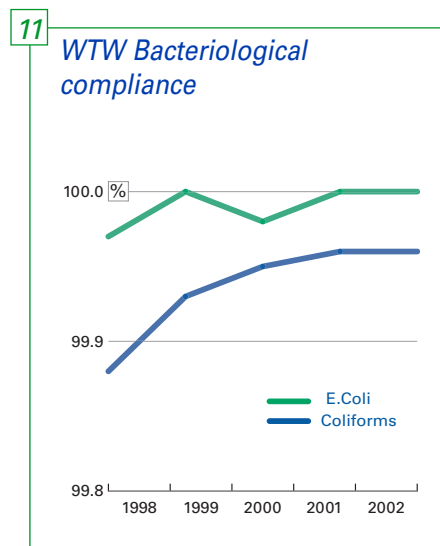
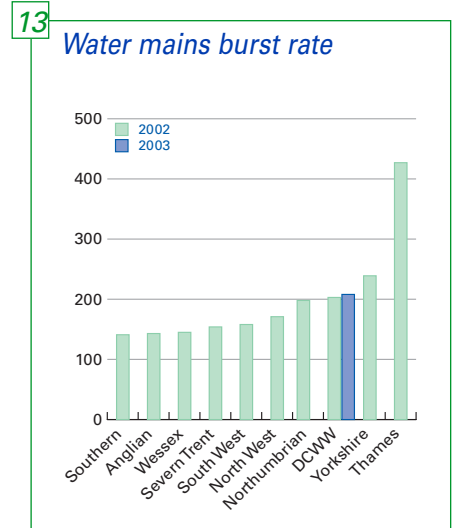
Investment in the first 3 years of AMP3 has been targeted at tackling the highest burst frequency mains, including initiatives to secure significant pressure reduction. It is against this background that the burst rate has increased and it is likely that, due to constraints on maintenance investment during the remaining two years of AMP3, the target 15% reduction by 2005 may not be achievable and we believe that a 10% reduction from 1999/00 levels may be more realistic.

Although there is no clear reason why the burst trend has reversed, we remain committed to reducing the impact of these bursts on customers as reflected in our improving DG2 and DG3 performance.

Our mains refurbishment

programme is steadily improving our compliance with the water quality standard for iron. Out of the Company's total of 161 zones, 32 experienced sample failure against the water quality standard for iron at least once during the year, which continues the trend of steady improvement. [14](#)

We have reported to DWI that 98.81% of samples from customers' taps, in 2002, were compliant within the required standard of 200 ug/l iron per litre.



Sewerage Service

Sewer Flooding DG5

Reducing the risk of sewage flooding is a priority for Dŵr Cymru. £23m of the £41m reinvestment of targeted savings announced in November 2001 is to accelerate work to reduce the risk of sewage flooding for some 250 properties which have been flooded more than once following very heavy rainfall. This takes our total planned AMP3 spend to £37m on alleviating sewage flooding problems and this will deliver over 600 solutions, which is around twice what was allowed for in the Final Determination and included in our Monitoring Plan.

During the reporting year we carried out investment schemes to remove the risk of sewage flooding from 95 properties, and we removed a further 44 properties from the “at risk register (ARR)” as a result of better information being available following re-investigation.

The average cost per property has reduced from £76,000 reported in 2001/02 to £58,000 in the report year mainly reflecting an increased focus on reducing the risk of flooding to properties at risk during severe storm periods, which are generally less expensive to rectify than those properties which remain on the ARR. The average cost for properties remaining on the ARR alone was in the order of £117,000.

During the year a total of 41 properties have been added to the register and so the total number of properties on the Company’s

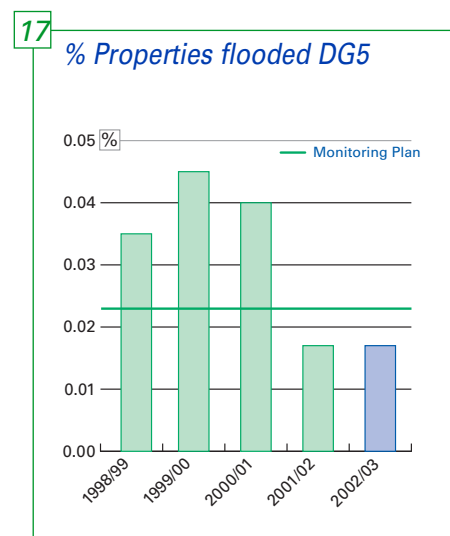
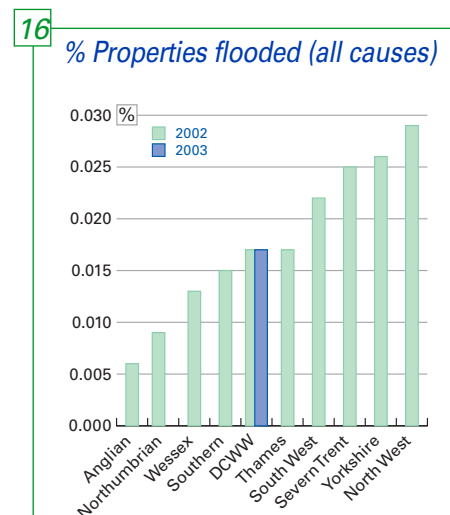
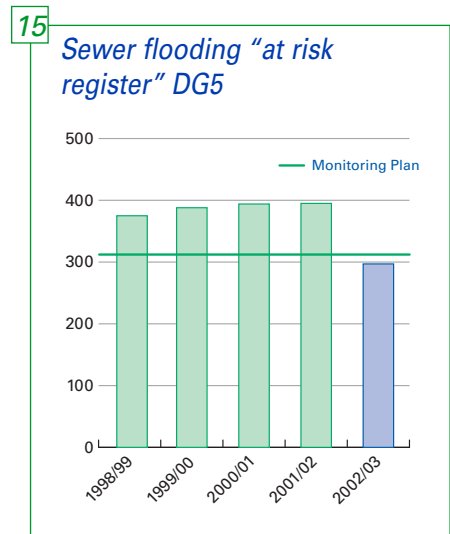
“at risk register” at the end of the reporting year was 297, a net decrease of nearly one quarter (98 properties) compared with the 2001/02. ¹⁵

Since March 2000 we have fixed almost 500 problems and the DG5 “at risk register” is now at its lowest ever level.

We have prioritised work throughout the year to address problems at properties where flooding has occurred most frequently. Significantly, the number of properties remaining on the “at risk register”, with a “2 in 10” (properties at risk of flooding more than twice in 10 year) risk of flooding, has reduced from 117 last year to 90 in the reporting year.

The underlying DG5 performance (ie excluding the incidents caused by exceptional weather) has remained stable over the report year. The percentage of properties that experienced flooding (all causes) was 0.017% in 2002/03. ¹⁶ ¹⁷

Although we are addressing properties which we know to be at risk, each year new incidents occur where flooding has not been experienced before (an average of 120 properties a year). It is high priority for the business, for the remaining part of AMP3 and in AMP4 to identify these vulnerable areas in advance of any problems occurring.



Delivering the quality enhancement programme

At the start of the current AMP3 period 2000-2005 the Company had some 3,000 intermittent discharges at sewage treatment works, sewage pumping stations, and within the sewerage system.

We commenced the 2002/03 reporting year with 966 unsatisfactory intermittent discharges identified on the Environment Agency (EA) list and we have dealt with 205 of these in the year against a business plan target of 177 ¹⁸

In the year we completed a total of 23 identified quality outputs of which 12 are on the NEP to be completed in the report year and 11 are scheme outputs completed early. We have also partially completed 4 schemes and one AMP2 scheme (previously delayed because of planning) carried over to AMP3.

In the first three years of AMP3 we have completed a total of 47 scheme outputs scheduled for completion in Years 1-3 benefiting a population equivalent of 824,564 against an NEP target of 68 outputs with a population equivalent of 963,978. The delays of the 21 outputs originally scheduled for completion in Year 1-3 have been caused by circumstances beyond our control e.g. planning and land use constraints or have been delayed with prior agreement between the Company and the EA where further investigation has been required.

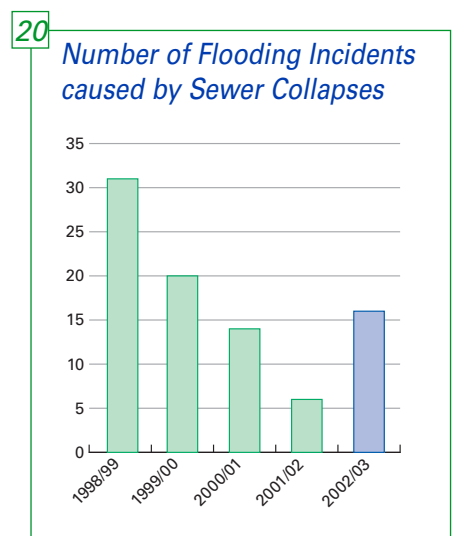
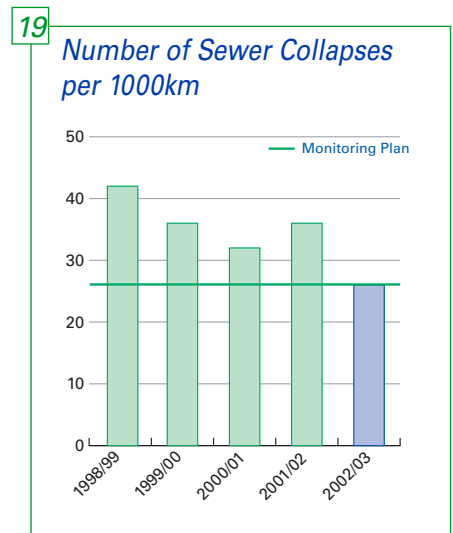
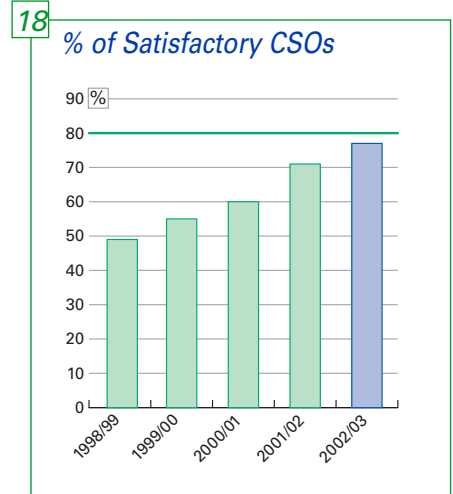
We recognise the importance of delivering the appropriate level of environmental improvements each to year in order to keep the overall programme on track. To mitigate the impact of these delays we have accelerated, and completed early, 11 additional scheme outputs from Years 4 and 5 with a total population equivalent of 101,285 as well as partially completing a further 4 schemes.

In the AMP3 period up to 31st March 2003, scheme outputs completed on wastewater treatment works have therefore delivered 96% of the population equivalent targeted on the NEP and subject to achieving the necessary planning approvals, we remain confident of meeting our agreed five year NEP target outputs by the end of year 5.

Maintaining Serviceability to Customers

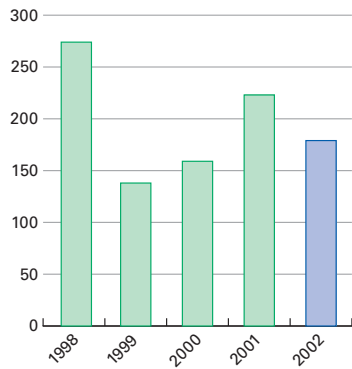
Over the AMP3 period the Company has targeted a 25% reduction in the rate of sewer collapses; aimed at bringing the number of collapses per 1,000km of sewer down to 26 per 1,000km by 2005.

In the reporting year we have reported a decrease in the number of sewer collapses from 36 per 1,000km in 2001/02 to 25.4 per 1,000km in 2002/03. During the year we have renovated / replaced 71km of sewers (not including refurbishment of sewers under the CSO programme of work).



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Number of Pollution Incidents at CSOs Cat 1, 2 and 3

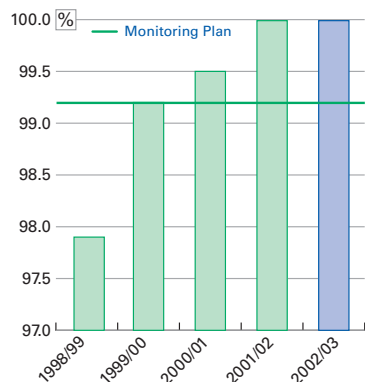


Number of Pollution Incidents associated with CSOs and Foul Sewers during 2002.

Incident Category	No. of incidents associated with CSOs	No. of incidents associated with Foul Sewers
1	0	0
2	4	2
3	108	65
Total	112	67

22

DG6 Performance - % of Billing contacts dealt with within 5 working days



However, despite achieving our Year 5 target early, the collapse rate remains significantly higher than the sector average (approximately 13 / 1,000km) ^[19]

Our sewer network contract partners have continued to undertake a programme of de-silting, cleaning and inspection, targeted in the North West and South East areas of Wales. A total of 230km of CCTV investigations have been carried out during the year further improving our understanding of asset condition and helping to direct investment.

Despite the overall decrease in collapse rates we have reported an increase in the number of flooding incidents resulting from sewer collapses. ^[20]

We have reported a total of 13 Category 1 and 2 pollution incidents of which 6 were associated with combined sewer overflows and foul sewers.

With the inclusion of Category 3 incidents the total number of incidents was 255 for the year. Of this total 179 were caused by CSOs and foul sewers, which compared to a figure of 223 for 2001 represents an improved performance on this important measure. ^[21]

Compliance at wastewater treatment works with numeric consents was 98.0% in calendar year 2002, down from 98.2% in calendar year 2001, caused by compliance problems at one additional works during the report year, which reflects the sensitivity of this measure. Two works failed "look-up" with the result that 99.97% of "equivalent" population

was served by "look-up" compliant works in calendar year 2002, the same as reported for calendar year 2001.

Customer Contact
Billing contacts DG6

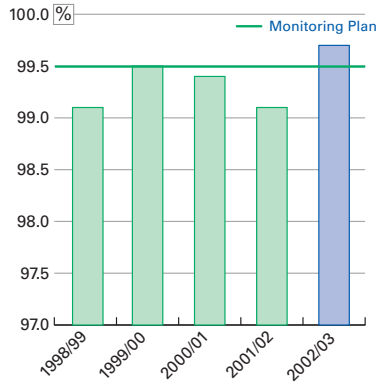
During the reporting year we handled over one million queries and requests concerning bills, a decrease of some 17% compared with 2001/02. Of the total nearly 160,000 were written contacts and just over 850,000 were telephone contacts.

We dealt with 99.99% of billing contacts within a five day period, in line with 2001/02.

Overall billing contacts have decreased due to a reduction in repeat contacts and debt recovery related queries. ^[22]

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DG7: % of Written Complaints responded to within 10 days
Performance against the monitoring plan



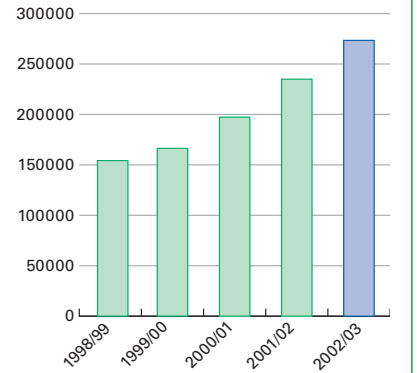
Written complaints DG7

In the reporting year we responded to 13,271 written complaints compared with 18,809 in 2001/02. This is a decrease of almost 30% and we have also reported an improvement in the DG7 performance from 99.1% to 99.7%. This performance is now above the monitoring plan target for 2005 set at 99.5%. 23 24

The decrease in the number of complaints reported has occurred mainly in the customer accounts area of the business, which accounts for almost 80% of the total number of complaints received. Approximately 15% of complaints were directly associated with the initiatives to collect outstanding customer debt.

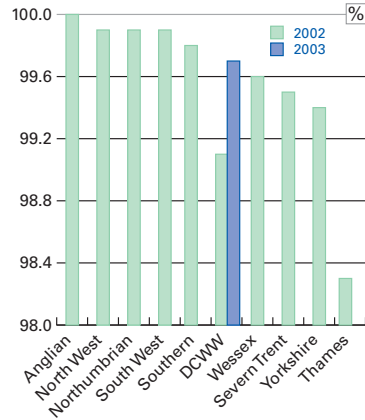
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Number of metered accounts



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DG7: % of Written Complaints responded to within 10 days
Industry Comparison



Meter reading DG8

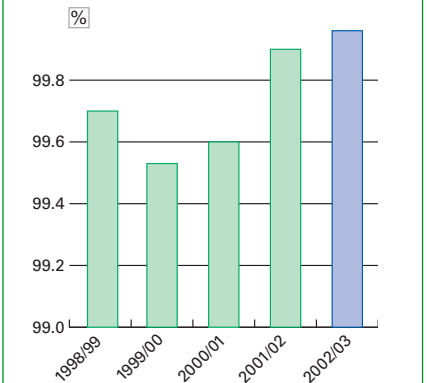
During 2002/03 we have achieved our best ever DG8 compliance, with 99.96% of metered accounts being read during the year. The number of meter readings has increased from 201,906 in 2001/02 to 249,242 in 2002/03. 25 26

In addition, we have reported only 154 meters that have not been read by the Company for two years, well within the Ofwat target of <0.15%.

During the report year we have implemented a series of initiatives to improve the performance associated with internal meter reading. These included new working practices and improved job scheduling. Our customers' responses to these initiatives have been positive.

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% Meters read DG8

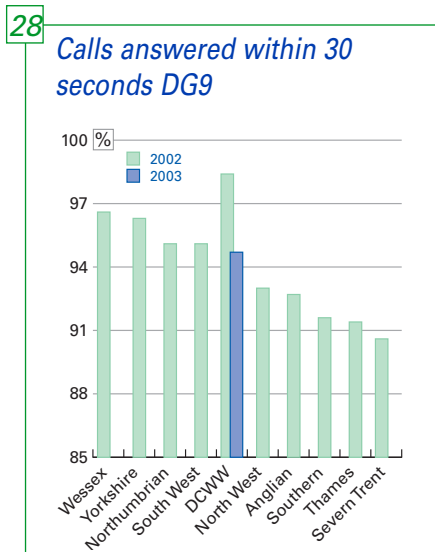
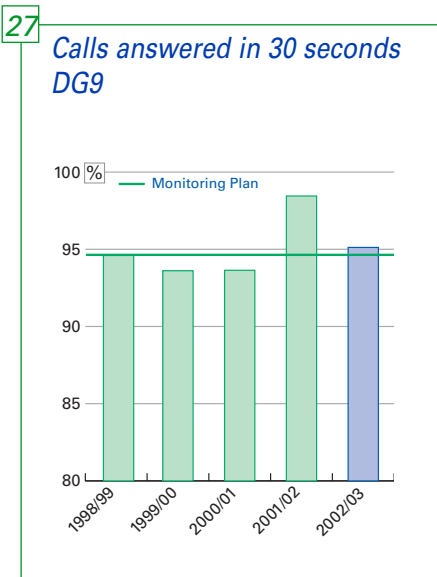


Telephone contact DG9

During the reporting year over one million calls were received on the principal advertised customer contact points.

This represents a 13% decrease compared to 2001/02. The improved performance is attributed to a reduction in repeat contacts, debt recovery related queries, multi-skilling of agents and the use of "Q-Max" for call forecasting and shift alignment.

The average time taken to answer telephone calls from customers was 5 seconds with 95.1% of calls being answered within 30 seconds. These are both slight reductions on the previous year, but represent an improvement in "real" customer service delivery as the call centre is now fully operational without any form of front-line facility, and with agents that are able to substantially answer customer queries directly. 27 28



Health and Safety

Progress in managing health and safety performance during the report year has been good and the process of health and safety management promoted by the Company has been extended to all Contract Partners working with Welsh Water to deliver services to water and sewerage customers.

The way in which we manage our health and safety responsibilities under an outsourced procurement strategy is fully documented. In general terms we assess the health and safety competence of contractors prior to appointment, we set proactive performance targets and monitor against these monthly to promote continuous improvement and robust health and safety practice. In addition to monthly reporting, we also have a process of internal cross auditing to supplement external and independent audits of health and safety performance. Where we have significant incidents

these are subject to thorough investigation and review to ensure that lessons are learnt, across all Contract Partners.

One of the key features of our process is that we monitor performance not just of individual contractors, but also of the natural business groups (alliances) which deliver services to our customers. We believe this to be relatively unique to the Company in the way that Contract Partners voluntarily work together to deliver jointly agreed health and safety targets and objectives to improve the overall performance of our business.

With the increase in the level and consistency of Health and Safety monitoring implemented across the business during the report year, any comparison with previous years' data would not be meaningful. In JR03/04 we will report fully against specific targets using 2002/03 as a baseline comparison.

Notwithstanding some excellent performance this year, we have some challenges ahead, particularly to reduce the overall number of incidents that arise from activities undertaken by or on behalf of the Company.

We have set our staff and Contract Partners the challenge of reducing the overall number of reportable incidents to 15% below 2002/2003 levels by March 2005, and to further reduce this to 30% below 2002/2003 by March 2010.

Chapter 2:

Financial Performance Measures

Glas Cymru's financial performance during the year was satisfactory with all financial measures being ahead of the forecasts made in the "Glas Cymru Bond Prospectus" in May 2001.

The following summarises the financial position for the year and actual performance against financial projections for both Dŵr Cymru and Glas Cymru.

Dŵr Cymru

Turnover in the year to 31 March 2003 was £457.6m, some 1% higher than in the previous financial year. Income from industrial customers fell, due to lower manufacturing activity.

The average domestic customer bill in 2002/03 was £275, as compared with £304 in the year 1999/00.

We have continued to make steady progress in managing costs. Operating expenditure for the water service before exceptional items was £112m which, in real terms, is some 5% less than 2001/02 but £5.4m above that forecast in the Final Determination.

Operating expenditure for the sewerage service, before exceptional items, was £94.5m, which is 2% higher than in 2001/02, in real terms reflecting substantial costs of operating new works in the year, but is in line with business plan projections and is £5.4m higher than that forecast in the Final Determination.

Capital expenditure during the year was £107m for the water service and £160m for the sewerage service, a total

of £267m (net of infrastructure contributions).

This figure was some £28m more than assumed for 2002/03 in the Final Determination (including IDOK and using Ofwat's November 1999 inflation assumptions).

The current five year AMP3 capital investment programme 2000-2005 is budgeted to cost £1.175bn in total (which is public domain). This figure includes the reinvestment of £41m for additional high customer value outputs announced in November 2001.

Investment spend in the first three years has been £679m, some £85m behind what was assumed in the Final Determination (including IDOK and using Ofwat's November 1999 inflation assumptions used to calculate the Company's RCV). The difference is due to some rephasing of the capital investment programme, some delays due to planning or Foot and Mouth during 2000/01, completing less expensive solutions in the early part of the programme (CSO programme) and better than assumed cost efficiency.

Overall, the programme remains on track to deliver required improvements on time and within budget.

We have overcome the restrictions on our mains refurbishment programme (which was delayed by the outbreak of Foot and Mouth disease) and are now on course to deliver all the reprofiled targets for the regulatory period. During the report year we have experienced delays to some wastewater treatment schemes but where possible we have brought forward additional schemes, from years 4 and 5, for early completion.

In addition, the total capital maintenance expenditure for both water and sewerage services is in line with the total allowed for in the Final Determination.

Glas Cymru

Operating cashflow (EBITDA) was £260m, an increase of 4% over the previous year. This is also some 5% ahead of the forecast for the equivalent period made in the bond issue prospectus in May 2001.

On 18 March 2003, Ofwat published an updated calculation of Regulatory Capital Value (RCV) for Dwr Cymru as at 31 March 2003 of £2,362m at outturn prices. The level of net debt was £2,014m. Financial "reserves" (RCV less net debt) as at 31 March 2003 were therefore £348m, up from £241m at the start of the year. This compares to a forecast level of financial "reserves" at 31 March 2003 of £224m which was

made in the bond prospectus in May 2001.

Net debt as at 31 March 2003 represents 85% of RCV, down from 89% at the start of the year.

Net interest payable (including indexation) during the period was £128m, up 3% on the previous year due to the increasing level of net debt over the period.

EBITDA interest cover over the year was 2.2 times up from 2.1 times in 2001/02.

Profit before tax for the year was £68m, including certain non cash items such as amortisation of negative goodwill of £47m.

The tax charge for the period was £7.4m, which wholly relates to deferred tax in accordance with FRS19. There is no current tax charge for the period due primarily to the tax allowances arising from the capital investment programme.

Chapter 3:

Key Supporting Information

The organisational changes within the business, following the acquisition by Glas Cymru, has resulted in an overall greater transparency of operating and capital costs for both the water and sewerage services. Over 75% of the Company's annual expenditure is carried out under contract with service providers and operating and capital partners.

The largest element of operating expenditure is undertaken by United Utilities. All service providers and partners report expenditure over the various functional expenditure categories in line with Ofwat definitions.

Overall operating expenditure for the water and sewerage services was £206.9m. Total operating expenditure is £10.8m above that assumed in the Final Determination.

Allowing for inflation and the operating cost impact of new treatment works, this represents an improvement in underlying cost efficiency of around 5% in real terms. Operation of the new Cardiff Wastewater Treatment Works alone cost the Company some £5m over the course of its first year

The operating expenditure position at the end of the year in respect of the four principal outsourced contracts is shown in the Table 1.

Water

Operating expenditure by purpose

Analysis of water operating expenditure shows a reduction per property served in 2002/03 of over 5% in real terms, compared with last year.

Total water service operating expenditure for the year was £113.0m, a comparison with last year and the Final Determination is shown in Table 2.

Capital expenditure

At the end of the third year of AMP3 the Company had broadly met its key output targets. One area where we have previously reported being behind target is the

Table 1 - Operating expenditure by principal contracts

£000

United Utilities (Operations)	92,757
Thames (Customer Contact)	19,199
Severn Trent (Labs & sampling)	7,977
Various (Sewerage Network)	9,847

<i>Table 2- Operating Expenditure Water Service (£m)</i>	<i>Ofwat allowance for 2002/03 – FD (Outturn)</i>	<i>Previous Year Opex 2001/02 (Outturn)</i>	<i>Actual Year Opex 2002/03 (Outturn)</i>
Base	103.6	111.7	106.7
Enhanced Service	0.0	0.3	0.3
Supply & Demand & IDOK	1.8	0.9	1.8
Quality & IDOK	2.4	3.5	4.2
Total Water Service (£m)	107.8	116.4	113.0

mains replacement programme, where, because of restrictions imposed by the Foot and Mouth Disease outbreak in 2000/01 we agreed a reprofiling of our undertaking with the DWI.

During the report year we refurbished some 433km of water mains under the S19 Undertaking and are making good progress against the reprofiled programme. Water service capital expenditure for the year was £72/property the same as reported for 2001/02.

A breakdown of capital expenditure during the reporting year is shown in Table 3.

In 2002/03 we delivered the following major outputs from our Water Service investment programme:

- **Water treatment works:** 35 schemes completed achieving the target for the year of 35. Schemes which were delayed at six sites due to Foot and Mouth disease and planning constraints have now been completed. Work has been focused on compliance with quality requirements including removal of lead and cryptosporidium.
- **Water mains programme:** 433km of water mains refurbished to improve water quality and reliability of supply. We are making good progress to catch-up the slippage in the programme caused by access restrictions during the foot and mouth outbreak in 2000/01 and we are on target to deliver the revised S19 Undertaking.

<i>Table 3 Capital Expenditure by Purpose Water Service (£/M)</i>	<i>Ofwat allowance for 2002/03 in Final Determination (Nov 99 assumption)</i>	<i>Previous Year Capex 2001/02 (Outturn)</i>	<i>Actual Year Capex 2002/03* (Outturn)</i>
Base - Infrastructure	23.2	26.9	29.8
Base - Non Infrastructure	29.1	28.7	39.3
Enhanced Service	0.0	0.1	0.0
Supply & Demand & IDOK	15.2	7.5	10.8
Quality & IDOK	25.1	31.0	27.0
Total	93.1	94.2	106.9

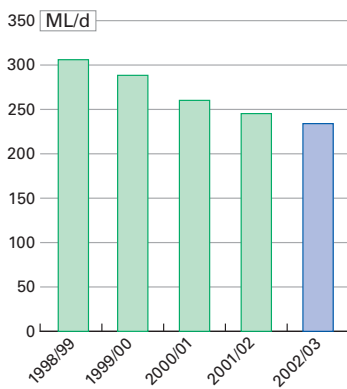
** Total Capex for water and sewerage (2002/03) was £271 million gross of infrastructure contributions.*

- **Meters:** Some 30,595 unmeasured customers have switched to measured charging in the year. 27177 customers received meters and a further 3,418 former unmeasured customers switched to paying on an Assessed Measured Charge (AMC).
- **Leakage reduction:** Leakage identification and prevention work has achieved a reduction of average leakage per day from 245MI to 234MI this year.
- **New assets for new development:** 70km of new water mains to serve new development.
- **Water supply asset maintenance:** Investment to maintain the performance of water treatment works, service reservoirs, impounding reservoirs, water pumping stations and water mains at over 260 sites.

Table D requires the Company to identify any water treatment works where maintenance investment in the year has exceeded 25% of the MEA value of the work.

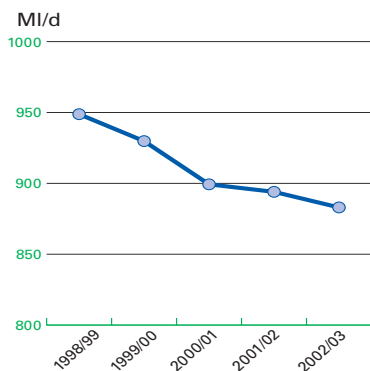
29

Total Leakage ML/d



30

Distribution Input ML/d



This threshold is too high and does not reflect the amount of capital maintenance actually carried out by the Company.

During the reporting year we have carried out capital maintenance at 87 of our 105 water treatment works, with 25 works having more than £100k invested during the year and of these 3 works had over £500k invested. Only on 1 small water treatment works did expenditure exceed 25% of the MEA value (Pilleth Bleddfra 0.2ML/d).

Maintenance work has also been undertaken at 111 service reservoirs and 70 water pumping stations during the report year.

Expenditure in excess of 25% of the MEA value of individual assets is reported on 1 service reservoir and 21 pumping stations.

During the year we renewed a total of 274km of water mains, which includes 214km of water mains renewed to meet the DWI S19 undertaking and 60 km renewed under prime purpose maintenance, and we relined 219km of unlined iron water mains. In the first three years of AMP3, relining has accounted for some 36% of the S19 mains refurbishment programme.

Leakage

Last year we made further progress to reduce leakage in our region. The annual leakage figure for the reporting year is 234ML/d, which is 1ML/d below the Ofwat target for 2002/03.

The rate of leakage was 8.7m³/km/day, down from 9.1m³/km/day

in the previous year.

Our leakage performance is in line with the rest of the sector, although in a number of resource zones leakage remains above estimated Economic Level of Leakage (ELL) and work is under way to reduce leakage further. 29

Distribution input and water delivered

Mainly as a result of leakage reduction, we have reduced the amount of water we need to abstract by around 10% since 1998.

The average distribution input for 2002/03 was 883ML/d. During the reporting year we have carried out a programme of work to verify the accuracy of meters measuring input to the distribution system and this too contributed to the lower leakage figures reported. 30

30

Metering

During the year an additional 30,595 customers have chosen to switch to a measured charge saving an average of 57% on their previous unmeasured bill. We have processed over 42,000 meter surveys resulting in 27,177 meters being fitted during the report year.

In addition, 3,418 customers have switched to an Assessed Measured Charge (AMC), where it has been impractical to install a meter unit.

Since April 2000 we have undertaken over 121,000 customer surveys and installed some 78,000 meters. Including AMC's a total of over 84,000 customers have switched from an unmeasured to a measured charge.

Over 14% of our customers are now receiving a measured charge for their water supply, which is slightly higher than Ofwat's assumption in the Interim Determination (IDOK 2000).

GSS – Payments

The total number of GSS payments made by the Company in the reporting year relating to the water service, both automatically generated and claimed was 32 (excluding Enhanced GSS).

GSS payments are categorised as follows

<i>Reason for GSS Payment</i>	<i>No.</i>
Planned Interruptions:	22
Unplanned Interruptions:	10
Total	32

Sewerage

Operating expenditure by purpose

Analysis of sewerage operating expenditure shows a slight increase in cost per property served in 2002/03, compared with last year because of additional costs arising out of the capital investment programme.

Total sewerage service operating expenditure for the year was £93.9m. A breakdown is shown in Table 4.

Capital expenditure

Total sewerage service capital expenditure for the year was £160m. A breakdown is shown in Table 5

Capital works activity

We are currently on target to achieve the agreed regulatory outputs within the overall capital

<i>Table 4 Operating Expenditure Sewerage Service (£m)</i>	<i>Ofwat allowance for 2003/023– Final Determination (Outturn)</i>	<i>Previous Year Opex 2001/02 (Outturn)</i>	<i>Actual Year Opex 2002/03 (Outturn)</i>
Base	65.7	72.8	71.5
Enhanced Service	0	0.2	0.3
Supply & Demand	1.5	0.3	0.5
Quality & IDOK	21.0	17.0	21.6
Total Sewerage Service	88.2	90.3	93.9

<i>Table 5 Capital Expenditure Sewerage Service (£m)</i>	<i>Ofwat allowance for 2002/03 – Final Determination (Nov 99 assumption)</i>	<i>Previous Year Capex 2001/02 (Outturn)</i>	<i>Actual Year Capex 2002/03 (Outturn)</i>
Base - Infrastructure	14.8	16.3	26.4
Base - Non Infrastructure	20.6	23.9	41.3
Enhanced Service	1.1	2.6	8.3
Supply & Demand	5.7	5.8	4.4
Quality + IDOK	104.2	61.8	79.6
Total	146.4	110.4	160.0

** Total Capex for water and sewerage (2002/03) was £271 million gross of infrastructure contributions.*

investment allowance included in the Final Determination.

Last year we delivered the following outputs from our Sewerage Service investment programme:

- **Wastewater treatment works:** 23 identified quality outputs of which 12 are identified on the NEP to be completed in the report year and 11 are scheme outputs completed early.
- **Sludge:** Continuing work at 28 centres across Wales to increase capacity by 20% and meet tighter standards.
- **Section 101a:** 21 schemes completed. On target to complete 25 schemes by the end of 2003/04. Four projects are

delayed due to land issues and an additional 4 projects have been scheduled for delivery by 2005.

- **CSOs:** 205 schemes completed. Major works undertaken at Merthyr, Afan, Ogmere, Rhondda Amman, and Western Valley sewers.
- **Sewer flooding:** Removed 95 properties from the "at risk register" as a result of company action.
- **New sewers and other sewer refurbishment:** 69km of new sewers laid and 63km of sewers refurbished in the year. A programme of CCTV surveys is being undertaken ahead of further investment.

- **Asset maintenance:** Work carried out at over 350 sites to improve asset quality and serviceability and ensure compliance with consents.

In the year we have dealt with 205 unsatisfactory CSOs identified under the AMP3 programme; we are now 43 outputs ahead of the 2002/03 year-end target agreed as part of the NEP programme.

During the year we have made a further assessment of the total number of active intermittent discharges on the Company's database. We are working closely with the Environment Agency (Wales) to assess newly identified discharges.

The total length of critical and non-critical sewer renovated or replaced during the year was 63km.

Through savings identified in the overall capital investment programme we have added additional outputs to our original AMP3 programme, including £23m to remove an additional 250 properties from the sewer flooding "at risk register" and £6m to support our plans to secure 100% compliance at our WWTWs.

The total sludge disposed of during the reporting year was 83ttds. All sludge was disposed of satisfactorily and 67.8% was treated to the enhanced standards.

Table D requires the company to identify any sewage works, intermittent discharges, sludge treatment works, pumping

stations and sea outfalls where maintenance investment has exceeded 25% of the Modern Equivalent Asset Value (MEA) of the asset. However, this is an extremely high threshold and is unlikely to reflect the amount of capital maintenance carried out by the Company.

During the report year we have carried out over 1100 maintenance projects each with a value over £1,000 across all of our 846 sewage treatment works. Of this total, 800 projects, with a combined value of £2.73m, were reactive maintenance work.

In addition during the year we have invested over £3m in other "low cost" reactive maintenance work with individual project values less than £1,000.

Sustainable Procurement

Dwr Cymru supports the principles outlined in the British Water "Guide to Sustainable Procurement" and the Confederation of Construction Clients "Charter".

We are committed to adopting a best practice approach to our procurement activities and supply chain management processes.

Our procurement processes will reflect those principles and practices aimed at enhancing the sustainability, efficiency and effectiveness of the supply chain.

We currently operate in an alliance with key service delivery partners. Extensive use is made within the Capital Alliance of the European Forum for Quality

Management Business Excellence Model. This framework supports the development and deployment of continuous improvement activities across Dwr Cymru and its partners under five key elements (enablers)

- Leadership
- People
- Policy & Strategy
- Partnerships & Resources
- Processes

The model has also led to the development of a holistic suite of Key Performance Indicators (KPIs) that demonstrate sustainability and continuous improvement across customer and supply chain alike.

The Capital Alliance Strategic Group (Board of Management) has reviewed the British Water "Guide to Sustainable Procurement" and endorsed its objectives and principles. In addition the Capital Alliance has been recognised by the construction industry through its acceptance as a demonstration project for Rethinking Construction (and Movement for Innovation). This demonstration covers two specific areas namely

- Process – Partnering & Project Implementation
- Organisational Change (covering collaborative relationship development within and between the customer and its supply chain)

It also links the Company and its partners to the Rethinking Construction Charter that closely reflects the principles of the British Water Guide.

Chapter 4:

Efficiencies

Operating efficiencies

Dŵr Cymru's operating costs are 6.5% lower in real terms compared to 1997/98 levels.

Operating costs for the year were £206.9m (excluding exceptional items), which is in line with our published forecasts but some £10.8m higher than the figure assumed in the Final Determination

Allowing for inflation and the operating cost impact of new treatment works this represents an improvement in underlying base cost efficiency of around 5% in real terms as compared to 2001/02.

Capital efficiencies

Dŵr Cymru undertook a thorough review of the capital investment programme following the change of ownership in May 2001. The published target for delivery of the AMP3 capital expenditure programme is £1,175m before capital contributions. This assumes additional efficiency savings compared to those assumed in the Final Determination in the order of 5%. Dŵr Cymru's Capital Alliance is working well and good results have been achieved to date. Delivering the AMP3 capital investment programme on time and within budget remains a key challenge for the Company.

Chapter 5: Competition

Dŵr Cymru Policy

Last year, the Government consulted on its proposals for extending competition in the water industry. These proposals were contained in the Water Bill which was introduced into Parliament in February 2003.

We support the Government's proposals. In particular, we welcome the recognition that the water and sewerage business is an essential public service, and that a balance has to be struck between development of competition and other Government objectives, including quality and affordability.

Competitive procurement

The performance of our service partners undertaking the outsourced asset operation, customer billing and contact centre management continues to deliver improved results.

These contracts were awarded following a highly competitive process and provide strong incentives for cost efficiency and quality of service delivery against KPIs and stretch targets.

The Capital Alliance, which undertakes delivery of the AMP3 capital investment programme, is continuing to deliver good results

A regional based reorganisation has taken place to enhance working efficiency and assist in the sharing of best practice across the alliance.

Preparations have commenced for the competitive re-tendering of the main service delivery contracts, asset operations, asset investment, income and billing, IT

and sampling and laboratories.

The new arrangements will take effect from 1 April 2005 and will provide support for AMP4 and beyond. We will continue our current practice of establishing strongly incentivised contracts which reward our partners for delivering sector leading performance and our procurement strategy is designed to ensure we enable the most capable and competent operators in the marketplace to deliver the best combination of value for money and quality of service for our customers.

It will also deliver predictable costs and transparent market pricing which will provide an additional source of regulatory information.

Network access

Dŵr Cymru's Network Access code was published in August 2000. It was not updated during the reporting year.

Inset Appointments

There has been no activity relating to new inset appointments during the reporting year.

Chapter 6:

Board Endorsement

On 6 June 2003, the Board of Dŵr Cymru duly endorsed this Overview of the June Return 2003. The Reporter attended the Board Meeting for this matter.