

# Business Review

## Financial Performance

Profit before tax for 2006 increased by 15% over 2005 to £2.8 million as a result of the combination of the effect of increased revenue from both water and non water sales and efficiency savings offsetting the cost of running the desalination plant during the year.

Retained profit for the year stood at £1,318,000 (2005: £744,000) and earnings per ordinary share were increased by 13% to £4.94 (2005: £4.38).

Revenue from water totalled £12.4 million in 2006, an increase of 2.7% on the prior year. The increase being attributed to a (below inflation) tariff increase in April 2006 of 1.95%, the addition of 1,001 new connections during the year and the dry weather over the spring and summer having a favourable effect on metered water income.

Rechargeable works income increased from £468,000 in 2005 to £864,000 in 2006 primarily due to the significant increase in the number of connections to the water network during the year.

Cost increases were held at 4% for the year despite the cost of £242,000 running the desalination plant for nearly three months in the summer, an increase of 10% in the cost of electricity from 1 January 2006 and the cost of meeting the demand for new connections. The project to convert meters to the electronically encoded type was substantially completed in 2006 resulting in a reduction of £92,000 in year on year expenditure. The continued expansion of the Company's telemetry network permitted further reductions in staff numbers through natural wastage with consequent productivity savings.

Further sales of surplus assets including the old St Peter's Booster Station and land in St Peter's Valley netted capital gains of £469,000, a little less than in 2005. The Company continues with the process of disposing of surplus land as and when it becomes redundant.

The income tax charge for the year has increased by 28% to £412,000 primarily due to the higher levels of taxable income arising on rechargeable works.

Dividends paid during 2006 totalled £1,070,000, compared to £1,372,000 in 2005. The implementation of FRS 25 in 2005 requires dividends to be accounted for in the period in which they are paid or become a liability, rather than when they are declared. The effect of this change in treatment coupled with the switch in 2005 to the Company's current dividend policy has caused the apparent reduction in dividends year on year. As shown in the table within the Directors' Report on page 17, actual dividends, paid and proposed for 2006, total £1,104,000, an increase of 5% over the prior year dividend of £1,051,000.

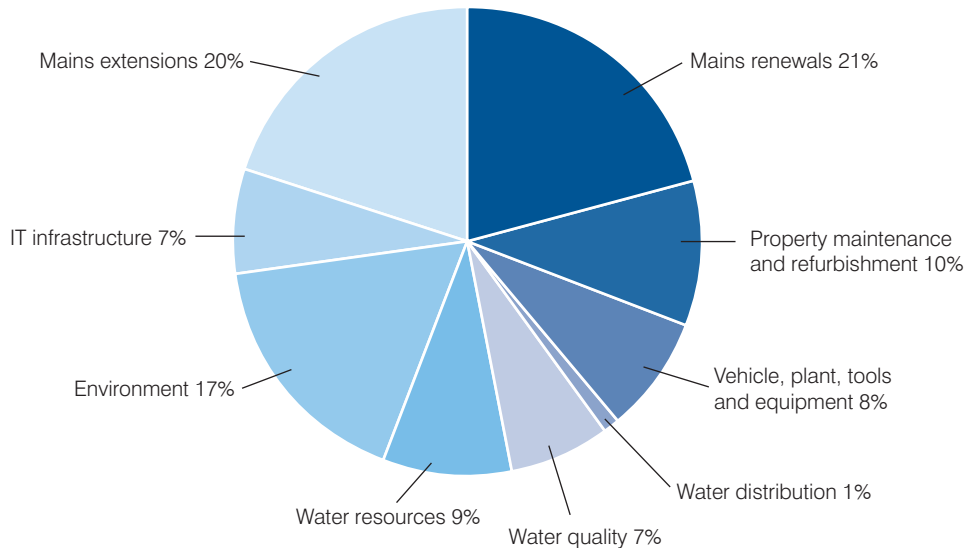
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During 2006 the Company made contributions totalling £588,000 into the defined benefit pension scheme (which has been closed to new members since January 2003). The actuarial valuation of the scheme as at 31 December 2006 shows a deficit net of tax of £2,000,000 compared with the deficit of £3,080,000 in 2005 an improvement mainly due to higher corporate bond yields at the year end (on which the FRS 17 present value of the scheme liabilities is based). Corporate Bond Yield rates do vary and these variations can have a material effect on the valuation of scheme liabilities. Whilst the results are positive they should not be taken as an indication of a permanent improvement in the level of the scheme's deficit. A review is currently underway into the future options for the scheme.

The Company generated net cash inflows of £550,000 during the year compared to outflows of £326,000 in 2005. Net debt at the year end stood at £20,009,000 compared to £20,559,000 in 2005.

## Business Review (continued)

### Capital expenditure by type



In 2006, capital expenditure totalled just under £3.0 million in line with the budget for the year. An analysis of the expenditure is provided in the chart above. Looking forward the Company expects to continue with annual capital expenditure in the region of £2.5 million (at current prices).

#### Connections, metering and charges

The recent surge in Jersey home building had the effect of increasing the number of new connections to the treated water network by 60% over 2005 levels. With 1,001 new connections during the year the level was 50% over the 10 year average connection rate. Whilst the number of connections is not expected to continue at this level, it will be dictated by the pace at which new buildings continue to be constructed and, in the longer term, by the policies for population growth implemented by the States of Jersey.

At the end of 2006, Jersey Water had 9,800 live metered connections to its network and 26,600 unmetered dwellings on supply. During 2006, 269 customers made the decision to switch from paying for water on an unmeasured basis to a measured (metered) basis.

The Company encourages customers to switch to paying for water by meter by offering free installation of a water meter and during the last five years has applied differential tariff increases which have reduced the cost of metered water by 7% in real terms over that period.

Jersey Water will be undertaking trials of a fixed network automated meter reading system which would allow water meters to be read using low frequency radio technology to collate meter readings remotely from across the Island. If successful, the system would significantly reduce the need for manual meter reading and could facilitate the future introduction of more widespread metering, for example on change of ownership of a property.

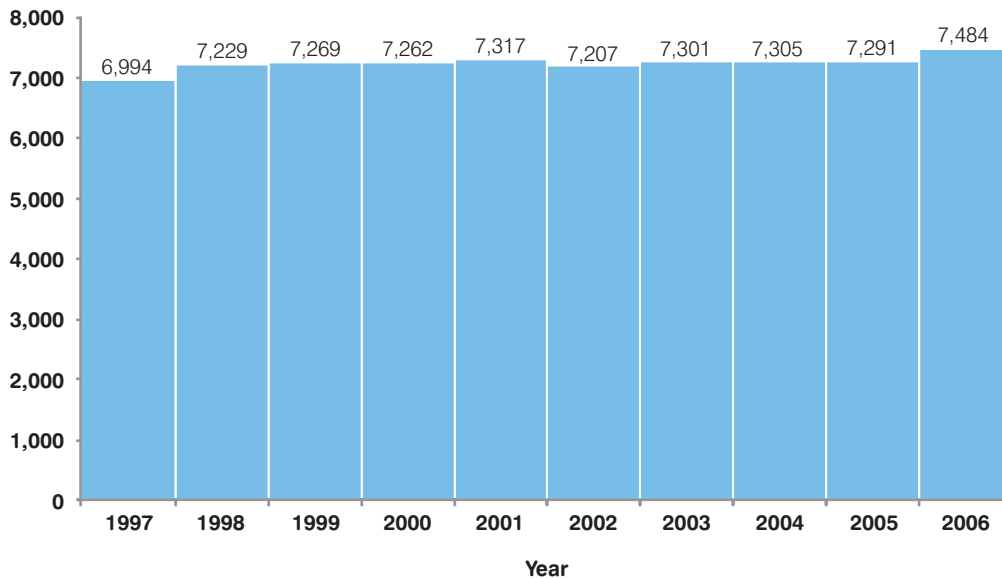
In December 2006, the Company announced tariff increases (based on the September RPI index) effective in April 2007 whereby metered water charges will increase by 2% and unmetered charges by 3.6%. The overall effect of the tariff changes on turnover for 2007 is expected to be an increase of 2.1%. The policy of keeping tariff increases broadly in line with the increase in the Jersey retail price index (RPI) continues.

## Business Review (continued)

### Water supply and demand

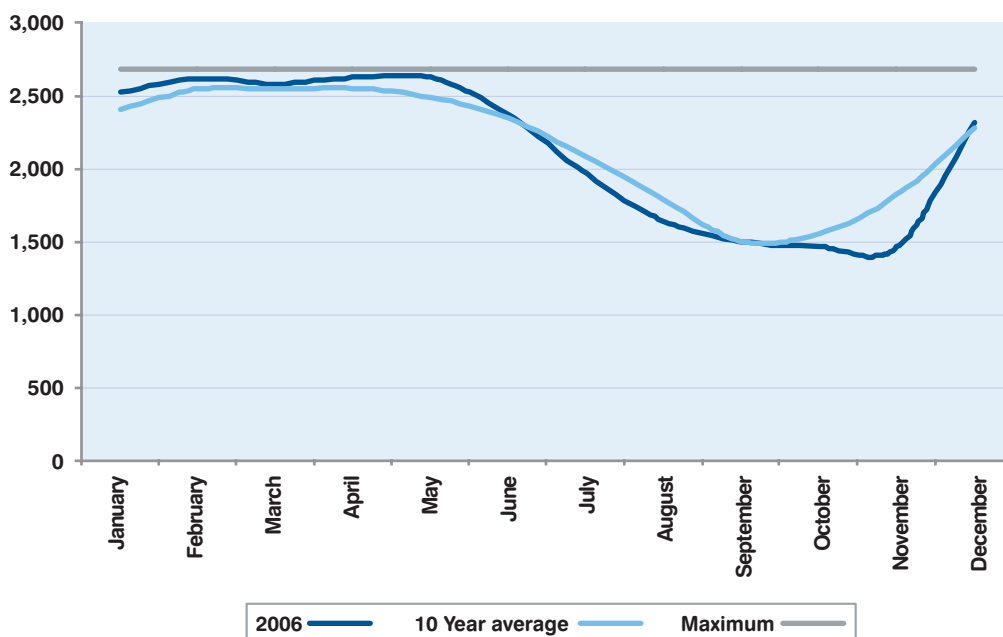
Demand for water during 2006 totalled 7,484MI (2005: 7,291MI), an increase of 2.6% over the previous year but in line with expectations during a year with relatively long dry periods.

**Total water supplied by year (MI)**



Water levels in the reservoirs started the year at 94% full, reached capacity in March and remained at near full capacity until May. Thereafter demand for water exceeded the rate of replenishment and reservoir levels continued to decline until December when we enjoyed rainfall some 32% above the ten year average; this lifted levels in reservoirs from 55% to 86% full.

**Water in store (MI)**



## Business Review (continued)

2006 was a predominantly dry year, with annual rainfall 11% below the long term average. Only February, March, September and December had rainfall levels at or above average levels. This resulted in steadily reducing stream flows throughout the spring and summer as the ground water dried up.

The lack of rainfall coupled with summer temperatures 3°C above the long term average resulted in daily demand peaking at 28.9MI in July 2006 (average daily demand for 2006 was 20.5MI). The Company ran a 'Use Water Wisely' campaign to raise awareness of the need for water conservation incorporating, for the first time a radio campaign promoting water saving tips and ideas. The national press coverage of water shortages in the South East of England helped to raise the issues of water conservation further. The aim of the Company's campaign was to reduce the volume of water consumed by garden watering which can account for up to one third of daily demand in the spring and summer months.

In August, the Desalination Plant was brought into action as a precautionary measure to protect against the risk of lower than average rainfall levels in the late summer and autumn. The plant ran until November and produced 397MI of water.

During 2006, the Company took delivery of new computer software which will enable the effect of variables including rainfall patterns, temperature and population to be modelled and will assist us in managing water resources by providing information on the various drought return periods which are the basis for water resource planning.

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### Water Quality

During 2006, the Company took 18,382 regulatory samples for physical, bacteriological and chemical analysis. Of these, only 6 samples exceeded the Maximum Allowable Concentrations (MAC) set out under the law. Full details of the quality of water supplied are shown in the 2006 Water Quality Report.

Water quality for 2006 was also in line with the requirements set out in the Water Supply (Water Quality) Regulations 2000 for England & Wales and in 2006 we achieved 99.97% compliance, slightly above the most recent England and Wales average of 99.96%.

During the year only 3 out of the 100 regulatory samples taken for nitrate were above 50mg/l limit, the highest being 51.4 mg/l. The low occurrence rate of nitrates can be attributed in the main to the rainfall pattern during 2006. The months when nitrate levels are traditionally high were drier in 2006 than normal resulting in less nitrates being washed off the fields into the Company's raw water sources.

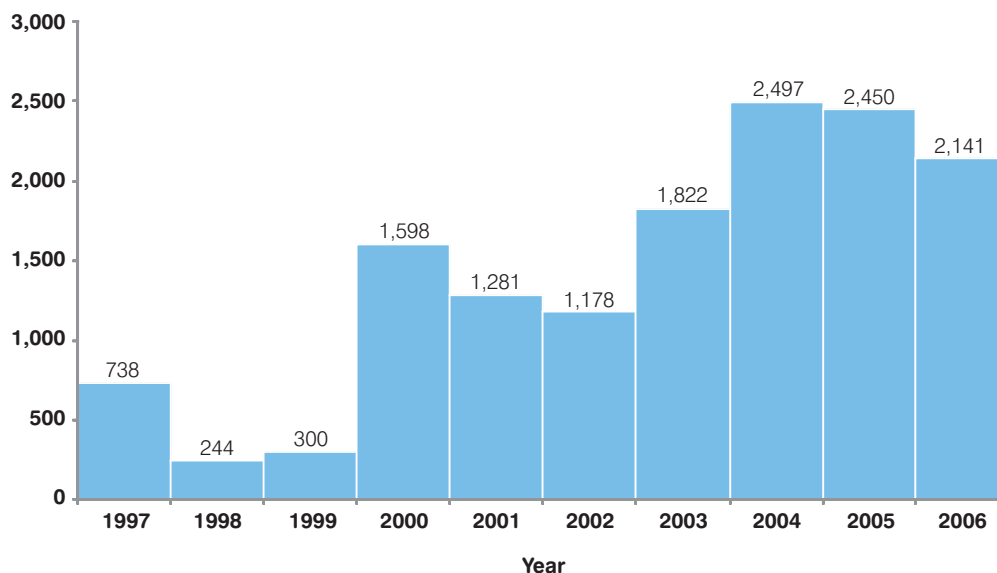
The Company has no control over catchment areas and the diffuse pollution of water resources from nitrate and other agricultural chemicals and will continue to need dispensations under the law. The Company remains an advocate for action by the States to introduce Water Catchment Management Areas under the Water Pollution (Jersey) Law to help reduce nitrates in streams and generally improve the quality of the Island's water resources. We understand that the introduction of the proposed Water Resource (Jersey) Law is required to enable this to be put in place.

### Mains network

In 2006 the Company renewed 2.1 km of old water mains, just short of the 2.5 km target for the year. The complex nature of the work makes the renewal of mains and services time consuming and costly. This is especially true in and around St Helier where the volume of underground cables, pipes, ducts and other apparatus is such that much of the work requires hand excavation.

## Business Review (continued)

### Mains renewals by year (Metres)



In the years to come, the Company plans further work on renewing old water mains and service connections in the St Helier town area, with a target of roughly 2.5km per annum. Inevitably, this necessary work brings short-term disruption to road-users and residents. Wherever possible we work in conjunction with the road authorities and other utilities to minimise the overall disruption.

During the year, the treated water mains network was extended by 6.5 km. Of this 3.5km was funded by developers wishing to bring treated water to property developments and the balance funded by the Company.

Due to the economics of extending the treated water mains network into the more sparsely populated areas of the Island coupled with the need to concentrate efforts and resources on the renewal of existing water mains it is expected that in the next five years only 5.6km of Company funded mains extensions will be laid. Whilst the extensions will bring mains water to some areas not yet supplied, the main purpose of these future extensions is to reinforce the existing treated water network, rationalise the system and connect those areas currently supplied with pumped water to the gravity fed distribution system, reducing the Company's energy usage and leakage.

In 2006, Jersey Water suffered only 14 bursts on the mains network. A review of the rate of bursts experienced in Jersey indicates that it is some 70% below the average rate in England & Wales. The difference being due partly to the Company's relatively modern water network and also the favourable ground conditions in Jersey.

The Company continues to make advances in dealing with leakage and during 2006 installed 3 district meters, which allow discrete areas of the Island to be monitored and tested for leaks. The Jersey Water leak detection team identified and reported 343 leaks (which were predominantly on customer pipe work). The use of pressure reducing valves at key locations around the Island helps to reduce the flow of water lost through leakage. A review undertaken during the year indicates that the leakage rates in Jersey are at least as good as those for Water Only Companies in England & Wales and significantly better than those for Water and Sewerage Companies.

## Business Review (continued)

### Treatment and processing

In October, the wash water pumping station at Augrès water treatment works was commissioned. This new plant, together with the new 4km connecting transfer pipeline, allows the wash water from the clarifiers and filters at Augrès WTW to be transferred to Handois for treatment at the Company's wash water recovery plant.

The Jersey Water Operational Supervisory & Data Acquisition (SCADA) system was further developed during the year to include remote control and monitoring of Augrès WTW and La Rosière Desalination Plant, allowing the productivity savings mentioned above. To improve site security, closed circuit TV systems have also been installed at Augrès WTW and La Rosière Desalination Plant with real-time images being transmitted by the SCADA network to the central control room.

### Investors in People

During 2006, the Company attained the "Investor in People" award, which recognises the management systems and processes in place throughout the organisation. In addition, the Company's leadership training program has for the second consecutive year resulted in a number of Managers and Supervisors obtaining their NVQ in team leadership and management skills.



Constable Geoffrey Fisher (left) presents the Investor in People award to Howard Snowden (right).