Chairman's statement

2006 was another successful year for the Company in terms of both strong growth in earnings and cash flow, and expansion by acquisitions and greenfield developments. The business is well placed for further growth in 2007.

Last year I said we expected 2006 to be a year of further growth and I am glad to report that it was. In 2006 our profit from operations* increased significantly from £536 million in 2005 to £773 million, an improvement of 44% and earnings per share* (EPS) increased from 14.6p to 22.4p, an improvement of 53%. In addition, free cash flow increased by 60% from £285 million in 2005 to £456 million in 2006.

In 2004, when we announced our first dividend payment, we stated that our dividend policy was to commence paying a dividend representing a pay-out ratio of 30% of pre-exceptional EPS progressing towards a pay out of 40% in the medium-term. This year the Board is proposing a dividend of 7.9p per share which reflects a pay-out ratio of 35%*, and an increase of 75% on last year's payment.

The financial results reflect the good operational performance of our assets, the improvement in the UK and US merchant markets and the continued growth of the business. In 2006 we completed the acquisition of a 40% interest in the 910 MW and 30 MIGD (gross) Hidd power and water plant in Bahrain, the coal fired 632 MW Coleto Creek power station in Texas, the 140 MW Indian Queens oil fired peaking plant in Cornwall, UK and the 436 MW Levanto wind farm portfolio, which has wind farms that are currently operating or under construction in Germany and France plus further potential growth from a pipeline of development opportunities. These acquisitions all met our financial criteria whilst fitting in with our strategic aims. The Hidd acquisition continued our growth in the Middle East in a new market for us – Bahrain. Coleto Creek increased our presence in Texas and added good fuel diversification. The Indian Queens peaking plant increased our ability to provide system support. Levanto represented our first major renewables business in Europe and, in addition to providing fuel diversification, gives the business immediate scale and credibility in this increasingly important area of electricity generation.

- Profit from operations* of £773 million (2005: £536 million) – up 44%
- EPS* of 22.4p (2005: 14.6p) – up 53%
- Free cash flow of £456 million (2005: £285 million) – up 60%
- Dividend per share of 7.9p proposed – up 75% from 4.5p in 2005

* Excluding exceptional items and specific IAS 39 mark to market movements.

The successful growth that has taken place in the last few years is testament to the strong leadership of the Chief Executive Officer, Phil Cox, and his executive team and the professionalism and efforts of all the Group's employees. On your behalf I would like to thank them all for their contribution to the continued success of the Company. Whenever I visit our assets (and in 2006 I visited plants in Australia and the Middle East), I have been very impressed by the enthusiasm demonstrated by the employees for our business and the obvious pride they all take in their work.

We take our commitment to safety very seriously. One of our core values is to instil safe behaviour in everything we do. We therefore decided to ask DuPont, an acknowledged world authority in this field, to carry out a safety review at a selection of our assets around the globe to ensure that our commitment to excellent health and safety standards, across our portfolio, is checked and challenged and that best practice is shared by all our plants. Health and safety is of vital importance in our business and therefore the accident frequency rate is one of the non-financial key performance indicators we use in managing our business.

Once again, I would like to express my thanks to our Non-Executive Directors, whose guidance, challenge and support continues to be invaluable. During the year there were changes at Board level. Following the retirement of Jack Taylor, as a Non-Executive Director, at last year's Annual General Meeting, John Roberts, formerly Chief Executive of United Utilities plc, has been appointed as a Non-Executive Director. John brings related power industry and international experience to the Board and has already made a positive contribution to the business.

Our broadly based international portfolio has been strengthened by the successful integration of acquired assets and the addition of new greenfield projects commissioned in 2006, and provides a solid platform for our business. This, coupled with a largely forward contracted position for our merchant capacity, gives us confidence that 2007 will be a year of further growth. We will continue with our disciplined approach to pursuing value enhancing growth opportunities in our core regions, alongside our commitment to increase our dividend pay-out ratio over the medium-term.

Sir Neville Simms
Chairman