Chief Executive Officer's statement

Dear Shareholder,

I am pleased to report earnings per share (before exceptional items) in line with our earnings guidance for 2003, but I recognise that 2003 was the difficult year we anticipated, with profits down on last year – principally due to low prices for wholesale power in two of our key markets, namely the US and the UK. The fact that we did deliver on our earnings guidance is a testament to the strength of our global portfolio.

The Operating and financial review that follows in this report will give you a full explanation of our regional performance. There were many success stories. Our European assets (outside the UK) had another excellent year, with EOP in the Czech Republic delivering a record performance and our contracted assets in Portugal and Turkey achieving high levels of availability that resulted in good financial results. This was balanced against our performance in the UK, where trading conditions remain difficult, with low margins for wholesale power generators. Our Middle East business, which is underpinned by long-term off-take contracts, continues to grow profitably, with the acquisition of the Umm Al Nar power and desalination plant in Abu Dhabi. In Australia, the strength of our contracted position has maintained financial performance in a year when underlying market prices were somewhat weaker. Our assets in the Rest of the World, namely in Malaysia and Thailand, had excellent years. In Pakistan the agreements reached in 2000 have stood firm, and we continue to be paid in full and on time.

We have also taken steps to strengthen our capital structure by issuing a new convertible bond, and by renegotiating and renewing our Corporate bank facility. These steps provide additional security and flexibility to our capital structure.

Looking forward, we have many opportunities and some challenges, all of which I believe we are well equipped to deal with. Our principal challenge is the US business, where the clear objective is to preserve value for our shareholders. A wide range of options are currently under review. The fundamental issue is oversupply, and it will probably take some time for the supply/demand imbalance in our US markets to be corrected. We are taking active steps to manage this position, including a reduction in our cost base, selective mothballing of plant that is uneconomic to run, and the renegotiation of our non-recourse project debt. At this stage, we cannot predict with certainty the outcome of these negotiations, but we remain focused on minimising the financial demands on the Group, whilst recognising the upside value from future market recovery. We have also taken a prudent view on the balance sheet value of our US merchant assets, and have written down their value by £404 million at the year end, based on our view of their long-term cash flows. Weak market conditions in the US is the sole reason our earnings guidance for 2004 is lower, with an EPS range of 7p to 9p.

We continue to be very active in reviewing growth opportunities, both in our existing merchant markets and in those that provide secure long-term contracts. Let me give you two examples. The low wholesale price environment means that selected merchant assets in both the UK and the US are potentially available at a discount to original cost, providing an opportunity to add value, scale and complementary assets in our core markets. Secondly, as an investment that will significantly increase our long-term contracted position, we announced in December 2003 that we will build four power stations in Saudi Arabia with a total capacity of 1,074 MW, all of which are fully contracted to Saudi Aramco, one of the largest oil and gas companies in the world. These plants will start operating during 2006. We continue to review further opportunities in the Middle East. Our investment criteria remain stringent and we will use your capital carefully.

We take our environmental and community responsibilities very seriously, and the corporate social responsibility section of this report will give you some practical examples of our commitment. We also announced in early 2004 our first wind farm development in Australia, and we continue to develop the capability to use more environmentally-friendly fuels in our UK coal-fired plant.

The senior management team and I have a clear vision of the future for your Company. Our strategy remains to create value through wholesale power generation in our core regions, and we have the people, the resources and the determination to ensure we deliver for the benefit of all our shareholders and stakeholders.

Philip Cox
Chief Executive Officer