Investor Report

For the quarter ended 31 December 2020

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References to the “Company”, “Dŵr Cymru” and “Welsh Water” in this document relate to Dŵr Cymru Cyfyngedig, the sole operating company in the whole business securitisation formed by the Glas Cymru Anghyfyngedig group. References to “Glas Cymru” and the “Group” refer, respectively, to Glas Cymru Anghyfyngedig and the group of which it is the parent.

Contents

General overview and business update

This quarterly Investor Report covers the nine-month period ended 31 December 2020. The Investor Report has been prepared to comply with the specific requirements of the Common Terms Agreement (CTA) which governs the Company's obligations to its bondholders and other financial creditors.

The financial information in this report is drawn from the Company's accounting records, applying the accounting policies as per the Company's statutory accounts, but is presented in a modified form for investors as required by the CTA.

Financial performance (unaudited)

Summary financial results for the nine months ended 31 December are as follows:

	9 months to 31 December 2020 £m	9 months to 31 December 2019 £m	Change %
Turnover	583	592	(2%)
Operating costs	(239)	(241)	(1%)
Exceptional item	(21)	-	
EBITDA (before infrastructure renewals expenditure)	**323**	**351**	(8%)
Net interest (excluding indexation)	(90)	(78)	
Capital expenditure (before grants and contributions)	(281)	(349)	

Operating profit before interest, tax, depreciation, amortisation and infrastructure renewals expenditure (EBITDA) for the nine months to 31 December 2020 was £28 million lower than the comparative period last year.

Revenue in the nine months to 31 December 2020 was £9 million lower than last year, principally as a result of reduced overall water usage during the lockdowns as well as the temporary suspension of standing charges for business customers deemed non-essential and ordered to close during that period (note that Ofwat's revenue cap mechanism allows under-recoveries of revenue to be recovered in future years).

Operating costs (excluding depreciation, amortisation, infrastructure renewals expenditure and exceptional items) of £239 million were £2 million (1%) lower than the same period last year reflecting inflationary increases being more than offset by savings as a result of a move to homeworking for many employees, along with a lower underlying bad debt charge and ongoing savings from efficiency initiatives.

General overview and business update (continued)

Financial performance (unaudited) (continued)

Exceptional costs of £21 million represent additional expenditure incurred as a direct result of the COVID-19 pandemic which includes additional bad debt charges (£9 million); personal protective equipment (£6 million), deep cleaning (£2 million) and an additional levy from National Grid following a drop in national demand (£3 million).

Net interest payable in the period of £117 million (excluding fair value movements) was broadly in line with the prior period (2019: £115 million) including an indexation charge on index-linked debt of £27 million (2019: £37 million); lower RPI indexation has been offset by interest charges on a higher level of borrowings.

The regulatory gearing (the ratio of net debt to regulatory capital value) of the Group was as follows:

£m	31 December 2020	31 December 2019
Net debt	3,652	3,459
Regulatory capital value	5,994	5,855
‘Financial reserves’	**2,342**	**2,396**
Regulatory gearing	60.9%	59.1%

On Glas Cymru’s acquisition of Welsh Water in May 2001, gearing stood at 93%. Since then the financial position of the Group has improved steadily, such that gearing is 61% and ‘financial reserves’ (RCV less net debt) are £2.3 billion as at 31 December 2020. An increase in gearing by 1.8% during the 12 months to 31 December 2020 is mainly the impact of a higher level of debt being only partially offset by RPI inflation on the regulatory capital value.

Capital investment programme

Capital investment (including infrastructure renewals expenditure) before grants and contributions totalled £281 million during the nine months (2019: £349 million), £68 million lower than last year reflecting the start of the new five-year “AMP7” capital programme (the planning and delivery cycle is such that investment tends to be at its lowest in the first year and to peak in year five).

General overview and business update (continued)

Prospective financial ratio tests

As required by the CTA to demonstrate compliance with prospective financial ratio tests (regulatory asset ratio and interest cover ratios), this report includes projected ratios to 31 March 2025. These projected ratios are derived from Glas Cymru's 2021 draft financial plan (which has been prepared by the Group) and are in the format specified by the CTA. On this basis, the prospective financial ratios are better than the "trigger" and "default" levels as defined in the CTA (see pages 9 and 10). It should be noted that the Group's business plan and the projected ratios have not been reviewed by the company's auditor and the reader's attention is drawn to the important notice at the front of this document.

Impact of COVID-19 pandemic on projected ratios

The three Investor Reports we have published since the COVID-19 outbreak was confirmed as a pandemic by the World Health Organisation have contained narrative estimates of the impact of the pandemic on our financial forecasts. In this Report for the quarter ended 31 December 2020 we have included revised forecasts (on pages 9 and 10) which incorporate our estimates of the financial impact of COVID-19; as noted above, these have been extracted from Glas Cymru's 2021 draft financial plan which was reviewed by the Board in February 2021.

Our COVID-19 impact modelling has been informed by external reports including those by the Office for Budget Responsibility which published updated coronavirus analysis and reference scenarios on 25 November 2020. Our plan reflects a continuation of social distancing in early 2021 with gradual lifting of restrictions thereafter. Unemployment is assumed to peak at around 7.5% in 2021, recovering to pre-pandemic levels by 2025; CPIH falls to a low of 0.6% in November 2020 and recovers to the government's long-term target of 2% by the end of 2023. The estimated impacts on turnover in 2020-21 are a £27 million reduction in non-household revenues of £172 million (16%, demand-driven) partially offset by £6 million of increases in household revenues (1%, demand-driven) – a net reduction of £21 million (however under regulatory mechanisms lost revenues are recoverable in future years).

Consequential impacts on the Group's cost base are greater pressure on bad debts (£4-7 million per annum through to 2022-23) and delays in the delivery of cost efficiencies (circa £10 million in 2020-21), as well as further reductions in revenues.

Reduced cash flows will impact on key financial metrics, in particular interest cover ratios. However, forecast gearing and interest covers retain an appropriate level of headroom within the trigger levels specified in borrowing covenants and indicative levels required to maintain the Group's current credit ratings.

Gearing policy

The Board has approved a regulatory gearing policy (being the ratio of net debt to regulatory capital value) of around 60%.

General overview and business update (continued)

Customer rebates

On 5 June 2020 the Company announced that it will provide £11 million of contributions to social tariffs over the year to 31 March 2021 to its lowest-earning customers, helping nearly 130,000 customers with their bills. These customer rebates represent revenues foregone by the Company by not applying the full price cap on charges available to it.

Credit ratings

The strong credit quality of the business is reflected in credit ratings which remain the highest in the UK water sector. The ratings of the Company's bonds are shown in the table below:

Bond class	Moody's	S&P	Fitch
A[1]	A2	AA	A
B	A3	A-	A
C	Baa2	BBB	BBB+

On 26 January 2021 Fitch confirmed the rating of the Group's senior bonds as A and of the junior bonds as BBB+. On 21 September 2020 Moody's confirmed Dŵr Cymru Cyfyngedig's corporate family rating as A3 and the rating of the junior bonds as Baa2. S&P downgraded the senior bonds to A- on 7 February 2020 and, on 11 February 2020, assigned a BBB rating to the junior bonds. All rating outlooks are stable.

Financing and liquidity

As at 31 December 2020 the Company's undrawn credit facilities and cash totalled £769 million, including debt service payment funds (£80 million) and revolving credit facilities (£200 million). All of the Group's revolving credit facilities have been renewed during the current financial year, each for two years with a one-year extension option. Three of the four facilities have been increased by £10 million, increasing the total available from £170 million to £200 million. As at the date of this report all facilities remain undrawn.

In line with prudent policies approved by the Board, cash is invested in AAA-rated liquidity funds and bonds, National Westminster Bank (as the group's Account Bank) and additional banks that are subject to minimum short-term rating criteria of A1/P1/F1.

The Group also has an undrawn special liquidity facility of £135 million which is available to be drawn in the event of a standstill being declared by the Security Trustee. The facility is provided on a rolling five-year 'evergreen' basis.

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[1] The credit ratings of the Company's class A bonds, which are guaranteed by Assured Guaranty (Europe) plc ("AG") (A2/AA/NR), carry the higher of either Glas or AG's rating; Moody's and S&P therefore revert to the higher AG rating but Fitch reflects the underlying rating of the Glas bonds.

Consolidated cash flow (unaudited)

	3 months ended 31 December 2020 £m	9 months ended 31 December 2020 £m	9 months ended 31 December 2019 £m
Revenue	197.7	582.6	591.6
Less: operating expenses	(85.7)	(238.5)	(240.6)
Less: exceptional item	(4.2)	(21.0)	-
Earnings before interest, taxation, depreciation and amortisation	107.8	323.1	351.0
Working capital movements	1.1	3.0	20.9
Non bond-related interest paid	(1.0)	(3.4)	(4.6)
Interest capitalised in accordance with IAS 23	(5.7)	(13.2)	(14.4)
Interest received	1.3	4.2	4.5
Net operating cash flow and interest received	103.5	313.7	357.4
New borrowings:			
Lease liabilities	-	-	1.3
Intercompany loan	-	-	2.8
Utilisation of reserves:			
Cash transferred to capex reserve	(122.0)	(334.0)	(290.8)
Cash utilised from capex reserve	122.0	334.0	420.8
Net cash utilised from other reserves	3.7	10.2	9.0
Capital expenditure:			
Net profit on disposal of assets	-	0.1	0.2
Infrastructure renewals expenditure	(23.8)	(73.3)	(70.2)
Non-infrastructure maintenance	(42.9)	(123.6)	(151.5)
Capital expenditure	(29.1)	(95.2)	(121.8)
Net cash flow after capital expenditure, new borrowings and reserve drawings	11.4	31.9	157.2
Transfer to debt service payments account	(37.5)	(125.0)	(125.0)
Principal repayments	(14.7)	(54.5)	(36.7)
Net cash flow after debt service	(40.8)	(147.6)	(4.5)
Free cash balances brought forward	528.1	634.9	192.5
Free cash balances carried forward	487.3	487.3	188.0

Consolidated debt service payments (unaudited)

	Payments due and made in 3 months ended 31 December 2020 £m	Amount accrued 31 December 2020 £m
Liquidity facility:		
Liquidity facility commitment fee	0.3	0.1
Interest on senior debt:		
A1 bond interest	-	55.3
A4 bond interest	-	15.9
A5 bond interest	-	4.1
A6 bond interest	-	1.4
B1 bond interest	-	3.4
B3 bond interest	-	16.9
B4 bond interest	-	2.5
B5 bond interest	-	1.5
B6 bond interest	-	0.3
B7 bond interest	-	1.7
B8 bond interest	-	5.7
European Investment Bank loan interest	2.1	3.1
KfW IPEX-Bank GmbH loan interest	0.2	0.3
Revolving credit facility commitment fees	0.3	-
Assured Guaranty wrapping fees	-	(1.2)
	2.9	111.0
Interest rate swaps	2.7	-
Senior interest payments	5.6	111.0
Interest on junior debt:		
C3 bond interest	-	2.5
Total debt service payments	5.6	113.5

Dŵr Cymru notes principal balance reconciliation (unaudited)

	Credit rating[1]	Opening balance 1 October 2020 £m	New issues £m	Repayment £m	Indexation £m	Closing balance 31 December 2020 £m
Lease liabilities		411.4	-	-	-	411.4
Class A bonds[2]						
A1 notes[3]	A2/AA/A	352.1	-	-	0.9	353.0
A4 notes		448.5	-	-	3.8	452.3
A5 notes		143.8	-	-	3.2	147.0
A6 notes[3]		149.1	-	-	0.9	150.0
Class B bonds						
B1 notes	A3/A-/A	325.0	-	-	-	325.0
B3 notes		217.6	-	-	1.9	219.5
B4 notes		126.9	-	-	3.0	129.9
B5 notes		74.5	-	-	0.6	75.1
B6 notes		351.0	-	-	1.8	352.8
B7 notes		300.0			-	300.0
B8 notes[3]		301.7	-	-	0.9	302.6
Class C bonds						
C3 notes[3]	Baa2/BBB/BBB+	201.1	-	-	0.6	201.7
Intercompany loan from Dŵr Cymru Holdings Limited		2.8	-	-	-	2.8
European Investment Bank/KfW loans		696.3	-	(14.6)	0.8	682.5
Local authority loans		0.3	-	(0.1)	-	0.2
		4,102.1	-	(14.7)	18.4	4,105.8

[1] Moody's/S&P/Fitch.
[2] Guaranteed by Assured Guaranty (Europe) plc rated A2/AA/NR. Class A bond ratings for Fitch therefore default to their higher underlying ratings of A2/AA/A.
[3] The class A1, A6, B8 and C3 notes were issued at a fixed rate and swapped to an effective index-linked rate; cumulative indexation has been recognised in this table.

Dŵr Cymru bank account movements (unaudited)

	Opening balance 1 October 2020 £m	Interest received £m	Deposits £m	Payments £m	Closing balance 31 December 2020 £m
Free cash balances:					
Receipts account	56.4	-	198.0	(247.5)	6.9
Payments account	471.6	-	593.9	(585.1)	480.4
Other bank accounts	0.1	1.3	376.7	(378.1)	-
	528.1	1.3	1,168.6	(1,210.7)	487.3
Debt service payments account:					
Debt service ledger	48.2	-	37.5	(5.6)	80.1
Capex reserve account	-	-	122.0	(122.0)	-
Customer payments account:					
Customer rebate ledger	5.5	-	-	(3.7)	1.8
	581.8	1.3	1,328.1	(1,342.0)	569.2

Interest cover ratio (ICR) – 5 years to 31 March 2025 (unaudited)

(See important notice at the front of the document)	Projection Year to 31 March 2021 £m	Year to 31 March 2022 £m	Year to 31 March 2023 £m	Year to 31 March 2024 £m	Year to 31 March 2025 £m
Income	792	805	843	826	834
Operating expenditure	(336)	(319)	(323)	(310)	(317)
Pre capital maintenance cash flows	**456**	**486**	**520**	**516**	**517**
Base maintenance	(216)	(205)	(205)	(164)	(155)
Post capital maintenance cash flows	**240**	**281**	**315**	**352**	**362**
Net interest paid (excluding indexation and capitalisation)	(130)	(95)	(90)	(92)	(94)
Enhancement expenditure	(130)	(162)	(217)	(188)	(170)
Customer rebates	(14)	(15)	(13)	(10)	(8)
Pre-financing cash flows	**(34)**	**9**	**(5)**	**62**	**90**
Interest payable:					
Fixed interest swap	9	9	9	10	10
Lease liability RPI swaps	18	16	14	14	15
Lease liability interest	5	5	5	5	3
A1 Bonds	9	9	9	9	9
B1 Bonds	23	-	-	-	-
B7 Bonds	8	8	8	8	8
Other index-linked bonds	47	47	46	47	48
RPI-linked senior bond	(4)	(5)	(5)	(5)	(5)
RPI-linked junior bond	(2)	(6)	(6)	(6)	(6)
Wrapping fees	5	5	5	5	6
Term-loan interest	14	10	9	9	9
Other fees	1	1	1	1	1
Interest receivable	(3)	(4)	(5)	(5)	(4)
Net interest payable	**130**	**95**	**90**	**92**	**94**
Senior interest cover pre capital maintenance (trigger 2.0, default 1.6)	3.4x	4.8x	5.4x	5.3x	5.2x
Senior interest cover post capital maintenance (trigger 1.0)	1.8x	2.8x	3.3x	3.6x	3.6x
Total interest cover pre capital maintenance (trigger 2.0, default 1.6)	3.5x	5.1x	5.8x	5.6x	5.5x
Total interest cover post capital maintenance (trigger 1.0)	1.8x	3.0x	3.5x	3.8x	3.9x

Regulatory asset ratio (RAR) – 5 years to 31 March 2025 (unaudited)

(See important notice at the front of the document)	As at 31 March 2021 £m	Projection As at 31 March 2022 £m	As at 31 March 2023 £m	As at 31 March 2024 £m	As at 31 March 2025 £m
Senior gross debt:					
Lease liabilities	395	379	378	173	95
Class A bonds[1]	1,105	1,134	1,167	1,202	1,234
Class B bonds[1]	1,385	1,411	1,436	1,460	1,512
Authorised loans	677	640	604	538	473
Net interest accrual on senior debt	48	44	39	15	6
Total senior gross debt	**3,610**	**3,608**	**3,624**	**3,388**	**3,320**
Less: cash and cash equivalents	**(217)**	**(454)**	**(399)**	**(149)**	**(100)**
Total senior net debt	**3,393**	**3,154**	**3,225**	**3,239**	**3,220**
Junior net debt:					
Class C bonds[1]	203	508	522	537	554
Total net debt	**3,596**	**3,662**	**3,747**	**3,776**	**3,774**
Regulatory capital value (RCV)	**6,021**	**6,186**	**6,349**	**6,497**	**6,629**
Customer Reserves (RCV less total net debt)	**2,425**	**2,524**	**2,602**	**2,721**	**2,855**
RAR	**59.7%**	**59.2%**	**59.0%**	**58.1%**	**56.9%**
Senior gearing	**56.4%**	**51.0%**	**50.8%**	**49.9%**	**48.6%**
Total gearing	**59.7%**	**59.2%**	**59.0%**	**58.1%**	**56.9%**

[1] For the purpose of calculating regulatory gearing, cumulative indexation relating to the class A1, A6, B8 and C3 notes is included above; these were issued at fixed rates and swapped to effective index-linked rates. Similar assumptions have been made in respect of forecast bond issuances.

Income statement (unaudited)

	3 months ended 31 December 2020 £m	9 months ended 31 December 2020 £m	9 months ended 31 December 2019 £m
Revenue	197.7	582.6	591.6
Operating expenditure	(85.7)	(238.5)	(240.6)
Exceptional item	(4.2)	(21.0)	-
EBITDA	**107.8**	**323.1**	**351.0**
Profit on disposal of fixed assets	-	0.1	0.2
Infrastructure renewals expenditure	(21.1)	(68.2)	(68.1)
Depreciation	(83.0)	(250.3)	(233.8)
Operating profit	**3.7**	**4.7**	**49.3**
Interest payable	(29.9)	(93.7)	(82.4)
Indexation of index-linked debt	(18.4)	(27.2)	(36.7)
Interest receivable	1.2	3.9	4.5
Fair value losses on financial instruments	(0.1)	(40.7)	(13.8)
Loss before tax	**(43.5)**	**(153.0)**	**(79.1)**
Taxation	-	19.5	12.5
Loss after tax	**(43.5)**	**(133.5)**	**(66.6)**

Statement of comprehensive income (unaudited)

	3 months ended 31 December 2020 £m	9 months ended 31 December 2020 £m	9 months ended 31 December 2019 £m
Loss for the period	(43.5)	(133.5)	(66.6)
Actuarial loss on defined benefit scheme liability	-	(56.6)	(28.0)
Movement on related deferred tax asset	-	10.8	4.7
Items that will not be reclassified to the profit or loss:			
Revaluation of property, plant and equipment (net of tax)	-	32.9	68.1
Total comprehensive loss	**(43.5)**	**(146.4)**	**(21.8)**

Statement of changes in reserves (unaudited)

	3 months ended 31 December 2020 £m	9 months ended 31 December 2020 £m	9 months ended 31 December 2019 £m
Reserves at start of period	1,135.2	1,238.1	1,308.6
Loss for the period	(43.5)	(133.5)	(66.6)
Actuarial loss on defined benefit pension scheme liability (net of tax)	-	(45.8)	(23.3)
Revaluation of property, plant and equipment (net of tax)	-	32.9	68.1
Reserves at end of period	**1,091.7**	**1,091.7**	**1,286.8**

Balance sheet (unaudited)

	At 31 December 2020		At 31 March 2020	
	£m	£m	£m	£m
Fixed assets		**5,957.7**		**5,940.4**
Current assets and liabilities:				
Debtors and prepayments	319.1		592.0	
Creditors and accruals	(572.2)		(878.7)	
		(253.1)		(286.7)
Total assets less current liabilities		**5,704.6**		**5,653.7**
Financing liabilities:				
Bonds	(3,008.9)		(2,984.3)	
Lease liabilities	(411.4)		(424.1)	
Bank loans (EIB, KfW)	(682.5)		(721.6)	
Other	(3.0)		(3.1)	
	(4,105.8)		(4,133.1)	
Net interest accrual	(118.9)		(53.1)	
	(4,224.7)		(4,186.2)	
Cash and cash equivalents:				
Receipts account	6.9		62.9	
Payments account	480.4		582.6	
Capex reserve account	-		-	
Debt service payments account	80.1		10.4	
Customer payments account	1.8		11.0	
Other bank accounts	-		(10.6)	
	569.2		656.3	
Net debt		**(3,655.5)**		**(3,529.9)**
Derivative financial instruments		(342.5)		(301.8)
Provisions for liabilities and charges		(156.1)		(102.5)
Net assets before deferred tax		**1,550.5**		**1,719.5**
Deferred tax		(458.8)		(481.4)
Net assets		**1,091.7**		**1,238.1**