Dŵr Cymru (Financing) UK plc

Interim report and accounts
for the six months ended 30 September 2021

Contents

Interim management report

The Directors have pleasure in presenting their management report, together with the financial statements for the six months to 30 September 2021, on pages 3 to 11.

Principal activities
The principal activity of Dŵr Cymru (Financing) UK plc ('the Company') is that of an investment company providing long-term funding for the activities of Dŵr Cymru Cyfyngedig (DCC).

Results and dividends
The loss before taxation amounted to £67,093,000 (six months to 30 September 2020: £37,527,000; year to 31 March 2021: loss of £45,299,000). No dividend was declared or paid during the period (six months to 30 September 2020 and year to 31 March 2021: none).

Business review
During the period the Company continued its activities as an investment company providing long-term funding for Dŵr Cymru Cyfyngedig ('DCC'), the only trading subsidiary in the Whole Business Securitisation of the Glas Cymru Holdings Cyfyngedig Group ('the Group').

On 31 March 2021 the Company repaid £325 million of senior Class B1 bonds with a fixed coupon of 6.907% which reached maturity as at that date.

In April 2021, the Company successfully issued £300m in new junior bonds. During the same period, the Company entered into swap contracts effectively hedging the new debt issuance to the Retail Prices Index (RPI), with RPI indexation accreting on the balance sheet over the term. The combined effect of these instruments generates a cash interest rate of -1.149% per annum until maturity in 2034 when the RPI-indexed principal (notional £300m x RPI) is repayable in full.

The Company has a special £135m liquidity facility which is a requirement of the Company's bond covenants; it can only be drawn in the event that the Company is in default of its covenants and unable to pay its interest bills. The facility is renewable on a rolling five-year evergreen basis (next renewal due 3 April 2024).

Principal risks and uncertainties
From the perspective of the Company, the principal risks and uncertainties are integrated with the principal risks of the group and are not managed separately. Accordingly, the principal risks and uncertainties of the Glas Cymru Group, which include those of the Company, are disclosed within the Group's annual report. Management does not consider that these have changed materially during the first six months of the year, nor that there will be any significant change between now and the end of the year. Page 10 of this report refers to risk management of treasury activities within the company.

Key Performance Indicators
The company is part of a group controlled by Glas Cymru Holdings Cyfyngedig. The directors of Dŵr Cymru (Financing) UK plc use group-wide key performance measures as indicators to the development, performance and position of the company. These are discussed in the Annual Report of Glas Cymru Holdings Cyfyngedig which does not form part of this report (available on the group's website at http://www.dwrcymru.com/en/Reading_Room_Library/Company-Reports.aspx).

Covid-19
The Company is not directly affected by the pandemic, having no need to source financing in the short-to-medium term and having only one customer, DCC. The potential for indirect impact is DCC's ability to service the debt on-lent by the Company. The Directors of the Group have taken into account the estimated impact of the pandemic on the valuation of the Group's consolidated and DCC's entity balance sheet as at 30 September 2021, concluding that the pandemic poses no significant threat to the viability of the Group or DCC and that they will be able to continue their activities for the foreseeable future. See also "going concern" in the notes to the financial statements on page 7.

Interim income statement

	Note	Six months ended 30 September 2021 (unaudited) £000	Six months ended 30 September 2020 (unaudited) £000	Year ended 31 March 2021 (audited) £000
Continuing activities				
- Financial income	4a	**47,335**	22,016	35,519
- Financial expenses	4a	**(47,928)**	(26,345)	(38,954)
- Fair value losses on derivative financial instruments	4b	**(66,500)**	(33,198)	(41,864)
Loss before taxation		**(67,093)**	(37,527)	(45,299)
Taxation credit	5	**9,195**	1,439	4,981
Loss for the period		**(57,898)**	(36,088)	(40,318)

Underlying profit			
Loss before taxation per income statement	**(67,093)**	**(37,527)**	(45,299)
Add back:			
- Effect of fair value losses on derivative financial instruments	**66,500**	**33,198**	41,864
Loss before taxation and fair value adjustments	**(593)**	**(4,329)**	(3,435)

The Company has no other recognised gains or losses in the periods presented and accordingly a Statement of Comprehensive Income has not been presented.

The notes on pages 7 to 11 are an integral part to these financial statements.

Interim statement of changes in equity

	Share capital £000	Share premium £000	Capital contribution reserve £000	Retained earnings £000	Six months ended 30 September 2021 (unaudited) Total £000	Six months ended 30 September 2020 (unaudited) Total £000	Year Ended 31 March 2021 (audited) Total £000
Surplus at start of period	**50**	**3,033**	**57,433**	**(18,823)**	**41,693**	82,011	82,011
Loss for the period	-	-	-	**(57,898)**	**(57,898)**	(36,088)	(40,318)
Surplus at end of period	**50**	**3,033**	**57,433**	**(76,721)**	**(16,205)**	45,923	41,693

The notes on pages 7 to 11 are an integral part to these financial statements.

Interim balance sheet

Assets	At 30 September 2021 (unaudited) £000	At 30 September 2020 (unaudited) £000	At 31 March 2021 (audited) £000
Non-current assets			
Deferred tax asset	**15,690**	2,905	6,471
Other financial assets:			
- loans to group undertakings	**4,067,565**	3,773,487	3,734,940
- derivative financial instruments	**68,806**	93,183	74,052
	4,152,061	3,869,575	3,815,463
Current assets			
Cash and cash equivalents	**516**	259	266
Other financial assets:			
- loans to group undertakings	**23,696**	399,910	56,677
- derivative financial instruments	**57,192**	46,955	38,759
	81,404	447,124	95,702
Total assets	**4,233,465**	4,316,699	3,911,165
Liabilities			
Current liabilities			
Trade and other payables	**(24,209)**	(32,377)	(651)
Other financial liabilities:			
- borrowings	**(47,673)**	(398,169)	(55,606)
- derivative financial instruments	**(15,371)**	(15,755)	(17,289)
	(87,253)	(446,301)	(73,546)
Net current assets	**(5,849)**	823	22,156
Non-current liabilities			
Other financial liabilities:			
- borrowings	**(3,732,717)**	(3,499,600)	(3,481,513)
- derivative financial instruments	**(429,700)**	(324,875)	(314,413)
	(4,162,417)	(3,824,475)	(3,795,926)
Total Liabilities	**(4,249,670)**	(4,270,776)	(3,869,472)
Net assets	**(16,205)**	45,923	41,693
Equity			
Share capital	**50**	50	50
Share premium	**3,033**	3,033	3,033
Capital contribution reserve	**57,433**	57,433	57,433
Retained earnings	**(76,721)**	(14,593)	(18,823)
Total equity	**(16,205)**	45,923	41,693

The interim financial statements on pages 3 to 6 were approved by the Board of Directors on 4 November 2021 and were signed on its behalf by:

Mike Davis
Director

The notes on pages 7 to 11 are an integral part to these financial statements.

Interim statement of cash flows

	Six months ended 30 September 2021 (unaudited) £000	Six months ended 30 September 2020 (unaudited) £000	Year ended 31 March 2021 (audited) £000
Cash flows from operating activities			
Interest received	**29,402**	44,299	200,427
Interest paid	**(29,359)**	(44,256)	(200,377)
Net cash flow from operating activities	**43**	43	50
Cash flows from financing activities			
Loan issued to group undertakings	**(297,077)**	-	-
Loan repaid by group undertaking	**15,909**	17,045	354,091
Bond repayment	**-**	-	(325,000)
Bond issue	**297,077**	-	-
Term loans repaid	**(15,909)**	(17,045)	(29,091)
Other cash receipt from group undertaking	**207**	-	-
Net cash flow from financing activities	**207**	-	-
Increase in cash and cash equivalents	**250**	43	50
Cash and cash equivalents at start of period	**266**	216	216
Cash and cash equivalents at end of period	**516**	259	266

Notes to the condensed interim financial statements

1. Basis of preparation

Dŵr Cymru (Financing) UK plc ('the Company') is a public limited company incorporated, domiciled and registered in Wales in the UK. The registered number is 11949988 and the registered address is Linea, Fortran Road, St Mellons, Cardiff, CF3 0LT. The Company is part of a group headed by Glas Cymru Holdings Cyfyngedig ('the Group') and it exists solely to act as an investment company providing long-term funding for the activities of Dŵr Cymru Cyfyngedig, a regulated water and sewerage undertaker and fellow group company.

These interim financial statements have been prepared in accordance with IAS 34 Interim Financial Reporting and should be read in conjunction with the Company's last annual financial statements for the year ended 31 March 2021. They do not include all of the information required for a complete set of IFRS financial statements, however selected explanatory notes are included to explain items that are significant to an understanding of the changes in the Company's financial position and performance since the last financial statements.

The principal accounting policies adopted in the preparation of these condensed interim financial statements are consistent with those of the previous set of published Annual Report and Accounts for the year ended 31 March 2021.

Estimates

The preparation of interim financial statements requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets and liabilities, income and expenditure. Actual results may differ from these estimates.

In preparing these condensed interim financial statements, the significant judgements made by management in applying the Company's accounting policies and the key sources of estimation uncertainty were the same as those that applied to the financial statements for the year ended 31 March 2021 with the exception of changes in estimates that are required in determining the provision for income taxes and derivative financial instruments.

Taxes on income in the interim accounts are accrued using the tax rate that would be applicable to expected total annual earnings.

Derivative financial instruments

Derivative instruments utilised by the Company are interest rate and inflation swaps. Derivative instruments are used for hedging purposes to alter the risk profile of existing underlying exposures within the Company and the Group as a whole.

Derivatives are recognised initially and subsequently re-measured at fair value. The fair values of derivative financial instruments are provided by swap counterparties. The Bloomberg financial dataset platform allows management to perform an independent valuation of these contracts which is then compared to the counterparty confirmations; management makes an adjustment for the Company's own credit risk using this valuation tool to extract an average of traded bond spreads at the balance sheet date.

During the period to 30 September 2021, one of the Company's derivatives qualified for hedge accounting under IFRS 9. We have selected not to apply hedge accounting to the qualified hedge instrument. Our hedge instruments are carried at fair value through profit or loss with changes in fair value being recognised immediately in the income statement.

Deferred taxation

Deferred corporation tax is provided, using the liability method, on all temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred tax liabilities are recognised in respect of all temporary differences. Deferred tax assets are recognised for all deductible temporary differences, carry-forward of unused tax assets and tax losses, to the extent that they are regarded as recoverable. They are regarded as recoverable where, on the basis of available evidence, there will be suitable taxable profits against which the future reversal of the underlying temporary differences can be deducted. The carrying value of the amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all, or part, of the asset to be utilised.

Notes to the condensed interim financial statements

1. Basis of preparation (continued)

Deferred taxation (continued)

Deferred corporation tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realised or the liability is settled, based on the tax rates that have been substantively enacted at the balance sheet date.

Going concern

The financial statements have been prepared on the going concern basis as the Directors have a reasonable expectation that the Group and parent company have adequate resources for a period of at least 12 months from the date of their approval and that there are no material uncertainties to disclose.

In assessing the appropriateness of the going concern basis of accounting the Directors have reviewed the resources available to the Group in the form of cash and committed bank facilities as well as consideration of the Group's capital adequacy, along with a business plan which reflects a view of the estimated impact of the Covid-19 pandemic on the Group.

The business plan reflects a gradual lifting of restrictions relating to the pandemic with unemployment peaking in the current year and recovering to pre-pandemic levels by 2025. CPIH fell to a low in late 2020, is expected to peak this year and is then assumed to gradually recover to the government's long-term target of 2% by 2024. This is considered to be a prudent assumption since higher inflation increases the value of the Group's regulatory capital value and lowers its level of regulatory gearing. Some pressure on the Group's bad debt charge is expected during the current year and next, as a consequence of rising unemployment.

Our Covid-19 impact modelling is informed by external reports including those by the Office for Budget Responsibility (OBR) which has published a number of updated coronavirus analyses, the latest being the Economic and Fiscal Outlook released on 27 October 2021. [Our performance to date is broadly in line with our business plan, and this latest update from the OBR does not materially impact those forecasts.]

The business plan has also been subject to an extreme downside stress scenario, which assumes an additional drop in CPIH of 4% (from 1% to -3%, recovering by March 2023), unemployment at around 12% as well as additional Covid-related revenue reductions and cost pressures. Reduced cash flows would impact on key financial metrics, in particular interest cover ratios. In the extreme downside scenario, the Group's gearing and interest covers retain significant headroom within the trigger levels specified in borrowing covenants.

Having considered these matters in relation to Group-wide activities, the Directors do not believe there are any material uncertainties to disclose in relation to the Company's ability to continue as a going concern.

2. Segmental information

The Company's business is solely to act as an investment company providing long-term funding for the activities of Dŵr Cymru Cyfyngedig and therefore it operates in a single segment.

Notes to the condensed interim financial statements

3. Net financial expense

a) Financing cost before fair value losses	Six months ended 30 September 2021 £000 (unaudited)	Six months ended 30 September 2020 £000 (unaudited)	Year ended 31 March 2021 £000 (audited)
Financial income:			
Intercompany	**47,335**	22,016	35,519
Financial expenses:			
Interest payable	**(47,928)**	(26,345)	(38,954)
Net financial expense before fair value adjustments	**(593)**	(4,329)	(3,435)

b) Fair value losses on derivative financial instruments	Six months ende 30 September 2021 £0((unaudited)	Six months ended 30 September 2020 £000 (unaudited)	Year ended 31 March 2021 £000 (audited)
Fair value losses on derivative financial instruments before indexation	**(66,500)**	(33,198)	(41,864)

4. Taxation

	Six months ended 30 September 2021 £000 (unaudited)	Six months ended 30 September 2020 £000 (unaudited)	Year ended 31 March 2021 £000 (audited)
Corporation tax			
Group relief	**(24)**	(25)	(49)
Deferred tax			
Current year movements	**9,219**	1,464	5,030
	9,195	1,439	4,981
Loss before tax	**(67,093)**	(37,527)	(45,299)
Loss before tax multiplied by the corporation tax in the UK of 19%	**12,748**	7,130	8,607
Effects of:			
Release of fair value adjustments - not deductible for tax	**(137)**	(847)	(701)
Fair value movements on derivatives - not taxable/ (deductible)	**(7,182)**	(4,844)	(2,925)
Effect of tax rate changes - deferred taxes calculated at 25% (30 September 2020 and 31 March 2021: 19%)	**3,766**	-	-
Total taxation credit	**9,195**	1,439	4,981

Notes to the condensed interim financial statements

5. Analysis and reconciliation of net funds

a) Net funds at the balance sheet date may be analysed as:	Six months ended 30 September 2021 £000 (unaudited)	Six months ended 30 September 2020 £000 (unaudited)	Year ended 31 March 2021 £000 (audited)
Cash and cash equivalents	**516**	259	266
Financial assets: group receivables	**4,091,261**	4,173,397	3,791,617
	4,091,777	4,173,656	3,791,883
Net accrued interest	**(24,119)**	(32,335)	(585)
Debt due after one year	**(3,732,717)**	(3,499,600)	(3,481,513)
Debt due within one year	**(47,673)**	(398,169)	(55.600)
	(3,804,509)	(3,930,104)	(3,537,704)
Net funds	**287,268**	243,552	254,179

b) The movement in funds debt during the period may be summarised as:	Six months ended 30 September 2021 £000 (unaudited)	Six months ended 30 September 2020 £000 (unaudited)	Year ended 31 March 2021 £000 (audited)
Net funds at start of period	**254,179**	244,971	244,971
Increase in net cash	**250**	43	50
Decrease/(increase) in receivables	**299,644**	(24,005)	(405,785)
Increase/(decrease) in debt	**(233,456)**	57,507	434,983
Increase in net funds arising from cash flows	**66,438**	33,545	29,248
Amortisation of bond issue premium	**389**	378	753
Indexation of index-linked debt	**(10,203)**	(3,973)	(21,174)
Movement in accrued interest	**(23,534)**	(31,369)	381
Movement in net funds during the period	**(33,348)**	(34,964)	(20,040)
Net funds at end of period	**287,268**	243,552	254,179

6. Financial risk management and financial instruments

The Company's activities expose it to a variety of financial risks: market risk (including fair value interest rate risk, cash flow interest rate risk and price risk), credit risk and liquidity risk.

The condensed interim financial statements do not include all financial risk management information and disclosures required in the annual financial statements; they should be read in conjunction with the Group's annual financial statements for the year ended 31 March 2021. There have been no changes in the risk management department or in any risk management policies since the year end.

In accordance with IFRS 13 Fair Value Measurement trading and treasury derivatives of the Company are categorised into different levels:

- Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices); and
- Level 3: inputs for the asset or liability that are not based on observable market data (that is, unobservable inputs).

6. Financial risk management and financial instruments (continued)

All of the Company's treasury derivatives are categorised at Level 2 and as at 30 September 2021 were valued as follows:

- Assets: treasury derivatives £126.0m (March 2021: treasury derivatives £112.8m); and
- Liabilities: treasury derivatives £445.1m (March 2021: treasury derivatives £331.7m).

Treasury derivatives relate to interest rate swap contracts and are recorded on the balance sheet at fair value. These have all been assessed as Level 2.

Level 2 debt investments are valued using a discounted cash flow approach, which discounts the contractual cash flows using discount rates derived from observable market prices of other quoted debt instruments of the counterparties.

Dŵr Cymru (Financing) UK plc

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Management responsibility statement of the Board of Directors

To the best of our knowledge, the financial statements have been prepared in accordance with the UK adopted international accounting standards in conformity with the requirements of the Companies Act 2006 and give a true and fair view of the assets, liabilities, financial position and profit or loss of Dŵr Cymru (Financing) UK plc ('the Issuer').

To the best of our knowledge, the management report includes a fair view of the development and performance of the business and the position of the Issuer, together with a description of the principal risks and uncertainties that we face.

Director
Name: Mike Davis

4 November 2021