Glas Cymru Cyfyngedig

Investor Report

For the quarter ended 31 December 2008

Important Notice

This report is being distributed in fulfilment of a document, the Common Terms Agreement (CTA), which governs the company's obligations to its bond holders and other financial creditors. It is directed to, and intended for, existing investors in the company. No other persons should act or rely on it. The company makes no representation as to the accuracy of forecast information (or any other information in this report, other than as set out in the CTA). These forecasts involve risk and uncertainty because they relate to events and depend on circumstances that will occur in the future. There are a number of factors that could cause actual results or developments to differ materially from those expressed or implied by these forecasts. This unaudited report should not be relied on as a guide to future performance, and should not be relied on in deciding whether to undertake future investment in the company. For the purposes of the financial promotions regime under the Financial Services and Markets Act 2000, this report is given on the basis of the exemption provided in Article 69 of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 (as it relates to bonds which are already admitted to trading on a relevant market).

Contents

General overview and business update

This quarterly Investor Report covers the three month period ending 31 December 2008. The Investor Report is a requirement of (and 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.

Business performance including key performance indicators (KPIs) for operations and customer service are reported in the company's annual report and accounts. These are available on the company's website (www.dwrcymru.com).

Financial performance

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

	Period to 31 December 2008 £m	Period to 31 December 2007 £m	Change
Turnover	495	466	+6%
Operating costs	204	177	+15%
EBITDA (before infrastructure renewals expenditure)	**291**	**289**	**+1%**
Net interest (excluding indexation and amortisation)	101	95	
Capital expenditure (before grants and contributions)	255	207	

General overview and business update cont'd

Operating profit before interest, tax, depreciation, infrastructure renewals and amortisation (EBITDA) for the nine months to 31 December 2008 is in line with that for the same period last year – in an increasingly challenging economic environment, price increases have been offset by increased power costs, bad debt provisioning and an actuarial loss on the pension scheme, as well as the impact on costs of general inflation.

Turnover in the nine months to 31 December 2008 was £495 million, as compared to £466 million in the nine months to 31 December 2007. The increase is a reflection of the overall price increase of 7.56% (being the RPI+K increase allowed by Ofwat less the increase in the 'customer dividend' for the year, from £20 per customer to £21 per customer). During the period, 18,000 domestic customers switched to metered charging (2007: 14,500).

Operating costs (excluding depreciation and infrastructure renewals expenditure) were £204 million (2007: £177 million); the increase is predominantly the result of higher power prices (£7 million), an increased bad debt charge (by £3 million) and an actuarial loss in the pension scheme (£2 million), as well as general inflation (some £8 million).

Net interest payable in the period (excluding fair value movements) was £129 million (2007: £117 million), including an indexation charge on index-linked debt of £28 million (2007: £21 million). Around 96% of borrowings are at fixed or index-linked rates of interest, in part through the use of RPI swaps, which means that the company has been insulated from recent volatility in market interest rates.

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

£m	31 December 2008	31 March 2008	31 December 2007
Net debt	2,640	2,529	2,517
Regulatory capital value	3,585	3,529	3,486
Regulatory gearing	**73.6%**	**71.7%**	**72.2%**

Glas Cymru's long-term objective is to reduce regulatory gearing to around 70% and to maintain it at such a level going forward. However, the company recognises that this is not achievable in the shorter term owing to the economic climate and fluctuations in the Retail Price Index (RPI); gearing has increased since March 2008, from 71.7% to 73.6%, principally a reflection of the recent falls in the level of RPI on the regulatory capital value. Subsequently, this fall in RPI will also impact to reduce the level of net debt, as the company has some £1.5 billion of index-linked bonds and swaps. However, due to the 8 month delay in RPI indexation for these purposes, this favourable impact will not arise until the year to 31 March 2010.

General overview and business update cont'd

Capital investment programme

Capital investment (including infrastructure renewals expenditure) was £255 million before grants and contributions (2007: £207 million), bringing the total expenditure over the AMP4 period to £1,063 million.

Ofwat have allowed for an investment programme by the company of £1,145 million (at 2002/03 prices) in order to meet its regulatory requirements over the period. These requirements include the maintenance of current service levels, further significant improvements in the protection of the environment as required by Government and a major programme to address the sewage flooding of properties.

Welsh Water's capital investment over the two years to 31 March 2010 is likely to be at or above £600 million. This will be a major challenge for the company and its alliance of capital investment partners.

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 up to 31 March 2010. These projected ratios are derived from Glas Cymru's 2008 business plan (which has been prepared by the company) and are in the format specified by the CTA. On this basis, the prospective financial ratios exceed the "trigger levels" as defined in the CTA (see pages 11 and 13). It should be noted that the company's business plan and the projected ratios have not been reviewed by the company's auditors and the reader's attention is drawn to the important notice at the front of this document.

The projections of interest cover and regulatory gearing ratios on pages 11 and 13 of this report were based on assumed rates of RPI inflation of 3.0% at 31 March 2008 and 2.5% at 31 March 2009 and therefore do not take into account recent falls in RPI and RPI expectations. The investor report for the quarter ending March 2009 will include 2008/09 actuals in place of the current projections, while the 2009/10 projections will be revised in line with the company's 2009 business plan.

Credit ratings

S&P, Moody's Investor Service ("Moody's") and Fitch Ratings ("Fitch") have all reviewed their credit ratings of MBIA and, as a consequence, their rating of the company's Class A Bonds, which are guaranteed by MBIA.

On 5 June 2008, S&P downgraded the AAA ratings of MBIA to AA and placed the ratings on CreditWatch with negative implications. On 26 June 2008, Fitch withdrew all of its outstanding ratings on MBIA. On 7 November 2008, Moody's downgraded MBIA's A2 rating to Baa1.

General overview and business update cont'd

Credit ratings cont'd

The underlying ratings of the company's Class A Bonds are unaffected by these reviews and remain at A3/AA/A for Moody's, S&P and Fitch respectively. Also the ratings of the company's Class B and C Bonds and the Moody's corporate family rating of Dŵr Cymru Cyfyngedig also remain unaffected and are stable, reflecting the stand alone credit quality of the company. The current ratings of the company's debt are summarised by the following table:

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

Moody's corporate family rating of Dŵr Cymru Cyfyngedig is A3.

Financing and liquidity

As at 31 December 2008, undrawn revolving credit facilities, EIB loans and cash (excluding the debt service reserve account) amounted to £461 million, giving the company a high degree of liquidity. As a result, the company has been insulated from the recent turmoil in credit markets and our bonds continue to trade well relative to our peers. The company's next expected bond maturity is of its Class C1 Bonds (£125 million) in March 2011.

On 23 October 2008, the company completed a £100 million loan agreement with the European Investment Bank, which will be used to help finance certain water and waste water capital schemes in the three years to March 2010. A first tranche of £25 million was drawn down under this agreement on 15 December 2008.

PR09 Business Plan

Glas Cymru submitted to Ofwat its draft business plan for the PR09 period on 11 August 2008. For further details, see the relevant section of the website, www.dwrcymru.com.

[1] *Guaranteed by MBIA*

General overview and business update cont'd

Investors

Glas Cymru held a seventh annual meeting for investors in London on 14 July 2008. At the meeting, the company presented a review of performance during the previous year and their objectives for the future.

If you would like to attend the annual meeting for investors, or would like a one-to-one meeting with the Finance Director and/or Treasurer, please contact Gina Cardwell (telephone 01443 452768) or send an e-mail request to investors@dwrcymru.com.

Consolidated cash flow

	3 months ended 31 December 2008 £m	9 months ended 31 December 2008 £m	9 months ended 31 December 2007 £m
Turnover	167.0	494.9	465.5
Less: operating expenses	(71.1)	(204.2)	(176.5)
Earnings before interest, taxation, depreciation and amortisation	95.9	290.7	289.0
Working capital movements	(29.7)	(18.3)	(33.0)
Non bond-related interest received/(paid)	(1.0)	(1.8)	(0.9)
Swap termination	-	-	(32.5)
Interest received	3.1	8.9	7.9
Net operating cash flow and interest received	68.3	279.5	230.5
New borrowings:			
Finance leases	-	-	85.0
European Investment Bank	25.0	25.0	-
Utilisation of reserves:			
Cash transferred to capex reserve	(47.0)	(127.8)	(100.3)
Cash utilised from capex reserve	47.0	127.8	100.3
Cash utilised from other reserves	6.9	20.6	20.3
Capital expenditure:			
Net proceeds from disposal of assets	0.2	0.1	0.9
Infrastructure renewals expenditure	(22.9)	(60.4)	(48.6)
Non-infrastructure maintenance	(27.3)	(80.2)	(62.2)
Enhancement expenditure	(42.7)	(115.2)	(83.5)
Net cash flow after capital expenditure, new borrowings and reserve drawings	7.5	69.4	142.4
Transfer to debt service payment account	(43.4)	(116.3)	(117.2)
Principal repayments	(2.2)	(4.6)	(4.5)
Net cash flow after debt service	(38.1)	(51.5)	20.7
Free cash balances brought forward	72.0	85.4	78.9
Free cash balances carried forward	33.9	33.9	99.6

Consolidated debt service payments

	Payments due & made in 3 months ending 31 December 2008 £m	Amount accrued 31 December 2008 £m
Liquidity facility:		
Liquidity facility commitment fee	0.2	0.1
Interest on senior debt:		
Finance lease interest payments	-	65.9
A1 interest payments	-	15.8
A4 interest payments	-	2.9
A5 interest payments	-	0.9
A6 interest payments	-	1.0
B1 interest payments	-	16.9
B3 interest payments	-	1.8
B4 interest payments	-	1.0
B5 interest payments	-	0.2
European Investment Bank loan	1.9	1.8
RCF commitment fees	0.1	-
Miscellaneous fees	-	0.8
	2.2	109.1
Interest on junior debt:		
C1 interest payments	-	7.7
	-	7.7
Total debt service payments	2.2	116.8

Glas notes principal balance reconciliation

	Credit rating[1]	Opening balance 1 October 2008 £m	New issues £m	Repayment £m	Indexation £m	Closing balance 31 December 2008 £m
Finance leases		842.4	-	-	-	842.4
Class A bonds[2]						
A1 notes	AA/A3/A	350.0	-	-	-	350.0
A4 notes		323.8	-	-	4.9	328.7
A5 notes		103.9	-	-	1.6	105.5
A6 notes[3]		107.6	-	-	1.7	109.3
Class B bonds						
B1 notes	A/A3/A	325.0	-	-	-	325.0
B3 notes		157.1	-	-	2.3	159.4
B4 notes		91.6	-	-	1.5	93.1
B5 notes		53.8	-	-	1.0	54.8
Class C bonds						
C1 notes	BBB+/Baa2/BBB+	125.0	-	-	-	125.0
EIB Loan		128.4	25.0	(2.2)	-	151.2
Local authority loans		2.8	-	-	-	2.8
		2,611.4	25.0	(2.2)	13.0	2,647.2

[1] *S&P/Moody's/Fitch ratings*

[2] *Guaranteed by MBIA*

[3] *The class A6 notes (£100m) were issued at a fixed rate of 4.473% but swapped into an effective index-linked rate of 1.35%. Cumulative indexation of £9.3m reflects the principal accrual on the index-linked swap.*

Glas bank account movements

	Opening balance 1 October 2008 £m	Interest received £m	Deposits £m	Payments £m	Closing balance 31 December 2008 £m
Free cash balances:					
Receipts account	56.4	-	182.9	(182.7)	56.6
Payments account	14.7	-	451.5	(514.9)	(48.7)
Other bank accounts	0.9	3.1	1,958.3	(1,936.3)	26.0
	72.0	3.1	2,592.7	(2,633.9)	33.9
Debt service payment account:					
Debt service ledger	54.1	-	43.4	(2.2)	95.3
Capex reserve account	-	-	47.0	(47.0)	-
Customer payments account:					
Customer rebate ledger	13.8	-	-	(6.9)	6.9
	139.9	3.1	2,683.1	(2,690.0)	136.1

Interest cover ratio (ICR) – Period to 31 March 2005

	Actual			
	Year to 31 March 2002 £m	Year to 31 March 2003 £m	Year to 31 March 2004 £m	Year to 31 March 2005 £m
Income	406.1	462.9	481.2	505.6
Operating expenditure	(183.8)	(204.0)	(210.4)	(210.3)
Pre capital maintenance cash flows	222.3	258.9	270.8	295.3
Capital maintenance expenditure	(82.1)	(137.3)	(111.0)	(85.7)
Post capital maintenance cash flows	140.2	121.6	159.8	209.6
Net interest (excluding indexation)	(104.8)	(119.4)	(124.3)	(122.7)
Capital expenditure	(98.0)	(124.7)	(148.7)	(142.0)
Customer rebates	-	-	(11.5)	(11.5)
Pre-financing cash flows	(62.6)	(122.5)	(124.7)	(66.6)
Interest payable on senior debt:				
Finance leases	8.7	12.6	12.8	12.5
Class A	43.2	47.0	46.4	50.0
Class B	30.5	33.8	36.3	37.8
MBIA financial guarantee fees	4.3	4.9	4.8	4.7
Interest rate and currency swaps	2.9	9.9	15.1	8.3
Authorised loans	-	-	-	0.5
Less interest receivable	(12.9)	(16.8)	(17.6)	(19.1)
Total net senior debt interest	76.7	91.4	97.8	94.7
Interest payable on junior debt:				
Class C	16.9	18.5	18.1	19.5
Class D	9.0	8.0	6.8	5.8
Other	2.2	1.5	1.6	2.7
Total interest payable	104.8	119.4	124.3	122.7
Senior interest cover pre capital maintenance (trigger 2.0; default 1.6)	2.9	2.8	2.8	3.1
Total interest cover pre capital maintenance	2.1	2.2	2.2	2.4
Senior interest cover post capital maintenance (trigger 1.1)	1.8	1.3	1.6	2.2
Total interest cover post capital maintenance	1.3	1.0	1.3	1.7

Interest cover ratio (ICR) – 5 years to 31 March 2010 (based on 2008 business plan – see page 3)

(See important notice at the front of the document)	Actual Year to 31 March 2006 £m	Actual Year to 31 March 2007 £m	Actual Year to 31 March 2008 £m	*Projections Year to 31 March 2009 £m*	*Projections Year to 31 March 2010 £m*
Income	576.5	602.7	648.6	*694*	*725*
Operating expenditure	(213.2)	(228.6)	(230.8)	*(254)*	*(262)*
Pre capital maintenance cash flows	363.3	374.1	417.8	*440*	*463*
Capital maintenance expenditure	(98.1)	(150.2)	(146.2)	*(152)*	*(162)*
Post capital maintenance cash flows	265.2	223.9	271.6	*288*	*301*
Net interest (excluding indexation)	(129.9)	(127.0)	(127.5)	*(134)*	*(135)*
Capital expenditure	(122.3)	(96.7)	(136.7)	*(165)*	*(150)*
Customer rebates	(23.0)	(24.7)	(25.7)	*(27)*	*(28)*
Pre-financing cash flows	(10.0)	(24.5)	(18.3)	*(38)*	*(12)*
Interest payable on senior debt:					
Finance leases	31.9	33.7	45.8	*48*	*41*
Class A	43.6	36.9	36.4	*38*	*38*
Class B	33.5	32.4	33.2	*34*	*35*
MBIA financial guarantee fees	4.7	3.6	3.7	*4*	*4*
Interest rate swaps	4.2	7.7	(0.2)	*(5)*	*(4)*
Authorised loans	5.4	8.5	8.3	*13*	*17*
Less interest receivable	(9.7)	(7.4)	(12.2)	*(9)*	*(7)*
Total net senior debt interest	113.7	115.4	115.0	*123*	*124*
Interest payable on junior debt:					
Class C	13.1	10.2	10.2	*10*	*10*
Class D	-	-			
Other	3.1	2.2	2.3	*1*	*1*
Total interest payable	129.9	127.8	127.5	*134*	*135*
Senior interest cover pre capital maintenance (trigger 2.0; default 1.6)	3.1	3.3	3.6	*3.6*	*3.7*
Total interest cover pre capital maintenance	2.8	2.9	3.3	*3.3*	*3.4*
Senior interest cover post capital maintenance (trigger 1.1)	2.3	2.0	2.4	*2.3*	*2.4*
Total interest cover post capital maintenance	2.0	1.8	2.1	*2.1*	*2.2*

Regulatory asset ratio (RAR) – period to 31 March 2005

	Actual			
	As at 31 March 2002 £m	As at 31 March 2003 £m	As at 31 March 2004 £m	As at 31 March 2005 £m
Senior gross debt:				
Finance leases	289	382	440	632
Class A	1,003	1,009	1,020	1,031
Class B	561	563	640	646
Net interest accrual on senior debt	49	14	43	32
EIB Loan	-	-	-	35
Authorised loan facility	-	-	-	-
Total senior gross debt	1,902	1,968	2,143	2,376
Less: cash balances and authorised investments	(383)	(287)	(280)	(325)
Total senior net debt	1,519	1,681	1,863	2,051
Class C	250	250	250	250
Interest accrual on Class C	10	-	-	-
Class D	100	76	56	-
Local authority loans	5	5	4	4
Other interest accruals	-	1	-	-
Total net debt	1,884	2,013	2,173	2,305
Regulatory capital value (RCV)	2,125	2,362	2,594	2,843
Reserves (RCV less total net debt)	241	349	421	538
Regulatory asset ratio:				
RAR (Senior)	71%	71%	72%	72%
RAR (Senior + C) (trigger 90%; default 95%)	83%	82%	81%	81%
RAR (Total debt)	89%	85%	84%	81%

Regulatory asset ratio (RAR) – 5 years to 31 March 2010 (based on 2008 business plan – see page 3)

(See important notice at the front of the document)	Actual			*Projections*	
	As at 31 March 2006 £m	**As at 31 March 2007 £m**	**As at 31 March 2008 £m**	***As at 31 March 2009 £m***	***As at 31 March 2010 £m***
Senior gross debt:					
Finance leases	740	767	842	*837*	*831*
Class A	742	856	875	*896*	*909*
Class B	553	611	623	*634*	*641*
Net interest accrual on senior debt	29	84	56	*55*	*57*
EIB Loan	60	135	131	*127*	*123*
Authorised loan facility	120	-	-	*120*	*159*
Total senior gross debt	2,244	2,453	2,527	*2,669*	*2,720*
Less: cash balances and authorised investments	(14)	(158)	(124)	*(150)*	*(150)*
Total senior net debt	2,230	2,295	2,403	*2,519*	*2,570*
Class C	125	125	125	*125*	*125*
Interest accrual on junior debt	-	10	-	*-*	*-*
Local authority loans	4	4	3	*3*	*3*
Total net debt	2,359	2,434	2,531	*2,647*	*2,698*
Regulatory capital value (RCV) [1]	3,042	3,310	3,529	*3,695*	*3,808*
Reserves (RCV less total net debt)	683	876	998	*1,048*	*1,110*
Regulatory asset ratio:					
RAR (Senior)	73%	69%	68%	*68%*	*67%*
RAR (Senior + C) (trigger 90%; default 95%)	77%	73%	72%	*72%*	*71%*
RAR (Total debt)	78%	74%	72%	*72%*	*71%*

[1] as published by Ofwat (RD 07/08) on 21 April 2008

Income statement

	3 months ended 31 December 2008 £m	9 months ended 31 December 2008 £m	*9 months ended 31 December 2007 £m*
Turnover	**167.0**	**494.9**	**465.5**
Operating expenditure	**(71.1)**	**(204.2)**	**(176.5)**
EBITDA	**95.9**	**290.7**	**289.0**
Infrastructure renewals expenditure	**(30.3)**	**(78.0)**	**(66.0)**
Depreciation	**(33.9)**	**(99.8)**	**(91.3)**
Profit on disposal of fixed assets	**0.2**	**0.1**	**0.9**
Operating profit	**31.9**	**113.0**	**132.6**
Interest payable	**(50.5)**	**(136.7)**	**(125.2)**
Interest receivable	**1.9**	**7.4**	**8.2**
Fair value losses on financial instruments	**(39.4)**	**(110.4)**	**(23.5)**
(Loss)/profit before tax	**(56.1)**	**(126.7)**	**(7.9)**
Current taxation	**-**	**-**	**-**
Deferred taxation			
Adjustment in respect of prior periods	**-**	**2.2**	**-**
Credit/(charge) at 28%	**-**	**19.5**	**(6.0)**
Effect of rate change	**-**	**-**	**25.9**
Effect of industrial buildings allowance abolition	**-**	**(34.4)**	**-**
	-	**(12.7)**	**19.9**
Taxation	**-**	**(12.7)**	**19.9**
(Loss)/profit after tax	**(56.1)**	**(139.4)**	**12.0**

Balance sheet

	At 31 December 2008		At 31 March 2008	
	£m	£m	£m	£m
Fixed assets		2,982.2		2,918.5
Current assets and liabilities:				
Debtors and prepayments	132.1		117.0	
Creditors and accruals	(102.6)		(120.4)	
		29.5		(3.4)
Total assets less current liabilities		3,011.7		2,915.1
Financing liabilities:				
Bonds	(1,650.8)		(1,623.0)	
Finance leases	(842.4)		(842.4)	
EIB Loan	(151.2)		(130.6)	
Other	(2.8)		(3.0)	
	(2,647.2)		(2,599.0)	
Net interest accrual	(129.3)		(54.0)	
	(2,776.5)		(2,653.0)	
Cash and cash equivalents:				
Receipts account	56.6		74.5	
Payments account	(48.7)		7.6	
Debt service payment account	95.3		11.2	
Customer payments account	6.9		27.5	
Other bank accounts	26.0		3.3	
	136.1		124.1	
Net debt		**(2,640.4)**		**(2,528.9)**
Derivative financial instruments		(181.7)		(71.3)
Provisions for liabilities and charges		(7.9)		(6.5)
Net assets before deferred tax		**181.7**		**308.4**
Deferred tax		(362.8)		(350.1)
Net liabilities		**(181.1)**		**(41.7)**