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Glas Cymru Cyfyngedig

Investor Report

For the quarter ended 31 December 2009

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 2009. 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.

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 9 months ended 31 December are as follows:

	Period to 31 December 2009 £m	Period to 31 December 2008 £m	Change
Turnover	511	495	+3%
Operating costs	196	204	-4%
EBITDA (before infrastructure renewals expenditure)	**315**	**291**	**+8%**
Net interest (excluding indexation and amortisation)	86	101	
Capital expenditure (before grants and contributions)	259	255	

General overview and business update cont'd

Operating profit before interest, tax, depreciation, infrastructure renewals and amortisation (EBITDA) for the 9 months to 31 December 2009 is slightly higher than last year – while the economic environment remains challenging, resulting in demand reductions and increased bad debt charges, the effect of these has been outweighed by the impact of price increases and falling power costs.

Turnover in the 9 months to 31 December 2009 was £511 million, as compared to £495 million in the 9 months to 31 December 2008. The increase is a reflection of the overall price increase of 5.4% (being the RPI+K increase allowed by Ofwat less the increase in the 'customer dividend' for the year, from £21 per customer to £22 per customer). During the period, 14,500 domestic customers switched to metered charging (2008: 18,000).

Operating costs (excluding depreciation and infrastructure renewals expenditure) were £196 million (2008: £204 million); the major variances result from power cost reductions (£4 million) offset by bad and doubtful debt charges (£3 million).

Net interest payable in the period (excluding fair value movements) was £68 million (2008: £129 million), including an indexation credit on index-linked debt of £18 million (2008: charge of £28 million). Indexation for the 9 months to December 2009 is based on the movement in the Retail Prices Index (RPI) from July 2008 (216.5) to July 2009 (213.4); as inflation was negative over this period, this results in a credit to the income statement.

Since the year-end the company has taken advantage of market conditions to fix the interest rate on £155 million of finance leases previously at floating rates of interest. Consequently, as at 31 December 2009, nearly all borrowings are at fixed or index-linked rates of interest (in part through the use of RPI swaps), which means that the company is insulated from 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 2009**	**31 March 2009**
Net debt	2,672	2,625
Regulatory capital value	3,756	3,626
Regulatory gearing	**71%**	**72%**

On Glas Cymru's acquisition of Welsh Water in May 2001, gearing stood at 93% (net debt/RCV). Since then, the financial position of the group has been steadily improved, such that gearing has fallen to 71% as at 31 December 2009 and 'financial reserves' (RCV less net debt) have exceeded £1 billion. The company's policy is to operate at a gearing level of around 70%.

General overview and business update cont'd

Capital investment programme

Capital investment (including infrastructure renewals expenditure) was £270 million before grants and contributions (2008: £255 million), bringing the total expenditure over the AMP4 period to date to £1,432 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 for the full year to 31 March 2010 will be around £350 million. This is 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 2009 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 Investor Report for the period to 31 March 2010, which will be published in June 2010, will contain projections covering the next regulatory period, from 2010 to 2015.

Credit ratings

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

As of 9 February 2010, the credit ratings of MBIA were B3 and BB+ from Moody's and S&P respectively, and MBIA is no longer rated by Fitch.

General overview and business update cont'd

Credit ratings cont'd

The credit ratings of the company's Class A Bonds, which are guaranteed by MBIA, revert to their higher underlying ratings of A3/A/A by Moody's, S&P and Fitch respectively. 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	A3	A	A
B	A3	A	A
C	Baa2	BBB+	BBB+

Moody's corporate family rating of Dŵr Cymru Cyfyngedig is A3, one of the strongest ratings in the industry.

Financing and liquidity

As at 31 December 2009, undrawn revolving credit facilities, EIB and KfW loans and cash (excluding the debt service reserve account) amounted to £510 million, giving the company a high degree of liquidity. The company's next expected bond maturity is of its Class C1 Bonds (£125 million) in March 2011.

On 15 December 2009, Dŵr Cymru Cyfyngedig drew down its £35 million loan facility with KfW IPEX-Bank GmbH.

General overview and business update cont'd

PR09 Regulatory Price Review

Ofwat has completed its Price Review for the period 2010-2015 ('PR09'), determining the price limits, investment allowances and service targets for each of the water companies. These were published on 26 November 2009 in Ofwat's Final Determination ("Future Water and Sewerage Charges 2010-2015: Final Determinations"). On 20 January 2010, Welsh Water announced that it had accepted the Final Determination. For further details, see the relevant section of the website, www.dwrcymru.com.

Outsourcing

At present, water operations and wastewater operations in north Wales are provided by United Utilities Operational Services and wastewater operations in south Wales are provided by Kelda Water Services.

Over the last nine months we have had lengthy discussions with United Utilities and Kelda Water Services, through the five yearly price and performance review of the contracts we have with both companies. We recognise and appreciate the considerable efforts made by both companies to meet our requirements. However, it has not proved possible to reach agreement with either company in relation to the terms for a continuation of the contracts for a further five years.

For further details, see the announcement of 9 February 2010 (www.dwrcymru.com/English/news/index.asp).

New non-executive director

On 26 October 2009, Professor Stephen Palmer, Head of Profession for Epidemiology at the Health Protection Agency, was appointed a non-executive director of Glas Cymru Cyfyngedig and Dŵr Cymru Cyfyngedig.

Investors

If you have any queries in relation to the content of this report, 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 2009 £m	9 months ended 31 December 2009 £m	9 months ended 31 December 2008 £m
Turnover	172.6	511.1	494.9
Less: operating expenses	(66.8)	(196.2)	(204.2)
Earnings before interest, taxation, depreciation and amortisation	105.8	314.9	290.7
Working capital movements	11.4	(11.8)	(18.3)
Non bond-related interest paid	0.8	(1.4)	(1.8)
Interest received	0.5	3.0	8.9
Net operating cash flow and interest received	118.5	304.7	279.5
New borrowings:			
European Investment Bank	-	-	25.0
KfW IPEX-Bank GmbH	35.0	35.0	-
Utilisation of reserves:			
Cash transferred to capex reserve	(58.9)	(162.7)	(127.8)
Cash utilised from capex reserve	58.9	162.7	127.8
Net cash utilised from other reserves	7.2	21.7	20.6
Capital expenditure:			
Net proceeds from disposal of assets	-	0.1	0.1
Infrastructure renewals expenditure	(14.6)	(51.3)	(60.4)
Non-infrastructure maintenance	(39.2)	(96.0)	(80.2)
Enhancement expenditure	(31.5)	(115.3)	(115.2)
Net cash flow after capital expenditure, new borrowings and reserve drawings	75.4	98.9	69.4
Transfer to debt service payment account	(46.4)	(106.6)	(116.3)
Principal repayments	(2.2)	(4.4)	(4.6)
Net cash flow after debt service	26.8	(12.1)	(51.5)
Free cash balances brought forward	56.5	95.4	85.4
Free cash balances carried forward	83.3	83.3	33.9

Consolidated debt service payments

	Payments due & made in 3 months ending 31 December 2009 £m	Amount accrued 31 December 2009 £m
Liquidity facility:		
Liquidity facility commitment fee	-	0.5
Interest on senior debt:		
Finance lease interest payments	-	51.5
A1 interest payments	-	15.6
A4 interest payments	5.7	2.8
A5 interest payments	1.8	0.9
A6 interest payments	-	1.0
B1 interest payments	-	16.6
B3 interest payments	3.5	1.7
B4 interest payments	2.0	1.0
B5 interest payments	0.4	0.2
European Investment Bank loan interest payments	0.3	-
KfW IPEX-Bank GmbH loan interest and commitment fee	0.1	-
Revolving credit facility commitment fees	0.1	-
Miscellaneous fees	-	0.5
	13.9	92.3
Interest rate swaps	2.9	-
RPI bond swap	-	-
VAT on finance lease payments	-	-
Senior interest payments	16.8	92.3
Interest on junior debt:		
C1 interest payments	-	7.5
	-	7.5
Total debt service payments	16.8	99.8

Glas notes principal balance reconciliation

	Credit rating[1]	Opening balance 1 October 2009 £m	New issues £m	Repayment £m	Indexation £m	Closing balance 31 December 2009 £m
Finance leases		892.1	-	-	-	892.1
Class A bonds[2]						
A1 notes	A3/A/A	350.0	-	-	-	350.0
A4 notes		324.3	-	-	2.5	326.8
A5 notes		104.0	-	-	1.5	105.5
A6 notes[3]		107.7	-	-	1.0	108.7
Class B bonds						
B1 notes	A3/A/A	325.0	-	-	-	325.0
B3 notes		157.4	-	-	1.2	158.6
B4 notes		91.8	-	-	1.3	93.1
B5 notes		53.9	-	-	0.4	54.3
Class C bonds						
C1 notes	Baa2/BBB+/BBB+	125.0	-	-	-	125.0
European Investment Bank loan		149.1	-	(2.2)	-	146.9
KfW IPEX-Bank GmbH loan		-	35.0	-	-	35.0
Local authority loans		2.5	-	-	-	2.5
		2,682.8	35.0	(2.2)	7.9	2,723.5

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

[2] *Guaranteed by MBIA rated B3/BB+/-. Class A bond ratings default to their higher underlying ratings of A3/A/A.*

[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 £8.7m reflects the principal accrual on the index-linked swap.*

Glas bank account movements

	Opening balance 1 October 2009 £m	Interest received £m	Deposits £m	Payments £m	Closing balance 31 December 2009 £m
Free cash balances:					
Receipts account	56.9	-	172.9	(170.1)	59.7
Payments account	(1.3)	-	459.9	(436.0)	22.6
Other bank accounts	0.9	0.5	1,305.3	(1,305.7)	1.0
	56.5	0.5	1,938.1	(1,911.8)	83.3
Debt service payment account:					
Debt service ledger	43.3	-	46.4	(16.8)	72.9
Capex reserve account	-	-	58.9	(58.9)	-
Customer payments account:					
Customer rebate ledger	14.5	-	-	(7.2)	7.3
	114.3	0.5	2,043.4	(1,994.7)	163.5

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 1.0)	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 (year to 31 March 2010 based on 2009 business plan)

(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	Actual Year to 31 March 2009 £m	*Projections* *Year to 31 March 2010 £m*
Income	576.5	602.7	648.6	684.2	*709*
Operating expenditure	(213.2)	(228.6)	(230.8)	(266.9)	*(276)*
Pre capital maintenance cash flows	363.3	374.1	417.8	417.3	*433*
Capital maintenance expenditure	(98.1)	(150.2)	(146.2)	(189.1)	*(167)*
Post capital maintenance cash flows	265.2	223.9	271.6	228.2	*266*
Net interest (excluding indexation)	(129.9)	(127.0)	(127.5)	(124.3)	*(115)*
Capital expenditure	(122.3)	(96.7)	(136.7)	(152.3)	*(183)*
Customer rebates	(23.0)	(24.7)	(25.7)	(27.0)	*(28)*
Pre-financing cash flows	(10.0)	(24.5)	(18.3)	(75.4)	*(60)*
Interest payable on senior debt:					
Finance leases	31.9	33.7	45.8	42.6	*22*
Class A	43.6	36.9	36.4	41.2	*38*
Class B	33.5	32.4	33.2	34.0	*34*
MBIA financial guarantee fees	4.7	3.6	3.7	3.6	*4*
Interest rate swaps	4.2	7.7	(0.2)	(7.9)	*4*
Authorised loans	5.4	8.5	8.3	7.2	*5*
Less interest receivable	(9.7)	(7.4)	(12.2)	(8.6)	*(3)*
Total net senior debt interest	113.7	115.4	115.0	112.1	*104*
Interest payable on junior debt:					
Class C	13.1	10.2	10.2	10.3	*10*
Class D	-	-			
Other	3.1	2.2	2.3	1.9	*1*
Total interest payable	129.9	127.8	127.5	124.3	*115*
Senior interest cover pre capital maintenance (trigger 2.0; default 1.6)	3.1	3.3	3.6	3.7	*4.2*
Total interest cover pre capital maintenance	2.8	2.9	3.3	3.4	*3.8*
Senior interest cover post capital maintenance (trigger 1.0)	2.3	2.0	2.4	2.0	*2.6*
Total interest cover post capital maintenance	2.0	1.8	2.1	1.8	*2.3*

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 (year to 31 March 2010 based on 2009 business plan)

(See important notice at the front of the document)	Actual As at 31 March 2006 £m	Actual As at 31 March 2007 £m	Actual As at 31 March 2008 £m	Actual As at 31 March 2009 £m	*Projections As at 31 March 2010 £m*
Senior gross debt:					
Finance leases	740	767	842	892	*884*
Class A	742	856	875	902	*898*
Class B	553	611	623	637	*647*
Net interest accrual on senior debt	29	84	56	54	*32*
EIB loan	60	135	131	151	*222*
Authorised loan facility	120	-	-	-	*76*
Total senior gross debt	2,244	2,453	2,527	2,636	*2,759*
Less: cash balances and authorised investments	(14)	(158)	(124)	(139)	*(150)*
Total senior net debt	2,230	2,295	2,403	2,497	*2,609*
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	2,625	*2,737*
Regulatory capital value (RCV)	3,042	3,310	3,529	3,626[1]	*3,717*
Reserves (RCV less total net debt)	683	876	998	1,001	*980*
Regulatory asset ratio:					
RAR (Senior)	73%	69%	68%	69%	*70%*
RAR (Senior + C) (trigger 90%; default 95%)	77%	73%	72%	72%	*74%*
RAR (Total debt)	78%	74%	72%	72%	*74%*

[1] as published by Ofwat (RD 06/09) on 14 May 2009 (incorporating amendments per Ofwat letter of 2 May 2008)

Income statement (unaudited)

	3 months ended 31 December 2009 £m	9 months ended 31 December 2009 £m	*9 months ended 31 December 2008 £m*
Turnover	172.6	511.1	494.9
Operating expenditure	(66.8)	(196.2)	(202.2)
EBITDA	105.8	314.9	292.7
Infrastructure renewals expenditure	(16.7)	(59.0)	(78.0)
Depreciation	(35.4)	(105.2)	(99.8)
Profit on disposal of fixed assets	-	0.1	0.1
Operating profit	53.7	150.8	115.0
Interest payable	(35.8)	(70.8)	(136.7)
Interest receivable	0.4	2.9	7.4
Fair value losses on financial instruments	(4.1)	15.5	(110.4)
Profit/(loss) before tax	14.2	98.4	(124.7)
Deferred taxation			
Adjustment in respect of prior years	-	(0.6)	2.2
(Charge)/credit at 28%	-	(23.9)	18.9
Effect of abolition of Industrial Buildings Allowances	-	-	(34.4)
Taxation	-	(24.5)	(13.3)
Profit/(loss) after tax	14.2	73.9	(138.0)

Statement of comprehensive income (unaudited)

	3 months ended 31 December 2009 £m	9 months ended 31 December 2009 £m	*9 months ended 31 December 2008 £m*
Profit/(loss) for the period	14.2	73.9	(138.0)
Actuarial loss in the pension scheme	-	(1.1)	(2.0)
Movement on related deferred tax asset	-	0.3	0.6
Total recognised gains/(losses) for the period	14.2	73.1	(139.4)

Balance sheet (unaudited)

	At 31 December 2009		At 31 March 2009	
	£m	£m	£m	£m
Fixed assets		3,121.6		3,026.2
Current assets and liabilities:				
Debtors and prepayments	125.4		107.1	
Creditors and accruals	(116.9)		(132.4)	
		8.5		(25.3)
Total assets less current liabilities		3,130.1		3,000.9
Financing liabilities:				
Bonds	(1,647.0)		(1,664.5)	
Finance leases	(892.1)		(892.1)	
European Investment Bank loan	(181.9)		(151.2)	
Other	(2.5)		(2.6)	
	(2,723.5)		(2,710.4)	
Net interest accrual	(111.7)		(54.5)	
	(2,835.2)		(2,764.9)	
Cash and cash equivalents:				
Receipts account	59.7		78.5	
Payments account	22.6		16.2	
Debt service payment account	72.9		14.9	
Customer payments account	7.3		29.0	
Other bank accounts	1.0		0.7	
	163.5		139.3	
Net debt		**(2,671.7)**		**(2,625.6)**
Derivative financial instruments		(142.2)		(157.8)
Provisions for liabilities and charges		(18.1)		(16.8)
Net assets before deferred tax		**298.1**		**200.7**
Deferred tax		(377.0)		(352.8)
Net liabilities		**(78.9)**		**(152.1)**