



Investor Report

For the quarter ended 31 December 2013

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General overview and business update

This quarterly Investor Report covers the three month period ending 31 December 2013. 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 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 months ended 31 December are as follows:

	9 months to 31 December 2013 £m	9 months to 31 December 2012 £m	Change
Revenue	554	540	+3%
Operating costs	222	213	+4%
EBITDA (before infrastructure renewals expenditure)	332	327	
Net interest (excluding indexation)	64	57	
Capital expenditure (before grants and contributions)	265	227	

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 2013 is broadly in line with the comparative period last year – Ofwat's RPI + K price increases are largely responsible for the rise in income of some £14 million, offset by an additional £9 million of operating costs.

Revenue in the nine months to 31 December 2013 was £554 million, as compared to £540 million in the nine months to 31 December 2012. The increase includes the impact of an overall price increase of 2.6% (being the RPI+K adjustment allowed by Ofwat). During the period, 13,000 domestic customers switched to metered charging (2012: 12,000).

Operating costs (excluding depreciation and infrastructure renewals expenditure) were £222 million (2012: £213 million) and have increased by 4% principally due to increased energy costs, a higher bad debt charge, additional expenditure necessary to maintain operations during the failure of the Daniel Contracting Limited business and the impact of general inflation.

Net interest payable in the period (excluding fair value movements) was £64 million (2012: £57 million), including an indexation charge on index-linked debt of £23 million (2012: £25 million).

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

£m	31 December 2013	31 March 2013
Net debt	2,778	2,744
Regulatory capital value	4,461	4,344
'Financial reserves'	1,683	1,600
Regulatory gearing	62%	63%

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 has fallen to 62% as at 31 December 2013 and 'financial reserves' (RCV less net debt) are over £1.6 billion.

General overview and business update cont'd

Capital investment programme

Capital investment (including infrastructure renewals expenditure) was £265 million before grants and contributions (2012: £227 million). Of that £265 million, £144 million is reported as capital maintenance as defined in the CTA, while for regulatory purposes £222 million is classed as capital maintenance. We have invested £1,108 million to date into our AMP5 capital programme; during the five year regulatory period to 2015 we plan to invest £1.5 billion to safeguard drinking water quality, protect our environment from pollution, improve customer service and deliver further cost savings.

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 2015. These projected ratios 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 9 and 10). 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.

Credit ratings

The strong credit quality of the business is reflected in credit ratings which are now the highest in the UK utility sector. The ratings of the company’s bonds are shown in the table below. All ratings have stable outlook.

Bond Class	Moody’s	S&P	Fitch
A*	A3	A	A
B	A3	A	A

*The credit ratings of the company’s Class A Bonds, which are guaranteed by MBIA (B/B1/-), revert to their higher underlying ratings of A3/A/A by Moody’s Investor Service (Moody’s), Standard & Poor’s (S&P) and Fitch Ratings (Fitch) respectively. On 29 January 2014, Fitch revised the UK Water Sector outlook to negative following guidance related to risk and rewards published by Ofwat for the 2014 price review.

Financing and liquidity

As at 31 December 2013, undrawn credit facilities and cash (excluding the debt service reserve account deposits of £73 million) amounted to £270 million, including undrawn revolving credit and European Investment Bank facilities of £140 million. The company drew £75 million of its loan facility with the European Investment Bank on 16 December 2013. In line with prudent policies approved by the board, cash is invested in AAA-rated liquidity funds and bonds, and banks subject to minimum short-term rating criteria of A1/P1/F1.

General overview and business update cont'd

Account Bank Agreements

Both Dŵr Cymru Cyfyngedig (DCC) and Dŵr Cymru (Financing) Limited (“Issuer”) have account bank agreements with National Westminster Bank plc (“Natwest”). Under these agreements, Natwest is required to hold a minimum short term rating of at least two of A1/P1/F1 (S&P/Moody’s/Fitch). On 7 November 2013, Natwest’s short term rating was downgraded by S&P from A1 to A2, so that the bank’s short term rating is now A2/P2/F1. The security trustee has been notified of the downgrade and, after consultation with secured creditors, has granted a temporary waiver of the requirement to terminate the appointment of Natwest under the two account bank agreements. The company intends to seek the consent of the security trustee and secured creditors to permanently relax the credit rating criteria for Natwest as an account bank.

2014 Price Review

On 25 July 2013, Ofwat published its final methodology and expectations for companies’ business plans for the price control period 2015-2020. The company submitted its business plan on 2 December 2013. Ofwat has subsequently published its ‘Risk and Reward’ guidance for companies on 27 January 2014 (http://www.ofwat.gov.uk/pricereview/pr14/prs_web201307finalapproach).

Investors

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

Consolidated cash flow

	9 months ended 31 December 2013 £m	9 months ended 31 December 2012 £m
Revenue	553.8	540.3
Less: operating expenses	(222.2)	(213.3)
Earnings before interest, taxation, depreciation and amortisation	331.6	327.0
Working capital movements	15.8	(4.4)
Non bond-related interest paid	(1.3)	(2.5)
Interest capitalised in accordance with IAS 23	(8.1)	(5.7)
Interest received	5.7	7.0
Net operating cash flow and interest received	343.7	321.4
New borrowings:		
European Investment Bank	75.0	
Utilisation of reserves:		
Cash transferred to capex reserve	(158.5)	(165.3)
Cash utilised from capex reserve	83.5	150.3
Capital expenditure:		
Net profit on disposal of assets	0.3	0.1
Infrastructure renewals expenditure	(59.3)	(81.8)
Non-infrastructure maintenance	(84.9)	(54.0)
Enhancement expenditure	(113.0)	(92.6)
Net cash flow after capital expenditure, new borrowings and reserve drawings	86.8	78.1
Transfer to debt service payments account	(115.6)	(88.2)
Principal repayments	(14.1)	(119.0)
Net cash flow after debt service	(42.9)	(129.1)
Free cash balances brought forward	97.7	242.3
Free cash balances carried forward	54.8	113.2

Consolidated debt service payments

	Payments due & made in 9 months ending 31 December 2013 £m	Amount accrued 31 December 2013 £m
Liquidity facility:		
Liquidity facility commitment fee	0.1	-
Interest on senior debt:		
Finance lease interest payments	2.7	43.6
A1 interest payments	-	15.7
A4 interest payments	6.7	3.2
A5 interest payments	2.1	1.0
A6 interest payments	-	0.3
B1 interest payments	-	16.8
B3 interest payments	4.0	2.0
B4 interest payments	2.3	1.2
B5 interest payments	0.4	0.2
B6 interest payments	2.8	1.3
European Investment Bank loan interest payments	0.7	0.3
KfW IPEX-Bank GmbH loan interest payments	0.1	-
Revolving credit facility commitment fees	0.1	-
Miscellaneous fees	0.6	0.2
	22.6	85.8
Interest rate swaps	3.4	-
Senior interest payments	26.0	85.8
Total debt service payments	26.0	85.8

Glas notes principal balance reconciliation

	Credit rating ¹	Opening balance 1 October 2013 £m	New issues £m	Repayment £m	Indexation £m	Closing balance 31 December 2013 £m
Finance leases		616.3	-	(2.7)	-	613.6
Class A bonds²						
A1 notes	A3/A/A	350.0	-	-	-	350.0
A4 notes		379.3	-	-	3.0	382.3
A5 notes		121.6	-	-	0.9	122.5
A6 notes ³		126.0	-	-	1.0	127.0
Class B bonds						
B1 notes	A3/A/A	325.0	-	-	-	325.0
B3 notes		184.1	-	-	1.4	185.5
B4 notes		107.3	-	-	0.8	108.1
B5 notes		63.0	-	-	0.5	63.5
B6 notes		297.5	-	-	0.3	297.8
European Investment Bank loan		204.2	75.0	(4.5)	-	274.7
KfW IPEX-Bank GmbH loan		35.0	-	-	-	35.0
Local authority loans		1.2	-	-	-	1.2
		2,810.5	75.0	(7.2)	7.9	2,886.2

¹ Moody's/S&P/Fitch.

² Guaranteed by MBIA rated B/B3/-. 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 £27.0m reflects the principal accrual on the index-linked swap.

Glas bank account movements

	Opening balance 1 October 2013 £m	Interest received £m	Deposits £m	Payments £m	Closing balance 31 December 2013 £m
Free cash balances:					
Receipts account	54.8	-	277.0	(268.1)	63.7
Payments account	18.0	-	392.3	(422.3)	(12.0)
Other bank accounts	(19.3)	1.2	525.6	(504.4)	3.1
	53.5	1.2	1,194.9	(1,194.8)	54.8
Debt service payments account:					
Debt service ledger	58.9	-	31.5	(26.0)	64.4
Insurance proceeds ledger	8.5	-	-	-	8.5
	67.4		31.5	(26.0)	72.9
Capex reserve account	-	-	106.1	(31.1)	75.0
	120.9	1.2	1,332.5	(1,251.9)	202.7

Interest cover ratio (ICR) – 5 years to 31 March 2015 (based on 2013 business plan)

(See important notice at the front of the document)

	Actual			Projections	
	Year to 31 March 2011 £m	Year to 31 March 2012 £m	Year to 31 March 2013 £m	Year to 31 March 2014 £m	Year to 31 March 2015 £m
Income	677	695	716	730	763
Operating expenditure	(265)	(273)	(295)	(299)	(301)
Pre capital maintenance cash flows	412	422	421	431	462
Capital maintenance expenditure	(97)	(169)	(203)	(141)	(129)
Post capital maintenance cash flows	315	253	219	290	333
Net interest (excluding indexation)	(132)	(140)	(102)	(124)	(133)
Capital expenditure	(131)	(84)	(122)	(192)	(169)
Pre-financing cash flows	52	29	(5)	(26)	31
Interest payable on senior debt:					
Finance leases	(2)	9	(4)	31	32
Class A	41	39	40	40	40
Class B	37	40	41	42	43
MBIA financial guarantee fees	4	4	4	5	5
Interest rate swaps	41	45	12	9	9
Authorised loans	2	4	12	4	7
Less interest receivable	(4)	(5)	(7)	(7)	(3)
Total net senior debt interest	120	136	98	124	133
Interest payable on junior debt:					
Class C (including £6m premium on early redemption)	9	-	-	-	-
Other	3	4	4	-	-
Total interest payable	132	140	102	124	133
Senior interest cover pre capital maintenance (trigger 2.0; default 1.6)	3.4	3.1	4.3	3.5	3.5
Total interest cover pre capital maintenance	3.1	3.0	4.1	3.5	3.5
Senior interest cover post capital maintenance (trigger 1.0)	2.6	1.9	2.2	2.3	2.5
Total interest cover post capital maintenance	2.4	1.8	2.2	2.3	2.5

Regulatory asset ratio (RAR) – 5 years to 31 March 2015 (based on 2013 business plan)

(See important notice at the front of the document)

	Actual			Projections	
	As at 31 March 2011 £m	As at 31 March 2012 £m	As at 31 March 2013 £m	As at 31 March 2014 £m	As at 31 March 2015 £m
Senior gross debt:					
Finance leases	742	734	616	608	559
Class A	922	950	969	985	1,003
Class B	796	949	969	992	1,012
Net interest accrual on senior debt	56	102	99	38	47
Authorised loans	248	260	246	308	392
Total senior gross debt	2,764	2,995	2,899	2,931	3,013
Less: cash balances and authorised investments	98	(301)	(157)	(103)	(173)
Total senior net debt	2,666	2,694	2,742	2,828	2,840
Local authority loans	2	2	1	1	1
Total net debt	2,668	2,696	2,744	2,829	2,841
Regulatory capital value (RCV)	3,980	4,171	4,344	4,493	4,745¹
Reserves (RCV less total net debt)	1,312	1,475	1,600	1,664	1,904
Regulatory asset ratio:					
RAR (Senior) (trigger 90%; default 95%)	67%	65%	63%	63%	60%
RAR (Total debt)	67%	65%	63%	63%	60%

¹ RCV at 31 March 2015 anticipates an adjustment incorporating an assumed movement in COPI relative to RPI during the five-year period.

Income statement (unaudited)

	9 months ended 31 December 2013 £m	9 months ended 31 December 2012 £m
Revenue	553.8	540.3
Operating expenditure	(222.2)	(213.3)
EBITDA	331.6	327.0
Infrastructure renewals expenditure	(58.5)	(83.9)
Depreciation	(122.4)	(119.1)
Operating profit	150.7	124.0
Interest payable	(69.8)	(63.3)
Indexation of index-linked debt	(23.4)	(25.4)
Interest receivable	5.7	6.7
Fair value gains on financial instruments	96.4	(6.6)
Profit before tax	159.6	35.4
Taxation	10.2	(2.0)
Profit after tax	169.8	33.4

Statement of comprehensive income (unaudited)

	9 months ended 31 December 2013 £m	9 months ended 31 December 2012 £m
Profit for the period	169.8	33.4
Actuarial gain in the pension scheme	4.6	0.5
Movement on related deferred tax asset	(1.7)	(2.9)
Total recognised gains for the period	172.7	31.0

Balance sheet (unaudited)

	At 31 December 2013		At 31 March 2013	
	£m	£m	£m	£m
Fixed assets		3,490.2		3,402.2
Current assets and liabilities:				
Debtors and prepayments	246.9		533.7	
Creditors and accruals	(317.9)		(610.4)	
		(71.0)		(76.7)
Total assets less current liabilities		3,419.2		3,325.5
Financing liabilities:				
Bonds	(1,961.7)		(1,938.4)	
Finance leases	(613.6)		(616.3)	
Bank loans (EIB, KfW)	(309.8)		(246.0)	
Other	(1.2)		(1.3)	
	(2,886.3)		(2,802.0)	
Net interest accrual	(94.6)		(98.8)	
	(2,980.9)		(2,900.8)	
Cash and cash equivalents:				
Receipts account	63.7		74.2	
Payments account	(12.0)		20.7	
Capex reserve account	75.0		-	
Debt service payments account	72.9		59.7	
Other bank accounts	3.1		2.8	
	202.7		157.4	
Net debt		(2,778.2)		(2,743.4)
Derivative financial instruments		(262.8)		(359.2)
Provisions for liabilities and charges		(44.5)		(53.4)
Net assets before deferred tax		333.7		169.5
Deferred tax		(235.4)		(243.9)
Net assets/(liabilities)		98.3		(74.4)