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Glas Cymru Cyfyngedig

Investor Report

For the quarter ended 30 June 2014

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General overview and business update

This quarterly Investor Report covers the three month period ending 30 June 2014. 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 three months ended 30 June are as follows:

	3 months to 30 June 2014 £m	**3 months to 30 June 2013 £m**	**Change**
Revenue	186	183	+2%
Operating costs	75	76	-1%
EBITDA (before infrastructure renewals expenditure)	**111**	**107**	
Net interest (excluding indexation)	13	22	
Capital expenditure (before grants and contributions)	87	82	

General overview and business update cont'd

Operating profit before interest, tax, depreciation, infrastructure renewals and amortisation (EBITDA) for the three months to 30 June 2014 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 £3 million.

Revenue in the three months to 30 June 2014 was £186 million, as compared to £183 million in the three months to 30 June 2013. The increase includes the impact of an overall price increase of 2.0% (being the RPI+K adjustment allowed by Ofwat). During the period, 5,000 domestic customers switched to metered charging (2013: 5,000).

Operating costs (excluding depreciation and infrastructure renewals expenditure) at £75 million (2013: £76 million) have remained stable in line with the comparative period last year; a reduction of 1% principally due to the receipt of business rates rebates.

Net interest payable in the period (excluding fair value movements) was £22 million (2013: £29 million), including an indexation charge on index-linked debt of £8 million (2013: £8 million). An accounting profit of £9m has been recognised following the termination of finance leases.

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

£m	**30 June 2014**	**31 March 2014**
Net debt	2,819	2,821
Regulatory capital value	4,491	4,468
'Financial reserves'	**1,672**	**1,647**
Regulatory gearing	62.8%	62.9%

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 62.8% as at 30 June 2014 and 'financial reserves' (RCV less net debt) are nearly £1.7 billion.

General overview and business update cont'd

Capital investment programme

Capital investment (including infrastructure renewals expenditure) was £87 million before grants and contributions (2013: £82 million). Of that £87 million, £49 million is reported as capital maintenance as defined in the CTA, while for regulatory purposes £74 million is classed as capital maintenance. We have invested £1,195 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/Ba2/-), 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 17 July 2014, following receipt of the company's draft determination on 30 May 2014, Fitch has affirmed the rating of our bonds as A with a stable outlook.

Financing and liquidity

As at 30 June 2014, undrawn credit facilities and cash (excluding the debt service reserve account deposits of £45 million) amounted to £184 million, including undrawn revolving credit facilities of £170 million. 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.

On 9 June 2014 the company terminated five former Santander leases at a cost of £47 million and at a discount to their book value. The company has recognised a £9 million accounting profit in the three months to 30 June 2014.

General overview and business update cont'd

Dŵr Cymru (Financing) Limited has a special liquidity facility of £135 million which it is required to maintain in order to meet certain group interest and other obligations that cannot be funded through the operating cashflow of the group, in the event of a standstill being declared by the Security Trustee. The facility is split equally between four providers : BNP Paribas, HSBC, J P Morgan and National Australia Bank.

On 19 May 2014, the company entered into a new £60 million five year revolving credit facility with BNP Paribas with an option to continue for a further year. The existing £20 million facility was cancelled.

On 6 August 2014, the company entered into further five year revolving credit facilities of £20 million each with the Royal Bank of Scotland, HSBC and J P Morgan, all with options to continue for a further year. The existing facility with these banks were also cancelled.

The company is in the process of agreeing a further £230 million loan facility with the European Investment Bank in respect of AMP5 capital expenditure. The completion of the loan facility is subject to EIB Board approval and finalisation of loan documentation.

2014 Price Review

On 30 May 2014 Ofwat published its draft determination for Dŵr Cymru (http://www.ofwat.gov.uk/pricereview/pr14/draftdet/). The draft determination sets out the proposed prices the company can charge its customers for water and sewerage services from 2015-2020. Under the plans submitted, Dŵr Cymru will decrease customer bills by 5% in real terms over the next price control period 2015-2020 while investing more than £2.5 billion to maintain and improve services for customers and the environment. The company submitted representations for the draft determination on 5 July 2014. Ofwat are planning to issue their final determination on 12 December 2014.

Consolidated cash flow

	3 months ended 30 June 2014 £m	3 months ended 30 June 2013 £m
Revenue	186.4	183.1
Less: operating expenses	(74.9)	(75.7)
Earnings before interest, taxation, depreciation and amortisation	111.5	107.4
Working capital movements	11.5	6.1
Non bond-related interest paid	(0.6)	(0.5)
Interest capitalised in accordance with IAS 23	(1.1)	(1.5)
Interest received	1.0	3.6
Net operating cash flow and interest received	122.3	115.1
Utilisation of reserves:		
Cash transferred to capex reserve	(2.3)	(26.2)
Cash utilised from capex reserve	29.3	26.2
Capital expenditure:		
Net profit on disposal of assets	(0.1)	0.1
Infrastructure renewals expenditure	(20.1)	(26.6)
Non-infrastructure maintenance	(28.1)	(25.4)
Enhancement expenditure	(34.5)	(27.0)
Net cash flow after capital expenditure, new borrowings and reserve drawings	66.5	36.2
Transfer to debt service payments account	(38.0)	(39.9)
Principal repayments	(59.6)	(4.5)
Net cash flow after debt service	(31.1)	(8.2)
Free cash balances brought forward	22.5	97.7
Free cash balances carried forward	(8.6)	89.5

Consolidated debt service payments

	Payments due & made in 3 months ending 30 June 2014 £m	Amount accrued 30 June 2014 £m
Liquidity facility:		
Liquidity facility commitment fee	0.1	-
Interest on senior debt:		
Finance lease interest payments	7.5	43.1
A1 interest payments	-	5.2
A4 interest payments	-	3.3
A5 interest payments	-	1.1
A6 interest payments	4.4	0.3
B1 interest payments	-	5.5
B3 interest payments	-	2.0
B4 interest payments	-	1.2
B5 interest payments	-	0.2
B6 interest payments	-	1.4
European Investment Bank loan interest payments	1.3	0.2
Revolving credit facility commitment fees	0.3	-
Miscellaneous fees	1.5	0.2
Total debt service payments	15.1	63.7

Glas notes principal balance reconciliation

	Credit rating[1]	Opening balance 1 April 2014 £m	Repayment £m	Indexation £m	Closing balance 30 June 2014 £m
Finance leases		571.2	(55.0)	-	516.2
Class A bonds[2]					
A1 notes	A3/A/A	350.0	-	-	350.0
A4 notes		385.4	-	2.2	387.6
A5 notes		125.4	-	0.7	126.1
A6 notes[3]		128.1	-	0.7	128.8
Class B bonds					
B1 notes	A3/A/A	325.0	-	-	325.0
B3 notes		187.0	-	1.1	188.1
B4 notes		110.6	-	0.6	111.2
B5 notes		64.0	-	0.4	64.4
B6 notes		301.5	-	2.6	304.1
European Investment Bank loan		272.6	(4.5)	-	268.1
KfW IPEX-Bank GmbH loan		35.0	-	-	35.0
Local authority loans		1.1	(0.1)	-	1.0
		2,856.9	(59.6)	8.3	2,805.6

[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 £28.8m reflects the principal accrual on the index-linked swap.**

Glas bank account movements

	Opening balance 1 April 2014 £m	Interest received £m	Deposits £m	Payments £m	Closing balance 30 June 2014 £m
Free cash balances:					
Receipts account	81.9	-	197.1	(219.6)	59.4
Payments account	(64.7)	-	486.7	(495.6)	(73.6)
Other bank accounts	5.3	1.1	297.0	(298.0)	5.4
	22.5	1.1	980.8	(1,013.2)	(8.8)
Debt service payments account:					
Debt service ledger	13.4	-	38.0	(15.1)	36.3
Insurance proceeds ledger	8.5	-	-	-	8.5
	21.9		38.0	(15.1)	44.8
Capex reserve account	49.9	-	2.3	(29.3)	22.9
	94.3	1.1	1,021.1	(1,057.6)	58.9

Interest cover ratio (ICR) – 5 years to 31 March 2015 (based on 2014 business plan)

(See important notice at the front of the document)	Actual				Projection
	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	737	742
Operating expenditure	(265)	(273)	(295)	(296)	(304)
Pre capital maintenance cash flows	412	422	421	441	438
Capital maintenance expenditure	(97)	(169)	(203)	(185)	(174)
Post capital maintenance cash flows	315	253	219	256	264
Net interest (excluding indexation)	(132)	(140)	(102)	(124)	(135)
Capital expenditure	(131)	(84)	(122)	(155)	(156)
Pre-financing cash flows	52	29	(5)	(23)	(27)
Interest payable on senior debt:					
Finance leases	(2)	9	(4)	5	31
Class A	41	39	40	44	40
Class B	37	40	41	42	43
MBIA financial guarantee fees	4	4	4	4	5
Interest rate swaps	41	45	12	29	13
Authorised loans	2	4	12	2	7
Less interest receivable	(4)	(5)	(7)	(6)	(4)
Total net senior debt interest	120	136	98	120	135
Interest payable on junior debt:					
Class C (including £6m premium on early redemption)	9	-	-	-	-
Other	3	4	4	4	-
Total interest payable	132	140	102	124	135
Senior interest cover pre capital maintenance (trigger 2.0; default 1.6)	3.4	3.1	4.3	3.7	3.2
Total interest cover pre capital maintenance	3.1	3.0	4.1	3.6	3.2
Senior interest cover post capital maintenance (trigger 1.0)	2.6	1.9	2.2	2.1	2.0
Total interest cover post capital maintenance	2.4	1.8	2.2	2.0	2.0

Regulatory asset ratio (RAR) – 5 years to 31 March 2015 (based on 2014 business plan)

(See important notice at the front of the document)	Actual As at 31 March 2011 £m	Actual As at 31 March 2012 £m	Actual As at 31 March 2013 £m	Actual As at 31 March 2014 £m	Projection As at 31 March 2015 £m
Senior gross debt:					
Finance leases	742	734	616	571	563
Class A	922	950	969	989	1,004
Class B	796	949	969	988	1,013
Net interest accrual on senior debt	56	102	99	58	46
Authorised loans	248	260	246	307	367
Total senior gross debt	2,764	2,995	2,899	2,914	2,993
Less: cash balances and authorised investments	98	(301)	(157)	(94)	(101)
Total senior net debt	2,666	2,694	2,742	2,819	2,892
Local authority loans	2	2	1	1	1
Total net debt	2,668	2,696	2,744	2,821	2,893
Regulatory capital value (RCV)	3,980	4,171	4,344	4,468	4,802[1]
Reserves (RCV less total net debt)	1,312	1,475	1,600	1,647	1,909
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)

	3 months ended 30 June 2014 £m	3 months ended 30 June 2013 £m
Revenue	186.4	183.1
Operating expenditure	(74.9)	(75.7)
EBITDA	111.5	107.4
Infrastructure renewals expenditure	(20.5)	(26.4)
Depreciation	(44.2)	(40.6)
Operating profit	46.8	40.4
Interest payable	(14.4)	(25.2)
Indexation of index-linked debt	(8.3)	(7.7)
Interest receivable	1.0	3.6
Fair value gains on financial instruments	1.7	74.6
Profit before tax	26.8	85.7
Taxation	-	-
Profit after tax	26.8	85.7

Statement of comprehensive income (unaudited)

	3 months ended 30 June 2014 £m	3 months ended 30 June 2013 £m
Profit for the period	26.8	85.7
Actuarial gain in the pension scheme	-	-
Movement on related deferred tax asset	-	-
Total recognised gains for the period	26.8	85.7

Balance sheet (unaudited)

	At 30 June 2014		At 31 March 2014	
	£m	£m	£m	£m
Fixed assets		3,546.5		3,526.2
Current assets and liabilities:				
Debtors and prepayments	436.3		534.4	
Creditors and accruals	(514.5)		(615.7)	
		(78.2)		(81.3)
Total assets less current liabilities		3,468.3		3,444.9
Financing liabilities:				
Bonds	(1,985.3)		(1,976.9)	
Finance leases	(516.4)		(571.3)	
Bank loans (EIB, KfW)	(303.1)		(307.6)	
Other	(0.9)		(1.1)	
	(2,805.7)		(2,856.9)	
Net interest accrual	(72.1)		(58.5)	
	(2,877.8)		(2,915.4)	
Cash and cash equivalents:				
Receipts account	59.4		81.9	
Payments account	(73.6)		(64.7)	
Capex reserve account	22.9		49.9	
Debt service payments account	44.8		21.9	
Other bank accounts	5.4		5.3	
	58.9		94.3	
Net debt		**(2,818.9)**		**(2,821.1)**
Derivative financial instruments		(263.3)		(265.0)
Provisions for liabilities and charges		(16.8)		(17.6)
Net assets before deferred tax		**369.3**		**341.2**
Deferred tax		(242.8)		(241.3)
Net assets/(liabilities)		**126.5**		**99.9**