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Glas Cymru Cyfyngedig

Investor Report

For the quarter ended 30 September 2015

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 persons should act or rely on it (except as provided in the CTA). 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).

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General overview and business update

This quarterly Investor Report covers the three month period ending 30 September 2015. 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 six months ended 30 September are as follows:

	6 months to 30 September 2015 £m	**6 months to 30 September 2014 £m**	**Change**
Revenue	368	375	-2%
Operating costs	(142)	(144)	-1%
Business rates refund	20	-	
EBITDA (before IRE)	**246**	**231**	
Net interest (excluding indexation)	(49)	(41)	
Capital expenditure (before grants and contributions)	(123)	(174)	

General overview and business update cont'd

Operating profit before interest, tax, depreciation, infrastructure renewals and amortisation (EBITDA) for the six months to 30 September 2015 is £15 million higher than the comparative period last year – business rates rebates are largely responsible for the reduction in operating costs by some £20 million which is offset in part by the reduction in revenue following Ofwat's PR14 price determination.

Revenue in the six months to 30 September 2015 was £368 million, as compared to £375 million in the six months to 30 September 2014. There has been an overall price decrease of 1.9% driven by the RPI+K adjustment allowed by Ofwat (reduction of 1%) and customers opting to switch to a metered supply.

Operating costs (excluding depreciation and infrastructure renewals expenditure) of £122 million (2014: £144 million) are lower in comparison with the same period last year; the impact of general inflation has been more than offset by savings arising from IT contract insourcing and on-going operational cost efficiencies. In addition, £20 million of business rates rebates have arisen from the company's challenge of the 2005 water networks assessment.

Net interest payable in the period (excluding fair value movements) was £49 million (2014: £41 million), excluding an indexation credit on index-linked debt of £1 million (2014: indexation charge £13 million). Net interest payable in 2014 included an £8 million accounting profit on lease termination.

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

£m	**30 September 2015**	**31 March 2015**
Net debt	2,824	2,885
Regulatory capital value	4,916	4,832
'Financial reserves'	**2,092**	**1,947**
Regulatory gearing	57.4%	59.7%

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 57% as at 30 September 2015 and 'financial reserves' (RCV less net debt) exceed £2 billion.

General overview and business update cont'd

Capital investment programme

Capital investment (including infrastructure renewals expenditure) before grants and contribution was £123 million (2014: £174 million). Of that £123 million, £85 million is reported as capital maintenance as defined in the CTA, while for regulatory purposes £101 million is classed as capital maintenance.

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 for the five years to 31 March 2020. These projected ratios are derived from Glas Cymru's 2015 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 are better than the "trigger" and "default" 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 remain the highest in the UK utility sector. The ratings of the company's bonds are shown in the table below.

Bond Class	Moody's	S&P	Fitch
A*	A3 (+ve)	A	A
B	A3 (+ve)	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.

The Moody's A3 rating was placed on positive outlook on 27 February 2015. The company's policy is to target maintaining ratings at an "A" grade. On 3 September 2015, Standard and Poor's affirmed our A rating with stable outlook.

Financing and liquidity

As at 30 September 2015, undrawn credit facilities and cash (excluding the debt service reserve account deposits of £53 million) amounted to £316 million, including undrawn EIB and revolving credit facilities of £190 million. In line with prudent policies approved by the board, cash is invested in AAA rated liquidity funds and bonds, The Royal Bank of Scotland as the group's account bank and banks subject to minimum short-term rating criteria of A1/P1/F1.

On 21 October 2015 we increased our revolving credit facility with Royal Bank of Scotland from £20 million to £50 million. £130 million of our revolving credit facilities have also been extended by one year to 2020.

On 11 November 2015 we signed a £60 million term loan facility with KfW.

General overview and business update cont'd

Gearing and distribution policy

The Board has approved a regulatory gearing policy (being the ratio of net debt to regulatory capital value) of around 60%. Later this financial year, the Board will consider its customer distribution policy as it is likely that there will be headroom to make distributions while maintaining gearing at 60%. A customer rebate of £6.2 million to fund social tariffs for financially disadvantaged customers has already been transferred to the Customer Payments Account for the year ended 31 March 2016 and is included in the "Transfers to 'customer reserves'" of £68 million for the year on page 9 of this report.

Consolidated cash flow

	6 months ended 30 September 2015 £m	6 months ended 30 September 2014 £m
Revenue	367.8	374.6
Less: operating expenses	(122.2)	(143.9)
Earnings before interest, taxation, depreciation and amortisation	245.6	230.7
Working capital movements	21.1	6.0
Non bond-related interest paid	(1.0)	(1.0)
Interest capitalised in accordance with IAS 23	(2.1)	(3.8)
Interest received	3.8	1.6
Net operating cash flow and interest received	267.4	233.5
Utilisation of reserves:		
Cash transferred to capex reserve	(6.3)	(10.2)
Cash utilised from capex reserve	57.6	60.1
Net cash utilised from other reserves	3.7	-
Capital expenditure:		
Infrastructure renewals expenditure	(31.7)	(36.3)
Non-infrastructure maintenance	(57.2)	(47.9)
Enhancement expenditure	(32.6))	(81.8)
Net cash flow after capital expenditure, new borrowings and reserve drawings	200.9	117.4
Transfer to debt service payments account	(108.7)	(61.7)
Principal repayments	(39.6)	(61.9)
Net cash flow after debt service	52.6	(6.2)
Free cash balances brought forward	(6.7)	22.5
Free cash balances carried forward	45.9	16.3

Consolidated debt service payments

	Payments due & made in 3 months ending 30 September 2015 £m	Amount accrued 30 September 2015 £m
Liquidity facility:		
Liquidity facility commitment fee	0.1	0.1
Interest on senior debt:		
Finance lease interest payments	-	47.4
A1 interest payments	-	10.6
A4 interest payments	6.9	-
A5 interest payments	2.2	-
A6 interest payments	-	0.7
B1 interest payments	-	11.3
B3 interest payments	4.2	-
B4 interest payments	2.4	-
B5 interest payments	0.5	-
B6 interest payments	2.9	-
European Investment Bank and KfW loan interest payments	0.3	1.0
KfW IPEX-Bank GmbH loan	35.0	-
Revolving credit facility commitment fees	0.1	-
MBIA wrapping fees	-	-
Miscellaneous fees	-	0.1
Interest rate swaps	5.0	-
RPI bond swaps	0.9	-
Total debt service payments	**60.5**	**71.2**

Glas notes principal balance reconciliation

	Credit rating[1]	Opening balance 1 July 2015 £m	Repayment £m	Indexation £m	Closing balance 30 September 2015 £m
Finance leases		507.2	-	-	507.2
Class A bonds[2]					
A1 notes	A3/A/A	350.0	-	-	350.0
A4 notes		394.6	-	(0.4)	394.2
A5 notes		128.5	-	(2.1)	126.4
A6 notes[3]		131.2	-	(0.2)	131.0
Class B bonds					
B1 notes	A3/A/A	325.0	-	-	325.0
B3 notes		191.5	-	(0.2)	191.3
B4 notes		113.3	-	(1.8)	111.5
B5 notes		65.5	-	(0.1)	65.4
B6 notes		309.6	-	(1.1)	308.5
European Investment Bank loan		414.3	(2.3)	1.3	413.3
KfW IPEX-Bank GmbH loan		35.0	(35.0)	-	-
Local authority loans		0.9	-	-	0.9
		2,966.6	(37.3)	(4.6)	2,924.7

[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 £31.0m reflects the principal accrual on the index-linked swap.

Glas bank account movements

	Opening balance 1 July 2015 £m	Interest received £m	Deposits £m	Payments £m	Closing balance 30 September 2015 £m
Free cash balances:					
Receipts account	53.3	-	182.4	(184.9)	50.8
Payments account	(43.0)	-	441.2	(409.2)	(11.0)
Other bank accounts	5.1	2.5	181.0	(182.5)	6.1
	15.4	2.5	804.6	(776.6)	45.9
Debt service payments account:					
Debt service ledger	27.4	-	78.0	(60.5)	44.9
Insurance proceeds ledger	8.5	-	-	-	8.5
	35.9	-	78.0	(60.5)	53.4
Capex reserve account	104.8	-	2.8	(30.1)	77.5
Customer payments account:					
Customer rebate ledger	4.6	-	-	(2.1)	2.5
	160.7	2.5	885.4	(869.3)	179.3

Interest cover ratio (ICR) – 5 years to 31 March 2020

(See important notice at the front of the document)	Projection Year to 31 March 2016 £m	Year to 31 March 2017 £m	Year to 31 March 2018 £m	Year to 31 March 2019 £m	Year to 31 March 2020 £m
Income	748	758	771	784	799
Operating expenditure	(302)	(305)	(307)	(305)	(310)
Pre capital maintenance cash flows	446	453	464	479	489
Capital maintenance expenditure	(198)	(206)	(217)	(220)	(227)
Post capital maintenance cash flows	248	247	247	259	262
Net interest (excluding indexation and capitalisation)	(119)	(124)	(128)	(131)	(135)
Capital expenditure	(135)	(148)	(153)	(110)	(101)
Transfers to 'customer reserves'[1]	(68)[2]	(52)	(44)	(95)	(105)
Pre-financing cash flows	(74)	(77)	(78)	(77)	(79)
Interest payable on senior debt:					
Finance leases	6	8	8	10	11
Class A	41	42	42	42	43
Class B	42	43	43	44	44
MBIA financial guarantee fees	6	6	6	6	6
Interest rate swaps	22	22	20	18	17
Authorised loans	6	6	13	15	18
Less interest receivable	(4)	(3)	(4)	(4)	(4)
Total interest payable	119	124	128	131	135
Interest cover pre capital maintenance (trigger 2.0, default 1.6)	3.7	3.7	3.6	3.7	3.6
Interest cover post capital maintenance (trigger 1.0)	2.1	2.0	1.9	1.9	1.9

[1] This is 'headroom' to balance gearing to the Glas Board's target of around 60% (see page 10). It represents amounts that may be returned to customers or used to fund additional investment for the benefit of customers.
[2] This figure includes £6.2 million transferred to the Customer Payments Account to fund social tariffs in the year.

Regulatory asset ratio (RAR) – 5 years to 31 March 2020

(See important notice at the front of the document)	As at 31 March 2016 £m	As at 31 March 2017 £m	Projection As at 31 March 2018 £m	As at 31 March 2019 £m	As at 31 March 2020 £m
Senior gross debt:					
Finance leases	505	456	446	436	421
Class A	1,043	1,018	1,031	1,041	1,054
Class B	792	815	837	861	884
Net interest accrual on senior debt	48	50	51	51	53
Authorised loans	708	869	964	1,065	1,168
Total senior gross debt	3,096	3,208	3,329	3,454	3,580
Less: cash balances and authorised investments	(108)	(100)	(100)	(100)	(100)
Total net debt	2,988	3,108	3,229	3,354	3,480
Regulatory capital value (RCV)	4,981	5,182	5,388	5,591	5,796
Reserves (RCV less total net debt)	1,993	2,074	2,159	2,237	2,316
Regulatory asset ratio:					
RAR (trigger 90%; default 95%)	60%	60%	60%	60%	60%

Income statement (unaudited)

	6 months ended 30 September 2015 £m	6 months ended 30 September 2014 £m
Revenue	367.8	374.6
Operating expenditure	(122.2)	(143.9)
EBITDA	245.6	230.7
Infrastructure renewals expenditure	(30.7)	(36.2)
Depreciation	(122.0)	(88.9)
Operating profit	92.9	105.6
Interest payable	(53.0)	(43.0)
Indexation of index-linked debt	1.0	(12.5)
Interest receivable	3.9	1.6
Fair value gains/(losses) on financial instruments	86.0	(49.5)
Profit before tax	130.8	2.2
Taxation	(26.2)	(0.4)
Profit after tax	104.6	1.8

Statement of comprehensive income (unaudited)

	6 months ended 30 September 2015	6 months ended 30 September 2014
	£m	£m
Profit for the period	104.6	1.8
Actuarial loss in the pension scheme	(19.0)	(26.2)
Movement on related deferred tax asset	3.7	5.4
Items that will not be reclassified to profit or loss:		
Revaluation of property, plant and equipment[2]	1,152.0	-
Related deferred tax	(230.4)	-
Total recognised gains/(losses) for the period	1,010.9	(19.0)

Statement of changes in reserves (unaudited)

	6 months ended 30 September 2015	6 months ended 30 September 2014
	£m	£m
(Deficit)/reserves at start of period	**(6.4)**	**100.0**
Revaluation net of tax	921.6	-
Profit for the period	104.6	1.8
Actuarial loss	(15.3)	(20.8)
Reserves at end of period	**1,004.5**	**81.0**

2 The group has decided that a ‘fair value’ approach to valuing its asset base better reflects the underlying value of the assets than historical cost accounting which understates the assets current value in use. The carrying values of the regulatory assets will be revalued periodically to their economic values at annual intervals starting on 1 April 2015. This change in accounting treatment has given rise to a net revaluation adjustment of £900m which is held in the non-distributable revaluation reserve.

Balance sheet (unaudited)

	At 30 September 2015 £m	£m	At 31 March 2015 £m	£m
Fixed assets		4,814.1		3,679.0
Current assets and liabilities:				
Debtors and prepayments	343.3		539.1	
Creditors and accruals	(448.2)		(638.7)	
		(104.9)		(99.6)
Total assets less current liabilities		4,709.2		3,579.4
Financing liabilities:				
Bonds	(2,003.3)		(2,005.5)	
Finance leases	(507.2)		(507.2)	
Bank loans (EIB, KfW)	(413.3)		(451.6)	
Other	(0.9)		(0.9)	
	(2,924.7)		(2,965.2)	
Net interest accrual	(78.6)		(66.6)	
	(3,003.3)		(3,031.8)	
Cash and cash equivalents:				
Receipts account	50.8		80.3	
Payments account	(11.0)		(92.4)	
Capex reserve account	77.5		135.0	
Debt service payments account	53.4		19.6	
Customer payments account	2.5		-	
Other bank accounts	6.1		5.5	
	179.3		148.0	
Net debt		**(2,824.0)**		**(2,883.8)**
Derivative financial instruments		(336.1)		(422.1)
Provisions for liabilities and charges		(71.9)		(60.1)
Net assets before deferred tax		1,477.2		**213.4**
Deferred tax		(472.7)		(219.8)
Net assets		**1,004.5**		**(6.4)**

Compliance certificate

To: Deutsche Trustee Company Limited **12 November 2015**

Dear Sirs

Common Terms Agreement dated 10 May 2001 between Dŵr Cymru Cyfyngedig, ("DCC") and the Deutsche Trustee Company Limited (the "DCC Security Trustee" and the "Issuer Security Trustee") ("the Common Terms Agreement")

Capitalised terms not defined in this certificate have the meaning given to them in the Common Terms Agreement.

We refer to the Common Terms Agreement and pursuant to Paragraph 1.5 of Schedule 3 of that Agreement hereby confirm that as of today's date, DCC is in compliance with the RAR, the Historical RAR, the Historical Senior RAR, the Projected RAR, the Projected Senior RAR and the Historical ICR, the Historical Senior ICR and the Projected Senior ICR (together the "**Ratios**").

The calculations of the ratios are set out on pages 9 and 10 of the Investor Report issued on today's date.

We also confirm that, in the period six months to 30 September 2015:

(a) No DCC Potential Event of Default, DCC Event of Default, Potential Trigger event or Trigger Event has occurred; and

(b) DCC's insurances are being maintained in accordance with:

- (i) Paragraph 4.2.1 of Schedule 3 of the Common Terms Agreement; and
- (ii) the provisions of each DCC Finance Lease

Yours faithfully
For and on behalf of
Dŵr Cymru Cyfyngedig

C A Jones Director	P J Bridgewater Director