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*Location: Llandegfedd Reservoir*

# Dŵr Cymru Welsh Water

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## Debt Investor Presentation

February 2020

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## Contents

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1) Introduction & Business Overview.....	Page 4
2) The Welsh Water Difference.....	Page 7
3) Financing & Liquidity.....	Page 15
4) Summary.....	Page 19
5) Appendices.....	Page 22





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# 1) Introduction & Business Overview

*Location: Pen Y Garreg Dam, Elan Valley*

# Introduction to Dŵr Cymru Welsh Water

## About us

- Dŵr Cymru Cyf. (Welsh Water) is the regulated water and sewerage company serving most of Wales and adjoining parts of England.

## Ownership

- Owned by Glas Cymru since 2001
- 'Not-for-shareholder-dividend' Group
- No shareholders – financial surpluses are reinvested in the business resulting in a sector-leading Gearing position and utilisation of reserves to benefit customers

## Key Statistics

- 5th largest company in Wales by turnover, as at 30 Sept 2019\*
- 828m litres of water supplied daily
- Over 3,000 people employed
- 27,644km of water mains; over 30,000km of sewers; 835 sewage treatment works; 78 impounding reservoirs, 462 service reservoirs.
- RCV £5.8bn as at 30<sup>th</sup> September 2019

### Customer base as at 30<sup>th</sup> September 2019

- Serving 1.4m (92%) households
- Around 124,000 (9%) business customer sites
- Approx. 100 business customers eligible for retail competition



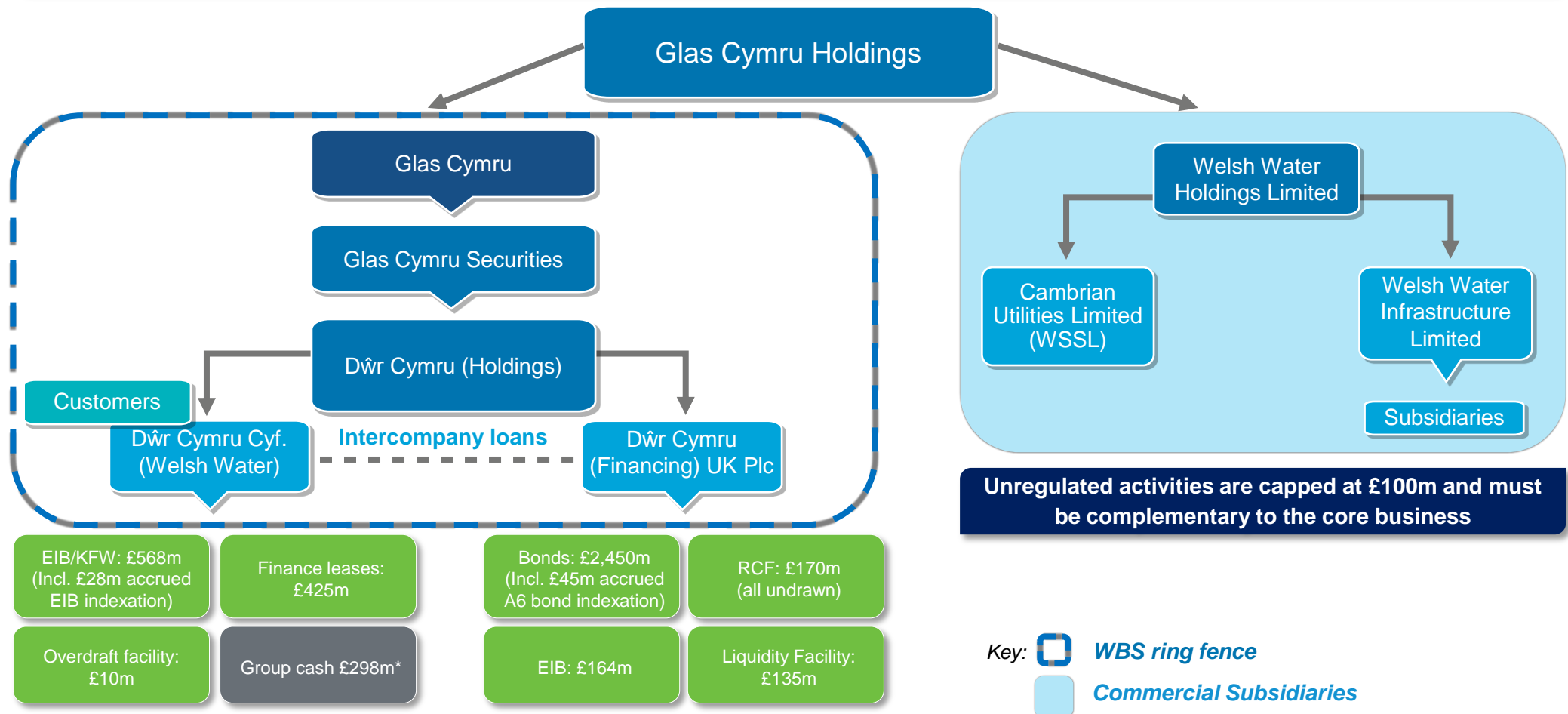
\*Source: Business Live: <https://www.business-live.co.uk/economic-development/wales-top-300-2019-biggest-17396726>



# Welsh Water's Financing Structure Overview - at 30 September 2019



- Dŵr Cymru Cyf. (Welsh Water) is a regulated water and wastewater utility
- Dŵr Cymru (Financing) UK Plc. is a special purpose financing vehicle which on-lends funds to Welsh Water
- All senior financial creditors have the benefit of a common package of structured finance covenants and security over shares of Welsh Water and other companies in the event of default
- Bonds are listed on the Luxembourg Stock Exchange
- Glas Cymru Holdings formed Commercial subsidiaries outside WBS ring-fence on 1<sup>st</sup> March 2016



Note: \*£10m held at Glas Cymru Holdings Cyfyngedig level and £55m held in debt service reserve

A scenic view of the Upper Lliw Reservoir in Velindre, Wales. The image features a prominent stone structure with a domed top, likely a water tower or part of the dam's infrastructure, situated on a stone wall overlooking the reservoir. The water is calm and reflects the clear blue sky. In the background, rolling hills and a forested slope are visible under a bright, clear sky.

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*Location: Upper Lliw Reservoir, Velindre*

## 2) The Welsh Water Difference



# Welsh Water's Key Investment Highlights

- 1 - Not-for-shareholder dividend business model
- 2 - Final Determination – acceptable outcome for the business
- 3 - Impressive financial discipline
- 4 - Strong customer service performance
- 5 - Long-term approach to sustainability & environment
- 6 - Experienced management team







# Not-for-Shareholder Dividend Business Model



- As a company wholly or mainly in Wales the company falls under the jurisdiction of the devolved Welsh Government.
- As a not-for-shareholder-dividend water group, profits have been used to deleverage the Group and benefit customers.
- Ownership model is aligned with the interests of both debt investors and customers.

## Benefits to our Investors

### Stronger Position vs. Peers as we move to AMP7 Challenges

Without shareholders, Dŵr Cymru is in a stronger position to invest to meet the regulatory challenges of AMP7 than its peers

### Lower Balance-Sheet Leverage than Peers & Ample Gearing Headroom

Welsh Water has significantly reduced leverage, where debt represented about 58.6% of the Group's RCV (at end of September 2019), compared to the peer average of c.80%. We have many refinancing options, balanced by more than ample gearing headroom, reflected in our strong credit ratings

### Strong Commitment to Investment in Infrastructure

We plan to retain leverage at around 60% and invest in our assets and service – this will improve future operational performance and ensure the resilience of our assets

## Benefits to our Customers

### Growth in Social Tariffs

At 58.6% gearing, some of the additional funds generated can be returned to customers to help those who genuinely struggle to pay their water and sewerage bills. Just over 130,000 of our customers are now receiving assistance through Social Tariffs (and continuing to grow)

### Constant Improvement in Customer Experience

The money received from customers is reinvested to maintain and improve our assets and services, in line with our commitment to customers in our Welsh Water 2050 strategy

### Protecting and Sustaining the Environment

Money received through bills helps to improve sewerage services and protect the environment, not just now, but for years to come



## Final Determination – Outcome for the Business

- As anticipated Ofwat has succeeded in setting a tough Determination for the sector
- Despite this, the Board, has decided not to appeal to the Competition and Markets Authority (“CMA”)
- The Final Determination differs from the August 2019 business plan (“BP”) as follows:

Key Features	August 2019 BP	Final Determination
Revenues	£3.721bn	£3.730bn
BOTEX*	£2.509bn	£2.493bn
Enhancement expenditure	£0.755bn	£0.584bn
RCV	Opening: £5.685bn Closing: £6.083bn	Opening: £5.667bn Closing: £5.819bn

*\*Base Operating Total Expenditure including household retail*

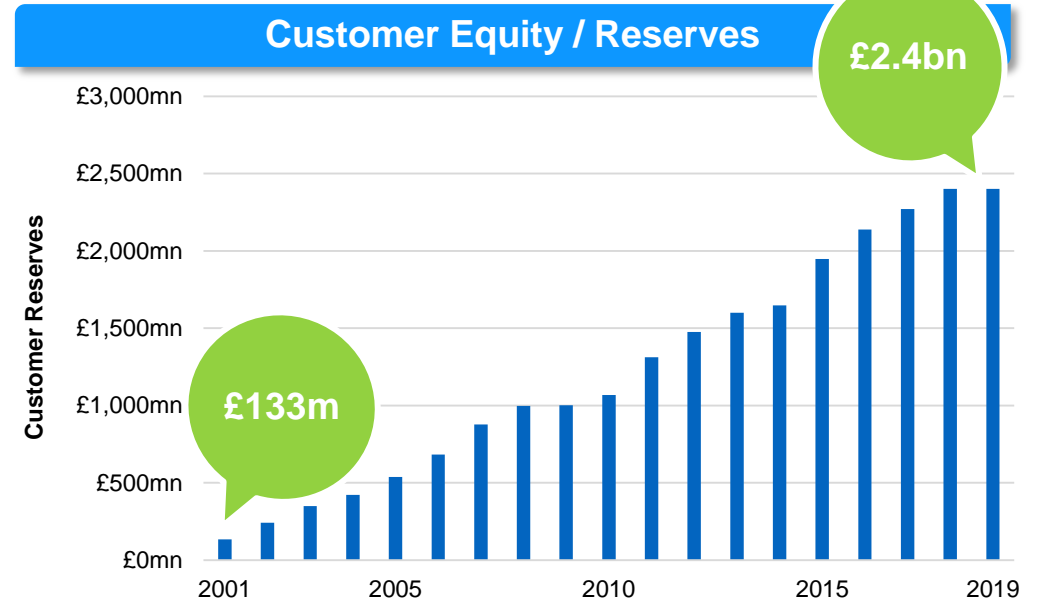
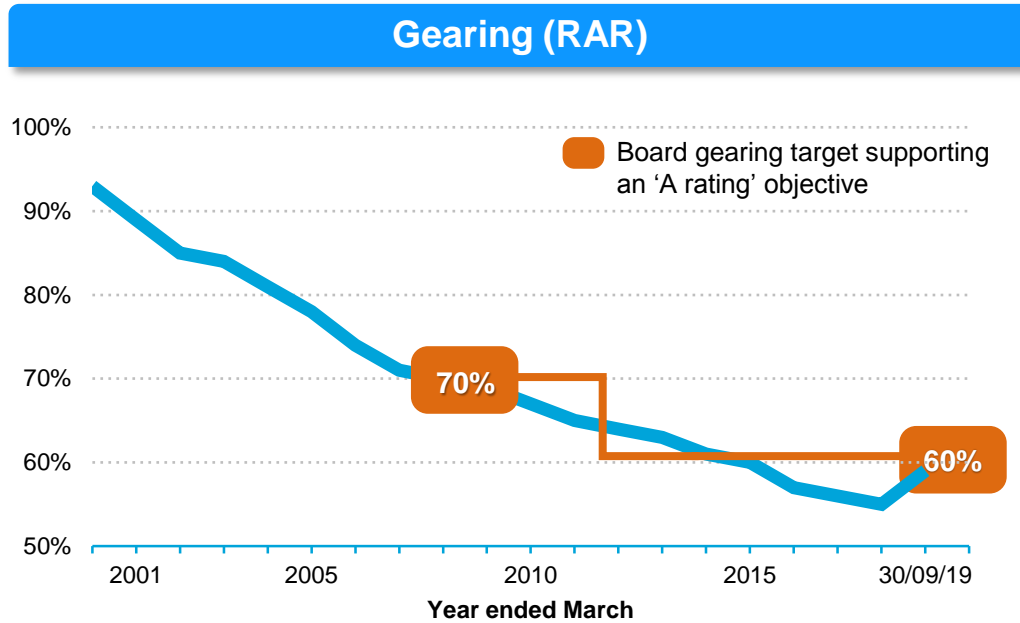
**A tough but financeable Final Determination**



# 3 Impressive Financial Discipline

- Conservative group leverage target (around 60%)

- Significant customer equity/reserves (£2.4bn as at 30/09/2019)



### Net Debt & Regulatory Gearing

(£m)	30 Sep 2019	31 Mar 2019	31 Mar 2018
Regulatory Capital Value	5,821	5,671	5,468
Net debt	(3,410)*	(3,327)	(3,130)
Financial reserves	2,411	2,344	2,338
<b>Gearing</b>	<b>59%</b>	<b>59%</b>	<b>57%</b>

- ### Interest Cover Ratio & Liquidity Position
- Interest Cover Ratio (ICR) of 3.4x as at 30 September 2019 (versus trigger level of < 2.0)
  - Strong liquidity position of £413m\* as at 30 September 2019. Prudent investment policy for surplus cash continues with short deposit maturities and focus on bank credit ratings
- \*Excluding debt service reserves of £55m as at 30 September 2019

\*Net debt at 30/09/19 includes £10m of cash held at Group level

## 4 Strong Customer Service Performance

- New measures of customer service introduced by Ofwat for PR19. The primary customer satisfaction measure from 1 April 2020 is C-MeX
- C-MeX is a single score combining two Ofwat surveys; customer service and customer experience
- Water companies to be ranked annually based on their score
- Performance payments of up to 6% of residential retail revenues annually and, for the top three performers, a higher performance payment of a further 6% is also potentially available (i.e. up to 12%). The 6% reward level for Dwr Cymru would be circa £3m per annum
- Our not-for-shareholder dividend model and vision demonstrates that we are already earning the trust of our customers

Shadow year 2019/20 Overall C-MeX Score				
	Q1	Q2	Q3	YTD
Company Score	82.61	83.46	79.82	81.96
Industry Average	76.41	76.69	76.33	76.48
Ranking	1 <sup>st</sup>	1 <sup>st</sup>	3 <sup>rd</sup>	

The shadow year-to-date data for 2019/20 illustrates that we are out-performing the industry average





# 5 Long-term Approach to Sustainability & Environment

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- £90 million invested in award-winning sustainable urban drainage systems (“RainScape”) to capture, divert or slow down the rate at which rainwater enters our sewer network. This reduces the risk of flooding or pollution from overloaded sewers creating greener and more sustainable places to live.
- Significant increase in the amount of site-generated energy in recent years. 6GWh during 2007-08 to almost 100GWh during 2018-19 (and growing)
- Capacity for the self-generation of power is continuously increasing (est. 26% by 31 March 2020) through wind, hydro, solar biomass and advance anaerobic digestion.
- Continuous improvement in driving down carbon emissions – at 31 March 2019 the Company reported a 79% reduction since 2010-11

**Demonstrates strong sustainability and environmental credentials**

# 6 Experienced Management Team

## ■ Welsh Water boasts a strong and well-experienced management team



### **Alastair Lyons CBE**

*Joined the Glas board as a Non-Executive Director in May 2016 before becoming Chairman in July 2016*

- Following an extensive executive career in financial services, Alastair has over 20 years' experience as a Non-Executive Chairman of both listed and private companies including at Admiral, Towergate Insurance, Serco, and as Deputy Chairman of Bovis Homes. Alastair is currently Non-Executive Chairman of the Harworth Group plc, Vitality Health, Admiral Europe Compania de Seguros, and the Eaton House Schools Group.



### **Chris Jones**

*Chief Executive – in post since September 2013*

- Co-creator of Glas Cymru, Chris became Chief Executive in September 2013 having previously been Finance Director of Welsh Water since May 2001 and Glas Cymru since April 2000.
- He has also previously served as Director of Regulation of Welsh Water and South Wales Electricity plc. Before joining Welsh Water in 1995, he was a Director at National Economic Research Associates and, prior to that, worked for HM Treasury.



### **Peter Perry**

*Chief Executive Designate (moving into post from 1<sup>st</sup> April 2020)*

*Managing Director – since October 2017*

- Appointed Operations Director in July 2006, Peter has a civil engineering background and was formerly the Chief Operating Officer for United Utilities Operational Services (UUOS), having previously been the Operations Director for UUOS with responsibility for the operational contract with Welsh Water and UUOS's water interests in Scotland and Ireland.
- Before joining the outsourced company UUOS he had previously worked for Welsh Water for over 20 years.



### **Mike Davis**

*Chief Financial Officer – in post since January 2020*

- Mike previously held the positions of Director of Strategy and Regulation and Financial Controller at Welsh Water, with a focus on regulatory price reviews and competition.
- He has previous experience in the Media, ICT and Mining industries including as Finance Director for two private equity start-up businesses. Mike has been a Non-Executive Director at RCT Homes, a registered social landlord, and a Director of UK Water Industry Research.



### **Menna Richards OBE**

*Senior Independent Director – in post since August 2017*

- Menna's executive career was in broadcasting as Director BBC Cymru Wales (2000—2011) and previously Managing Director, HTV Wales. She was awarded the OBE for services to broadcasting in 2010.
- Menna is currently Chair of The ALOUD charity and Vice President of The Royal Welsh College of Music and Drama and has held a variety of Chair and Non-Executive Director roles with a number of other Welsh institutions.



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## 3) Financing & Liquidity

*Location: Alwen Water Treatment Works*

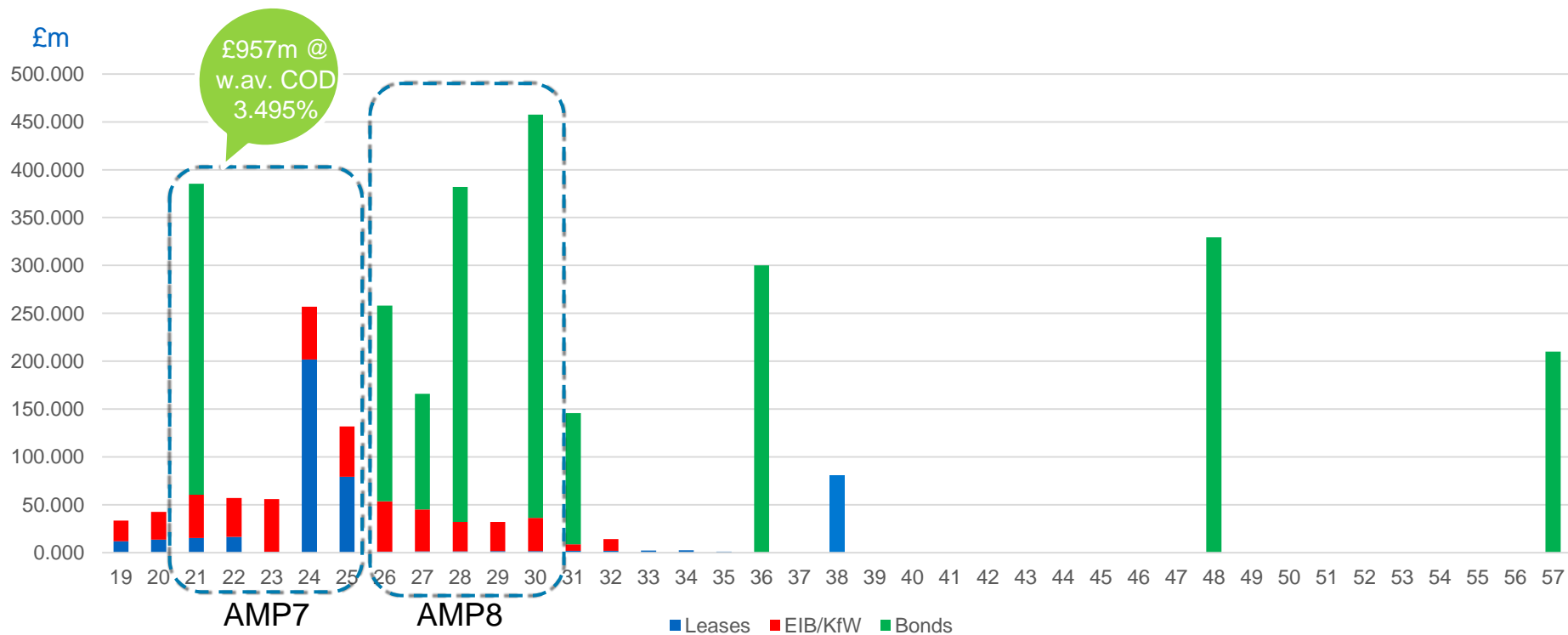
## Group Cashflow and Net Debt

	6 Months		Year
(£m)	30 Sep 2019	31 Mar 2019	31 Mar 2018
Revenue	398	782	757
Operational expenditure	(159)	(336)	(319)
EBITDA (before IRE)	239	446	438
Net working capital movements	(30)	(12)	(36)
Capital expenditure	(218)	(452)	(415)
Net interest payable (incl. indexation)	(74)	(180)	(188)
(Increase)/decrease in net debt	(83)	(198)	(201)

**Stable business with a substantial regulated capital programme**

# AMP7 Financing

- The first AMP since the creation of Glas where total revenues fund the expenditure needs of the business (including interest)
- Financing requirements aligned to the debt maturity profile

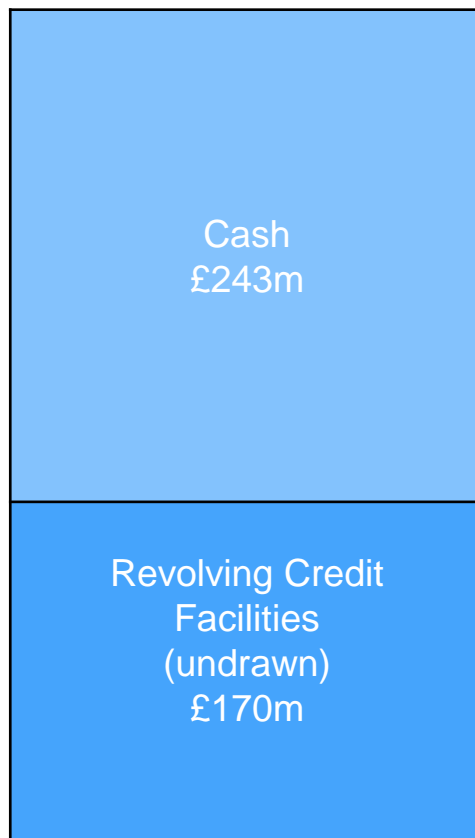


Funding requirements restricted to refinancing existing maturing debt only



# Liquidity – as at 30 September 2019

Liquidity as at 30 September 2019  
£413m



- Revolving credit facilities available until 2020.
- Revolving credit facilities to be renewed from April onwards. Expected to be sized at circa £150 million with 4-5 banks participating.
- Prudent investment policy for surplus cash continues with deposit maturities limited to maximum of one month and focus on strong bank credit ratings.
  
- **Strong liquidity position of £413m\* at 30 September 2019 – at least 18 months of financing needs before refinancing activity.**

*\*Excluding debt service reserves of £55 million*





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## 4) Summary

*Location: Elan Valley*



# Summary

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1

- Not-for-shareholder dividend business model

2

- Final Determination – acceptable outcome for the business

3

- Impressive financial discipline

4

- Strong customer service performance

5

- Long-term approach to sustainability & environment

6

- Experienced management team



# Indicative Term Sheet

- Dŵr Cymru (Financing) UK plc's financing documents employ a different naming system than other WBS issuers in the water sector
  - Class A refers to senior bonds which benefit from a guarantee from a monoline insurance company
  - Class B refers to senior bonds without a guarantee from a monoline guarantee
  - Class C bonds are subordinate to Class A and Class B

	Senior Bonds (Class B)	Junior Bonds (Class C)
<b>Issuer</b>	Dŵr Cymru (Financing) UK plc	
<b>Format</b>	RegS, Senior Secured, Bearer Bonds	RegS, Secured, Bearer Bonds Subordinated Obligations of the Issuer and are subordinated to the Class A Bonds and Class B Bonds
<b>Expected Ratings (Moody's / S&amp;P / Fitch)</b>	A3 (stable) / A- (stable) / A (stable)	Baa2 (stable) / BBB (stable) / BBB+ (stable)
<b>Currency</b>	GBP	
<b>Size</b>	Benchmark	£200m (expected)
<b>Maturity</b>	13 years (expected)	6 years
<b>Optional Redemption</b>	Spens Clause	
<b>Use of Proceeds</b>	General corporate purposes	
<b>Minimum Denominations</b>	£100,000 + £1,000	
<b>Listing</b>	Luxembourg Stock Exchange	
<b>Governing Law</b>	English	
<b>Documentation</b>	£4bn Base Prospectus dated 11 November 2019 and supplemented 7 February 2020	
<b>Joint Active Bookrunners</b>	HSBC, Lloyds Bank Corporate Markets	



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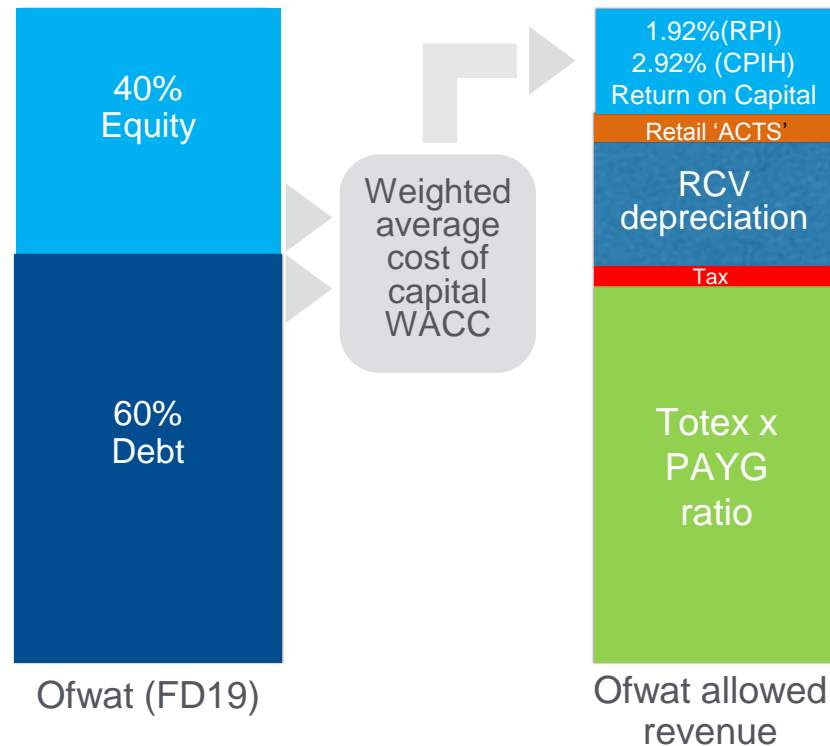
## **5) Appendices**

*Location: Llyn Celyn reservoir*

# AMP7 cost of capital and Ofwat building blocks

Final Determination	
Total equity market return	8.63%
Risk-free rate	0.58%
Equity risk premium	8.05%
Gearing (Net Debt/RCV)	60%
Asset beta	0.36
Equity beta	0.71
<b>Cost of equity</b>	<b>6.27%</b>
Ratio of new to embedded debt	20:80
Cost of new debt	2.54%
Cost of embedded debt	4.47%
Issuance and liquidity costs	0.10%
<b>Overall cost of debt</b>	<b>4.18%</b>
<b>Appointee WACC</b>	<b>5.02%</b>
Deduction for retail amrgin	0.04%
<b>Wholesale WACC (nominal)</b>	<b>4.98%</b>

Source: Ofwat





# Debt Characteristics

Gross debt as at 31 Dec 2019 (£m)	Fixed	Index-linked	Floating	Total	
Finance leases	-	380	43	424	12%
Bonds	975	1,498	-	2,473	68%
EIB/KfW	-	259	466	725	20%
Local authority debt	-	-	1	1	-
	975	2,137	510	3,623	100%
Swaps - floating to fixed	192	-	(192)	-	
Swaps - floating to index-linked	-	81	(81)	-	
Free cash balances - floating to index-linked	195	-	(195)	-	
Gross debt	1,362	2,218	42	3,623	
Percentage	38%	61%	1%	100%	

## Reconciliation to Investor Report:

Gross debt as above	3,623
Accrued interest	110
Cash	(195)
Net debt* as at 31 Dec 2019	3,538

### Notes

\*Net debt using free cash balances at DCWW level only (i.e. excludes £11m held at Glas Cymru Holdings level and excludes debt service reserves of £83m)

# Fair Market Value Movements on Swaps

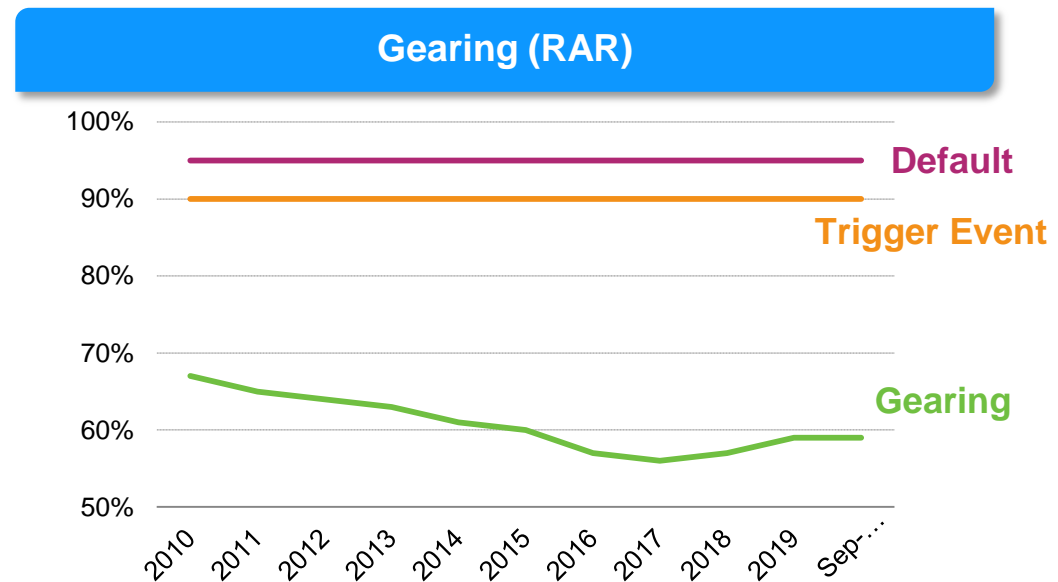
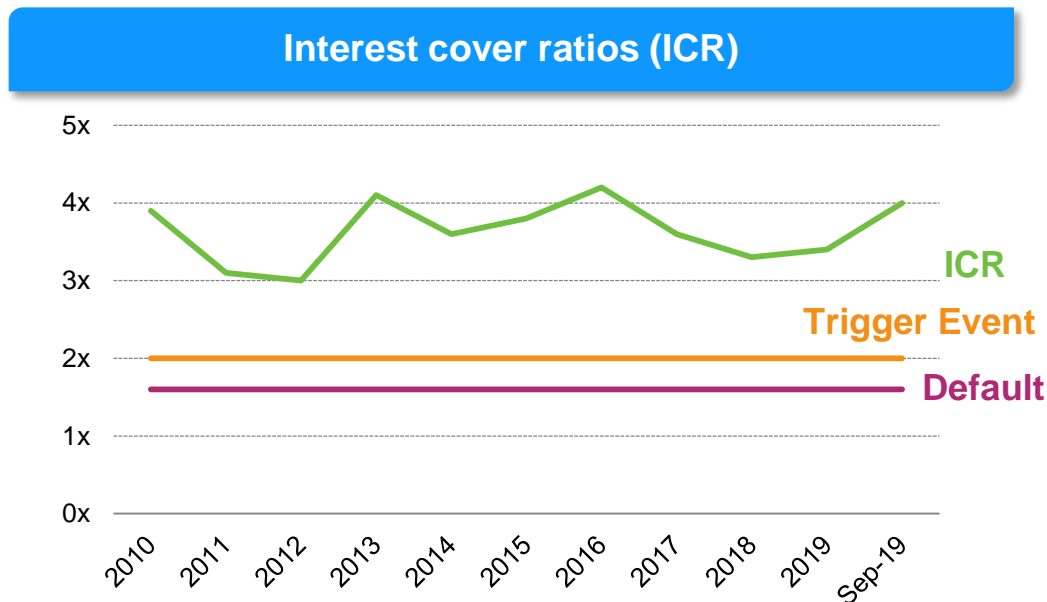
Derivatives as at (£m)	30 <sup>th</sup> Sep 2019	31 <sup>st</sup> Mar 2019	Movement
Floating to fixed rate interest rate swaps	(103)	(91)	(12)
Index-linked swaps	(422)	(340)	(82)
Energy Swaps	8	4	4
<b>Total MTM</b>	<b>(517)</b>	<b>(427)</b>	<b>(90)</b>

**Notes:**

1. Swap contracts are with NatWest Markets, HSBC and Lloyds
2. None of the swap contracts have break clauses or accretion paydowns
3. In addition to the MTM values above, there is an additional liability for cumulative indexation of £46m (Mar 2019: £45m) relating to the A6 bond swap

# Stringent Investor Protections

- Comprehensive protections provided to investors through the Whole Business Securitisation (“WBS”) structure
- Tightened by amendment to the Gearing Trigger Event covenant to 85% (from 90%)
- ICR of 4.0x and Gearing of 59% as at 30 September 2019



**Significant headroom over trigger event default levels**



# Covenant Package

Normal business Operating within covenant package	Trigger event step-in period One or more financial or operational 'trigger' covenants breached	Default standstill period One or more events of default occur and continue	Special administration
No creditor involvement	<p>No customer dividends</p> <p>Option to commission independent review</p>	<p>Majority of secured claims frozen</p> <p>18 month opportunity to remedy situation or find a buyer for Welsh Water</p> <p>Liquidity facilities keep senior debt whole</p> <p>Security over shares of Welsh Water and holding Group can be enforced</p>	<p>Regulator applies to court to appoint a Special Administrative Receiver (SAR) to run business</p> <p>SAR acts in interest of creditors and customers</p>
<b>Financial covenants:</b>			
	<ul style="list-style-type: none"> <li>• Senior ICR: &lt;2.0</li> <li>• Senior PMIC: &lt;1.0</li> <li>• Gearing Ratio: &gt;85%</li> </ul>	<ul style="list-style-type: none"> <li>• Senior ICR: &lt;1.6</li> <li>• Senior PMIC: N/A</li> <li>• Gearing Ratio: &gt;95%</li> </ul>	