

ISSUER COMMENT

18 April 2017

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RATINGS

Dwr Cymru Cyfyngedig

Outlook	Stable
Corporate Family Rating	A2

Dwr Cymru (Financing) Limited

Outlook	Stable
Senior Secured	A2

Contacts

Paul Marty 44-20-7772-1036
Senior Vice President
 paul.marty@moodys.com

Velina Karadzova 44-20-7772-5478
Analyst
 velina.karadzova@moodys.com

Neil Griffiths-Lambeth 44-20-7772-5543
Associate Managing Director
 neil.griffiths-lambeth@moodys.com

Dwr Cymru Cyfyngedig

Proposal to amend financing arrangements is credit neutral

On 13 April 2017, Dwr Cymru Cyfyngedig (Welsh Water, A2 stable) published a Security Trust and Intercreditor Deed (STID) proposal, which seeks to amend certain of the terms of the documentation (including the Common Terms Agreement or CTA) which underpins its financial structure. The amendments would allow for (1) the removal of the "Material Deviation in Projections" trigger event which limits Welsh Water's ability to allocate additional funds to capital expenditure projects between each periodic review, and (2) amending from 90% to 85% the historical and projected leverage ratio (expressed as senior net indebtedness to Regulatory Capital Value or RCV) that applies to certain trigger events and to the "Restricted Payments" covenant.

The STID proposal reflects Welsh Water's strategy, following engagement with its customers, to use the existing financial headroom relative to its targeted leverage of 60% (vs. current leverage of 56%), by investing further into its regulated water and wastewater business instead of paying customer rebates in the short term or continuing to reduce leverage. Prior to the proposed amendment, the CTA has been restricting Welsh Water's ability to exceed over a regulatory period the capital expenditure assumed by the regulator by 10% or more.

Moody's believes that the credit quality of Welsh Water would be broadly unchanged following the proposed amendments to the group's financing arrangements. This is because the protection provided by the existing covenants, particularly the limitations on additional indebtedness and permitted distributions (including the proposed reduced leverage ratio), in maintaining the current rating is already limited as the group has significant headroom to increase leverage before additional creditor oversight would be triggered. As a result, and unlike comparable transactions such as Anglian Water (CFR of Baa1 stable) or Thames Water (CFR of Baa1 stable), Welsh Water's current A2 rating does not include any uplift from structural considerations.

Peer Group:

- » [Anglian Water Ltd](#)
- » [Thames Water Utilities Ltd](#)
- » [United Utilities Ltd](#)
- » [Severn Trent Plc](#)
- » [Wessex Water Services Limited](#)

Moody's Related Research**2017 Industry Outlook**

- » [2017 Outlook – UK Water Sector: Stable outlook but macroeconomic and regulatory pressures rising, 11 October 2016](#) (1044706)

Sector-in-Depth

- » [UK Water Sector: Retailers likely to have weak credit quality, 11 October 2016](#) (1044093)
- » [UK regulated utilities: Low interest rate scenario is credit negative for water and energy networks, 11 October 2016](#) (1043970)
- » [UK Water Sector: 'Water 2020' Proposals Are Credit Negative, 13 January 2016](#) (1012879)

Sector Comment

- » [UK Water Sector: Ofwat's licence change proposals in line with 'Water2020' agenda, 11 November 2016](#) (1049626)
- » [UK Water Sector: Ofwat confirms approach for PR19, 31 May 2016](#) (1029257)

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