



YorkshireWater

# Yorkshire Water Financing Group

## Investors Report

*For the period ended 31 March 2015*

## IMPORTANT NOTICE

- This report is not an offer or solicitation of an offer to buy or sell securities. It is solely provided for information only.
- This report is not directed to, or intended for distribution to or use by, any person or entity that is a citizen or resident or located in any locality, state, country or other jurisdiction where such distribution, publication, availability or use would be contrary to law or regulation or which would require any registration or licensing within such jurisdiction. Neither this report nor any copy hereof may be sent, or taken or distributed in the United States or to any U.S. person (as such term is defined in the U.S. Securities Act of 1933) (the "Securities Act") except (i) to persons that are qualified institutional buyers as defined in Rule 144A under the Securities Act and (ii) outside the United States to non-US persons as defined under Regulation S of the Securities Act.
- This report contains statements about future events and expectations that are forward-looking statements. These statements typically contain words such as "expects" and "anticipates" and words of similar import. Various known and unknown risks, uncertainties and other factors may cause the actual future results, financial situation, development, performance or achievements of Yorkshire Water Services Limited (the "Company") to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. None of the future projections, expectations, estimates or prospects in this report should be taken as forecasts or promises nor should they be taken as implying any indication, assurance or guarantee that the assumptions on which such future projections, expectations, estimates or prospects have been prepared are correct or exhaustive or, in the case of the assumptions, fully stated in the report. 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 or the bonds issued under the £8,000,000,000 multicurrency programme for the issuance of guaranteed bonds financing the Company (the "Programme"). We assume no obligations to update the forward-looking statements or any other information contained herein to conform them to future events or developments.
- Investment in the bonds issued under the Programme also involves certain risks. A summary of the material risks relating to a particular offering of bonds issued under the Programme is set out in the relevant prospectus. There may be additional material risks that are currently not considered to be material or of which the Company and its advisors or representatives are unaware.
- This report and its contents are confidential and are being provided to you solely for your information and may not be retransmitted, further distributed to any other person or published, in whole or in part, by any medium or in any form for any purpose.
- Any opinions presented herein are based on general information gathered at the time of writing and are subject to change without notice. The Company relies on information obtained from sources believed to be reliable but does not guarantee its accuracy or completeness. It should be noted the auditors of the Company have not reviewed the information herein and the information has not been independently verified.
- This report is being distributed in fulfilment of a document, the Common Terms Agreement dated 24 July 2009 (as amended and restated on 3 August 2010, 13 December 2011, 26 September 2012 and 11 March 2014, and as further amended and restated on 15 July 2015) (the "CTA"), which governs the obligations of the Company to the holders of bonds issued under the Programme and other Secured Creditors. Capitalised terms used but not defined in this report shall have the meaning ascribed to them in the Master Definitions Agreement (the "MDA") dated 24 July 2009 (as amended and restated on 3 August 2010, 13 December 2011, 26 September 2012 and 11 March 2014, and as further amended and restated on 15 July 2015). This report is directed to, and intended for, existing Secured Creditors of the YW Financing Group. No other persons should act or rely on it. 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 may 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 or the bonds issued under the Programme.
- 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).
- A copy of this report may be obtained at [www.keldagroup.com](http://www.keldagroup.com).

## Contents

1.	General	4
2.	Overview	4
3.	Business update	4
4.	2014/15 financial performance	9
5.	Company vision - "Taking responsibility for the water environment for good"	9
6.	Regulatory update	10
7.	Director changes	11
8.	Permitted Subsidiaries acquired pursuant to a Permitted Acquisition	12
9.	Regulated capital investment	12
10.	Outsourcing	12
11.	Financing	13
12.	Ratings	13
13.	Surplus	13
14.	Bank and liquidity facilities held by the YW Financing Group	13
15.	Non-Participating YWSF Bond Reserve Account	14
16.	Authorised Investments	14
17.	The Conformed ICR	14
18.	Ratios	15

## 1. General

The information provided in this report is sourced primarily from the audited Yorkshire Water Services Ltd (“YW”) unconsolidated Annual Report and Financial Statements for the year ended 31 March 2015.

## 2. Overview

Over the past 12 months YW’s customers have benefited from some of the highest ever standards of operational and customer service as the company delivered unprecedented levels of performance in several key areas of the business.

Customer satisfaction levels continued to rise, pollution incidents continued to fall, YW generated more renewable energy than ever before and achieved stable serviceability in all areas of its water and waste water networks for the third consecutive year. In addition, the Environment Agency (“EA”) classed YW as the ‘industry leading’ water company in 2014.

On 12 December, Ofwat made their final determination of future prices and plans. YW’s regulatory business plan for the 2015-2020 period, which is called ‘Blueprint for Yorkshire’, will see YW invest a further £3.8 billion in the Yorkshire region. This will require YW to continue to focus on delivering more for less, with YW’s customer bills due to fall by an average of 3% in real terms by 2020. This will ensure that YW’s customer bills remain one of the lowest in the UK.

YW’s regulatory business plan for the 2015-20 period is focused more than ever before on delivering its customers’ priorities which is central to YW’s strategy and SBOs. YW engaged with over 30,000 customers and a wide range of stakeholders during the price review process to ensure that the company fully understood customer priorities, and to ensure that YW’s “Blueprint for Yorkshire” met their expectations.

## 3. Business update

Throughout 2014/15, YW’s performance against the key operational and environmental performance indicators has shown excellent results as the company delivered unprecedented levels of performance in several key areas of the business. These key areas are detailed below:

### Delivering leading customer service

- In January 2015 YW was recognised as the leader in customer service in the utilities sector by the Institute of Customer Service.
- The Service Incentive Mechanism (“SIM”), Ofwat’s water industry measure of customer service, was not measured for price control purposes in 2014/15 and therefore no industry comparisons can be made. However, YW continues to measure customer service based on the SIM methodology and in 2014/15 YW’s performance improved, scoring 85 points out of 100 (compared to 82 points in 2013/14). YW has estimated that this would have resulted in a relative ranking of 6th in the sector (second out of the ten water and sewerage companies). YW continues to prioritise improvements to its customer service and to increase both its SIM score and relative sector performance and strives to be first in SIM by 2020.
- YW has continued with its programme of customer service improvements, for example the implementation of a new website based on extensive analysis of customer expectation.

### Ensuring affordability and managing customer debt

- The average YW water and waste water bill was £373 in 2014/15. YW reduced this by £6 by not taking the 1.6% above Retail Price Index (“RPI”) increase that was previously agreed with Ofwat. YW has also reduced the average bill to £360 in 2015/16 and will cap increases at RPI though to 2019/2020.
- Non-recovery of customer debt threatens profitability in the short-term and may increase cost to paying customers in the medium to long-term. To help minimise bad debt YW operates a range of schemes designed to help customers who genuinely cannot afford to pay their bills, while having strong processes in place for overall debt collection. In 2014/15 YW piloted a new support scheme to add to its portfolio of

assistance packages called “WaterSupport”. WaterSupport is aimed at customers whose household income is assessed as being “low” and who have a bill over a set threshold (£410 in 2015/16). Under the scheme the customer’s bill can then be capped at the cost of the average YW bill (£360 in 2015/16). YW’s pilot proved successful and is being fully implemented in 2015/16.

- Another of YW’s many help mechanisms is the Yorkshire Water Community Trust which was established in 1995 to help customers who are unable to pay their bill. Each year the Board of Kelda Group allocates a set amount to the Trust and a group of trustees make awards to deserving customers who have fallen into arrears with their water bill. In 2014/15 the Trust helped over 2,000 customers with over £800,000 of financial support.
- YW is committed to helping more customers who are struggling with their bills. In 2015/16 YW aims to use its portfolio of help mechanisms to support 22,000 of its customers struggling to pay their bill. In parallel, YW will also work to ensure the cost to customers of our bad debt is kept at no more than 3.16% of the average bill.

### **Maintaining excellent drinking water quality**

- Drinking water quality throughout the Yorkshire region remains excellent with 99.94% of hundreds of thousands of samples meeting stringent regulatory standards.
- YW continues to see the benefits of the service reservoir inspection and improvement programme that was undertaken during 2013/14, together with the new programme of inspections and remedial actions that have been implemented more recently. The main area of non-compliance in 2014 related to metaldehyde, a pesticide used in slug control on arable crops. There is currently no effective process to remove metaldehyde from water supplies however YW is researching possible future treatment options and working with the agricultural sector to minimise future risk.

### **Securing water supplies**

- YW operates, maintains and enhances over 50 water treatment works and a distribution network of over 31,000km of water mains in order to treat and supply around 1.3 billion litres of drinking water each day.
- Following extensive investments, Yorkshire has had no service restrictions such as hosepipe bans since the 1995/1996 drought. YW maximises the benefit of the good range and balance of water supply options in its region by developing infrastructure that allows the company to move water around the region to where it is needed via the Yorkshire grid, which covers 99% of YW’s customers. YW manages the Yorkshire grid to offer one of the most resilient water supply systems in the country.
- The risk of water shortages or supply interruptions is a constant priority for YW because of the consequences to its customers, and to its operations and finances. YW’s 2014/15 supply interruption and security of supply performance remained strong, with improved performance on the duration of supply interruptions (reduced to an average of 9 minutes 36 seconds per property, or 0.16 hours per property) and maximum possible performance maintained on the industry measure for security of supply.
- In 2014/15 YW published the final version of its new Water Resources Management Plan which describes how YW will maintain the balance between water supply and demand over the next 25 years. YW’s detailed assessment of this plan confirms that climate change presents a growing threat to the company’s ability to maintain the balance between supply and demand. However, YW is well placed to manage this threat as water resources management is one of YW’s most mature areas of current resilience and future planning.

### **Serviceability - Ensuring reliable services today and for the future**

- YW invests over a million pounds a day to maintain and enhance the assets and infrastructure it manages to ensure reliable services to its customers.
- In 2014/15 YW achieved stable serviceability in all four asset categories for the third year running.
- YW manages risks to all hazards through its corporate and operational risk management processes which have worked well through numerous emergency events in recent years. In addition, YW has extensive emergency plans to enable a fast and effective response and recovery should any emergency occur.

### Sustainably reducing leakage

- Leakage is by far the dominant source of water waste. YW measures, reports and invests to reduce leakage (of which about two thirds results from our distribution network and a third is from leaks in customers' supply pipes).
- YW has almost halved leakage since 1995 and recorded its lowest ever levels in 2012/13, at 265 mega litres per day ("Ml/d"). This was below the Sustainable Economic Level of Leakage ("SELL") of 297Ml/d (the SELL is an industry term and methodology that defines the optimum level of leakage based on a suite of economic, environmental and social considerations). YW's 2012/13 leakage performance was not affordable on a long term basis so the company manages its leakage control activities closer to the SELL, reporting 288Ml/d in 2014/15.
- YW also helps and encourages its domestic and business customers to save water and during 2014/15 YW helped its customers save over 7.5Ml/d by providing free water saving devices and a range of advice and support services.

### Managing flood risk

- YW continues to invest in the region's drainage network and reduce the number of properties at risk from sewer flooding. In 2014/15 YW removed 90 properties from being at risk of sewer flooding and reduced the overall number of properties at risk of sewer flooding on its regulated risk register to approximately 175.
- In 2014/15, 121 incidents of sewer flooding inside properties were reported within the Yorkshire region, compared to 76 incidents in 2013/14 and 155 in 2012/13. However, the number of incidents in 2014/15 exceeded the company's target for no more than 118 incidents primarily due to the Yorkshire region experiencing exceptionally wet weather during August 2014.
- Climate change and urban growth increase the pressure on YW's sewer network and also increase the risk of flooding. YW has published documents setting out its risks and plans for climate change and storm water management and will continue to invest to mitigate the risk and manage the consequences of sewer flooding. In addition, YW continues to work in ever closer partnership with a number of third party organisations to manage flood risk.

### Reducing pollution and enhancing river water quality

- YW collects, treats and returns 1 billion litres of waste water safely back to the environment every day and has delivered a step change in river water quality over the last 20 years by investing heavily in the region's waste water treatment works and network.
- YW further improved its performance on waste water treatment in 2014, with discharge permit compliance reaching 99.3% (two failing works), improved from 98.0% in 2013 (six failing works). YW's performance in 2014 was its best ever and YW was delighted that its high standards were recognised by the EA in their annual environmental performance review of the water companies where YW stood alone as the only "industry leading" company in 2014.
- The total number of pollution incidents from YW's sewer network has continued to reduce over recent years. Performance fluctuates each year because sewer performance is influenced by the weather, however, in 2014, YW achieved its best ever performance with 58.82 Category 1, 2 or 3 pollution incidents per 10,000km of sewer, down from 78.10 in 2013 and 82.68 in 2012.
- The number of the most serious pollution incidents also shows an overall trend of improvement and best ever performance with 1.31 Category 1 and 2 incidents per 10,000km of sewer. This has fallen from 3.27 Category 1 and 2 incidents per 10,000km of sewer in 2013 and 1.63 incidents in 2012.

### Investing in the region's bathing waters

- YW has completed the £110m investment programme to enhance Yorkshire's coastal water quality, playing a lead part in the multi-agency Yorkshire Bathing Water Partnership. This group is working to align the region's activities on bathing water quality and beach management.
- Together, our joint efforts have resulted in a step change in the region's bathing water quality over recent years. The region's beaches will continue to provide a high quality experience for users and YW's assets are ready to ensure compliance with the tighter requirements of the revised Bathing Water Directive which came into effect for the 2015 bathing season.

- In 2014, 19 of the 20 Yorkshire bathing beaches met the minimum “Mandatory” standard under the previous directive standards with 14 of the region’s bathing beaches achieving the higher “Guideline” standard.
- Under the revised directive's tighter standards, 18 of the 20 beaches exceeded the new minimum ‘Sufficient’ standard, achieving either “Good” or “Excellent”. Only one bathing beach (Staithe) failed to meet the required minimum standard which was a result of agricultural runoff.

### **Reducing operational greenhouse gas emissions**

- YW has reduced its operational emissions by 15% since 2008/09 primarily by reducing the amount of electricity it uses together with increasing the amount of renewable electricity it generates.
- YW has successfully reduced its electricity consumption by 8% since 2010/11. This follows years of growth in electricity demand since privatisation, driven primarily by investment to meet new legislation for environmental water quality. YW has achieved this through a variety of approaches, including cost-effective capital investment, operational efficiencies and targeted training.
- YW is also investing to grow its renewable energy generation capabilities, primarily by using sewage sludge. In 2014/15 YW increased its renewable generation to supply over 12% of its total consumption through a range of activities. These activities included:
  - concluding a £34m project to make Esholt waste water treatment works in Bradford almost entirely self-sufficient for its electricity needs by using a range of renewable energy technologies;
  - installing a 123 high metre wind turbine at Knostrop waste water treatment works in Leeds. The turbine is now generating enough energy to power approximately 10% of the site’s needs (equivalent to 1,100 homes). This supports the city council’s ambition for the Lower Aire Valley to become a hub for green energy and industry; and
  - winning an Environment and Energy Award for innovative Remote Energy Visibility Optimisation software that YW has installed on 60 of its key sites within the Yorkshire region. This software has helped YW reduce energy consumption during times of peak electricity demand.
- YW’s success in achieving the Carbon Trust Standard demonstrates the company’s performance in reducing its operational greenhouse gas emissions.

### **Putting people’s health, safety and wellbeing first**

- With regards to health, safety and wellbeing, YW drives a “Plan–Do–Check–Act” continuous improvement cycle which is underpinned by the following principles:
  - strong and active leadership from the top down;
  - employee engagement and involvement; and
  - assessment and review.
- YW maintains a clear focus on meeting the needs of its people, stakeholders, customers and other members of the public and strives for continual improvement by:
  - complying with its duties under the Health and Safety at Work etc Act 1974 and all other relevant legislation;
  - identifying hazards and mitigating risks to levels as low as reasonably practicable;
  - seeking to eliminate injuries, incidents and ill health and minimise any consequences that might arise in the event of any incident;
  - providing training, monitoring, supervision and leadership to ensure the competence of employees and compliance with our Occupational Health and Safety (“OH&S”) policies and procedures;
  - assessing and monitoring the OH&S systems and performance of YW’s suppliers, partners and contractors to ensure their competence;
  - continually reviewing and challenging YW’s performance, and setting objectives; and
  - aiming to meet all of the above at an affordable cost to YW’s customers.
- YW uses an Occupational Health & Safety Management System to help ensure compliance with the standards and expectations of the Health and Safety Executive. YW aims to certify to the Occupational Health and Safety Assessment Series 18001 standard in 2015/16.

### **YW’s approach to risk management**

- Effective risk management is essential to manage YW’s uncertainties and achieve its Strategic Business Objectives. YW’s company-wide risk management framework provides a standard approach to the identification, assessment, monitoring and reporting of risk.

- All risks and their possible causes are considered and these are assessed to understand the potential impact if the risk were to occur. Risk assessment is completed using probability and impact scales and considers strategic, financial, commercial, operational, social, environmental, reputational and ethical opportunities and threats.
- Risks are monitored through a series of aligned registers at strategic, functional and operational levels. These registers are used to assess the risks, document their controls, establish mitigation plans and define ownership and accountability.
- YW's strategic risks capture everything that it has identified that could compromise the company's delivery of customer services, the expected outcomes for its key stakeholders, YW's regulatory contract and the company's reputation.

### Benchmarking

- YW assesses its performance using the Business in the Community Corporate Responsibility Index. During 2014/15, YW increased its score following improvements to both environmental and social practices, for example becoming a certified "Living Wage" employer, and achieved 4.5 out of 5 stars (up from 3.5 stars in 2013/14). YW continues to work to further improve its performance and aims to achieve 5 stars within the next two years.

### YW's key operational and environmental performance indicators

- YW's performance against the key operational and environmental performance indicators are shown in the table below.

Yorkshire Water		Target description	2014/15 performance	2013/14 performance	2012/13 performance
Service Incentive Mechanism (SIM)	Overall Score	Internal	<b>85</b>	82	78
Internal Sewer Flooding	Number of Incidents	Internal	<b>121</b>	76	155
Water Supply Interruptions	Hours per Properties Served	Internal	<b>0.16</b>	0.17	0.17
Serviceability Water Infrastructure	Stable / Improving / Marginal / Deteriorating	FD Obligation	<b>Stable</b>	Stable	Stable
Serviceability Water Non Infrastructure	Stable / Improving / Marginal / Deteriorating	FD Obligation	<b>Stable</b>	Stable	Stable
Serviceability Sewerage Infrastructure	Stable / Improving / Marginal / Deteriorating	FD Obligation	<b>Stable</b>	Stable	Stable
Serviceability Sewerage Non Infrastructure	Stable / Improving / Marginal / Deteriorating	FD Obligation	<b>Stable</b>	Stable	Stable
Total leakage	MI/d	FD Obligation	<b>288</b>	282	265
Security of Supply Index (SoSI)	Index Score	FD Obligation	<b>100</b>	100	100
Water Quality (Overall Compliance)*	Percentage	Internal	<b>99.94%</b>	99.96%	99.93%
Greenhouse Gas (GHG) Emissions	ktCO2e	FD Projection	<b>369</b>	357	386
Satisfactory Sludge Disposal*	Percentage	FD Obligation	<b>100.00%</b>	100.00%	97.72%
Discharge Permit Compliance*	Percentage	EA	<b>99.32%</b>	98.00%	97.31%
Pollution Incidents (sewerage)*	Category 1-3 incidents per 10,000km of sewer	EA	<b>58.82</b>	78.1	82.7
Serious Pollution Incidents (sewerage)*	Category 1-2 incidents per 10,000km of sewer	EA	<b>1.31</b>	3.27	1.63

\* Calendar year measures

## 4. 2014/15 financial performance

YW has again had a good set of financial results underpinned by continuing investment and improvement in its operational and environmental performance. The key financial performance indicators are shown in the table below.

YW key financial performance indicators	2014 £m	2015 £m	Increase / Decrease %
Turnover	984.2	<b>1,014.1</b>	3.0
Operating profit	330.2	<b>350.4</b>	6.1
EBITDA	601.6	<b>624.0</b>	3.7
Net interest payable	(188.0)	<b>(214.4)</b>	14.0
Net debt	4,560.4	<b>4,491.1</b>	(1.5)
Capital expenditure	356.0	<b>285.7</b>	(19.7)

The key financial performance highlights include the following.

- YW had anticipated a reduction in turnover during 2014/15 as the Company did not take up the annual price increase of 1.6%. However, a warm summer and an increase in commercial demand has offset this impact and the increase in turnover of 3.0% to £1,014.1m (2014: £984.2m) is primarily due to the movement in RPI during the period.
- Operating costs have been closely managed in the period increasing by £9.7m or 1.5%, principally caused by inflation. Given the rate of increase is below that of the increase seen in turnover this has resulted in an increase in operating profit of 6.1% to £350.4m (2014: £330.2m) and an increase in EBITDA of 3.7% to £624.0m (2014: £601.6m).
- Net interest payable increased to £214.4m in 2014/15 (2014: £188.0m). The principal reason for the increase is the change in the discount rate applied to the liability on YW's index linked swaps which has followed the movement in government gilts. This increase has been offset by lower levels of interest payable on intercompany loans.
- Net debt, which represents the value of loans and finance leases owed to third parties and other companies within Kelda Group and offset by available cash, decreased slightly by 1.5% to £4,491.1m (£4,560.4m).
- Capital expenditure for the 12 months to 31 March 2015 was £285.7m (2014: £356.0m) which was in line with the lower amount of capital expenditure planned towards the end of AMP5.

## 5. Company vision - "Taking responsibility for the water environment for good"

YW's activities and aspirations are bigger than its regulatory commitments alone and YW's six Strategic Business Objectives ("SBOs") include long term outcomes which will enable the company to achieve its vision of "Taking responsibility for the water environment for good".

YW's vision and six SBOs summarise everything that the company strives to deliver for society and its shareholders and encompass all its material issues as a business including environmental, financial and social. Each SBO is underpinned by annual targets that drive YW's activities towards medium-term milestones and long-term outcomes and to deliver these SBOs YW will have to out-perform its regulatory objectives and targets, to give the company the right reinvestment choices.

YW's six SBOs are as follows.



**Trusted company** – The way we do business means our products, services and promises are trusted by all our stakeholders, now and in the future.



**Safe water** – We work safely and we protect public health by ensuring drinking water is always safe to drink and waste water never harms customers or communities at any point in the process.



**Excellent catchments, rivers and coasts** – We maintain and improve the water environment from source to sea, and influence others to do the same.



**Water efficient regions** – We ensure water needs are met now and in the future by using water wisely and inspiring others to do the same.



**Sustainable resources** – We are efficient and effective now and in the future, with an industry leading workforce, zero waste and a responsible supply chain.



**Strong financial foundations** – We deliver services to customers at a price they are willing and able to pay, while providing investors with returns that attract long-term investment.

Through the company's 25 year planning process, YW has identified a range of external forces that are shaping its business over the long term. YW monitors and manages these forces through its risk management systems and long term planning. This is an on-going iterative process that ensures that YW always acts on the latest and best available evidence and understanding to ensure the long term sustainability of the business and the essential services that YW provide.

Throughout 2015/16 YW will update its analysis of the strategic forces shaping its business and services over the long term.

## 6. Regulatory update

### Ofwat's final determination

On 12 December, Ofwat made their final determination of future prices and plans. YW's regulatory business plan for the 2015-2020 period, which is called "Blueprint for Yorkshire" will see YW invest a further £3.8 billion in the Yorkshire region.

This will require YW to continue to focus on delivering more for less, with YW's customer bills due to fall by an average of 3% in real terms by 2020. This will ensure that YW's customer bills remain one of the lowest in the UK.

YW's regulatory business plan for the 2015-20 period is focused more than ever before on delivering its customers priorities which is central to YW's strategy and SBOs. YW engaged with over 30,000 customers and a wide range of stakeholders during the price review process to ensure that the company fully understood customer priorities, and to ensure that YW's "Blueprint for Yorkshire" met their expectations.

Through this engagement process YW worked with its customers to create seven customer outcomes. These seven customer outcomes (and associated 26 performance commitments) will ensure further improvement to all standards, including improvements to water quality and reducing pollution incidents. YW's seven customer outcomes are also underpinned by regulatory reputational and financial incentives.

#### Customer outcomes



We provide you with water that is clean and safe to drink



We provide the level of customer service you expect and value



We take care of your waste water and protect you and the environment from sewer flooding



We understand our impact on the wider environment and act responsibly



We protect and improve the water environment



We make sure that you always have enough water



We keep your bills as low as possible

**Water Act 2014**

The Water Act 2014 is driving the biggest programme of industry reform since privatisation, with several significant changes in the pipeline, the most immediate being the introduction of greater retail competition. From April 2017 all non-household customers (including YW's charity and public sector customers) will have the opportunity to choose their provider of water and waste water retail services.

YW recognises that increased retail competition presents both opportunities and threats to its business and is monitoring national developments closely as the company continues to prepare for the new retail operating regime. To manage the risks and exploit the opportunities that this presents, YW has created a new retail business (Yorkshire Water Business Services) to enhance how the company will meet the future needs of its non-domestic customers. YW continues to develop its strategy to ensure it remains the supplier of choice for its customers throughout the Yorkshire region.

The Water Act 2014 also introduces new provisions to facilitate the creation of a national water supply network and further improve the country's water efficiency and resilience. The Act aims to make it easier for water companies to buy and sell water from each other. YW has traded water with its neighbouring water companies for many years and considers such options as a standard part of its planning. YW documented its water trading policy in early 2015 and continues to investigate new trading opportunities that may prove financially and environmentally effective options to maintain the water supply demand balance in the future.

The Government is working to reform the abstraction licence regime over the coming years, with primary legislation anticipated. YW is engaged with the Department for Environment, Food and Rural Affairs, UK Water Industry Research and Water UK to monitor and inform the evolving national approach.

**7. Director changes**

On 18 June 2014 Kevin Whiteman announced that he would stand down from his role as non-executive Chairman of YW and Kelda Holdings Ltd prior to April 2015. Kevin remained on the board of each of these companies until his period of appointment as a non-executive director with the Kelda Group expired on 30 June 2015. Kevin also resigned from board appointments at each of the companies within the YW Financing Group on 30 June 2015.

On 27 June 2014 Roger Hyde retired from his role as independent non-executive director of YW.

On 27 June 2014 Ray O'Toole was appointed as an independent non-executive director of YW, replacing Roger Hyde. Ray's career includes senior positions in the transport sector including National Express plc, the British Transport Police Authority and the Office of Rail Regulation.

On 5 November 2014 YW announced that Richard Parry-Jones, CBE, was to become the non-executive Chairman of YW and Kelda Holdings Ltd from 1 April 2015, replacing Kevin Whiteman. Richard joined the Board of Directors of YW and Kelda Holdings Ltd on 1 January 2015, before officially taking over as non-executive chairman. Richard retired in 2007 as Group Vice-President, Global Product Development and Chief Technical Officer with the Ford Motor Company, where he had enjoyed a successful career spanning almost four decades around the world. Since his retirement, Richard has combined a career in consultancy with board roles at the global engineering business, GKN plc, where he is the Senior Independent Director, and at the UK's rail infrastructure and system operator, Network Rail, at which he was non-executive Chairman from 2012 to 2015. Richard has also devoted considerable time over the last ten years to providing public policy advice to governments in Westminster and Cardiff on topics ranging from industrial policy to transport and energy, and to working with universities to improve and promote teaching and research excellence in engineering. Richard is a fellow of the Royal Academy of Engineering, the Institute of Mechanical Engineers and the Royal Society of Statistical Science.

On 13 November 2014 it was announced that Chantal Forrest would become YW Company Secretary and Group Company Secretary from January 2015. Chantal's most recent role was Company Secretary and General Counsel at Electricity North West. Chantal has extensive experience operating in a combined legal/company secretary role having previously worked for WBB Minerals and Yorkshire Electricity Group. Chantal has also been appointed to the boards of each of the companies within the YW Financing Group.

On 31 December 2014 Stuart McFarlane resign from his role as YW Company Secretary and also on this date resigned from his other Kelda Group board appointments.

On 31 December 2014 Helen Phillips retired from her role as director of Customer Services and Networks.

## 8. Permitted Subsidiaries acquired pursuant to a Permitted Acquisition

There were no Permitted Subsidiaries acquired pursuant to a Permitted Acquisition during the 12 months to 31 March 2015.

## 9. Regulated capital investment

YW invests significant capital expenditure to add to and replace its plant and equipment. The price limits set by Ofwat every five years take into account the level of capital expenditure expected to be incurred during the relevant period and the associated funding costs and operating costs.

Regulated capital investment for the 12 months to 31 March 2015 was £285.7m (2014: £356.0m) as YW successfully completed its capital programme for AMP5. In addition, YW delivered all regulatory outputs on time and as forecast in the final business plan for the period 2010 to 2015, with the exception of one multi-agency sewer flooding study, the impact of which was partially offset by the over-delivery of sewer flooding outputs.

## 10. Outsourcing

YW continues to monitor and comply with the Outsourcing Policy as detailed under the Common Terms Agreement which states, amongst other things, that YW will act as a reasonably prudent water and sewerage undertaker and in accordance with good industry practice.

During July 2015, YW completed the renewal of its waste water network repair and maintenance contract. This is a major contract award and has been designed to deliver the best possible service for YW's customers at the best possible price. The new contract includes two fundamental changes to our service levels:

- speed of responses - 70% of front line customer responses will be on the same day and within an average of six hours. At present 75% of these jobs are next day within an average of 15 hours; and
- time to full restoration - a 40% reduction in the time it takes to close down the customer case from the time of the first customer contact.

The new contract will commence during September 2015.

## 11. Financing

On 30 October 2014 Yorkshire Water Services Bradford Finance Limited (“YWSBFL”) completed the issuance of £90.0m of Class A notes with a 15 year term. The interest payable on these notes was swapped into floating rate (without breaks) for the full term at issuance. The funds of this issuance were on-lent to YW on completion.

During June 2015, YW completed a liability management process that resulted in the removal of all of the 2018 break dates on its portfolio of index-linked swaps. As a result, the notional value of YW’s portfolio of index-linked swaps with mandatory breaks has been reduced from £452m to £292m with the first mandatory breaks now being in February 2020 (with a notional value of £117.5m).

## 12. Ratings

In May 2015, Standard & Poor’s announced that it held the rating of YW’s Class A debt at A, Stable and YW’s Class B debt at BBB, Stable.

In March 2015, Moody’s Investors Service downgraded YW’s corporate family rating to Baa2 from Baa1, YW’s Class A debt to Baa1 from A3, and YW’s Class B debt to Ba1 from Baa3. Moody’s noted that, in their view, notwithstanding that YW’s final determination was largely in-line with its business plan submissions and the company’s track record of solid operational performance, YW’s credit quality continues to be pressured by the company’s portfolio of inflation-linked derivatives and the deterioration in their associated mark-to-market value.

In February 2015, Fitch Ratings announced that it held the rating of YW’s Class A debt at A, Negative Outlook and moved the rating of YW’s Class B debt to BBB+, Stable from BBB+, Negative Outlook.

## 13. Surplus

YW’s dividend policy is:

- to deliver real growth in dividends recognising the management of economic risks, the continuing need for reinvestment of profits in the business, and to pay additional dividends which reflect efficiency improvements and particularly improvements beyond those assumed in the determination of price limits;
- to pay dividends in respect of the non-appointed business reflecting the profitability of those activities; and
- where it is foreseeable that the company will have sufficient profits available for distribution to continue to pay annual dividends consistent with this dividend policy, the Company can also pay special dividends as part of any capital reorganisation which the Board concludes to be in the best interests of the Company and which complies with its obligations under its licence.

YW’s Board and ultimate shareholders are committed to ensuring compliance with its covenanted financial ratios and also to maintain current ratings via, amongst other things, the retention of distributions and other balance sheet strengthening measures as and when it is prudent to do so.

## 14. Bank and liquidity facilities held by the YW Financing Group

During April 2015 both the O&M Reserve Facility (“O&M”) held at Yorkshire Water Services Odsal Finance Limited (“YWSOFL”) and the Debt Service Reserve Liquidity Facility (“DSR”) held at YWSBFL were renewed with a modest increase from the previous level of £292.3m to £305.4m in total (£65.6m and £239.8m for the O&M and DSR respectively) for a further 12 months to 31 March 2016.

As at 31 March 2015 there were no balances outstanding on either of these facilities.

As at 31 March 2015 YWSOFL had no drawn amounts on either of the Class A Capex Facility (£430m) or the Working Capital Facility (£60m). YWSOFL on-lends any drawings made on these facilities to YW.

## 15. Non-Participating YWSF Bond Reserve Account

The balance on the Non-Participating YWSF Bond Reserve Account on 31 March 2015 was £1.4m.

## 16. Authorised Investments

Authorised Investments as at 31 March 2015 are shown below.

Liquidity Fund	£m
GSAM	1.4
HSBC	15.9
<b>Total</b>	<b>17.3</b>

## 17. The Conformed ICR

As a result of changes to the way Ofwat calculates revenue for water companies from 1 April 2015, key covenants within YW's securitisation documents that rely upon the concept of Adjusted Interest Cover Ratio ("AICR") no longer operate as originally intended. This is because the concepts of Current Cost Depreciation ("CCD") and Infrastructure Renewals Charge ("IRC") no longer exist within the regulatory pricing regime (both CCD and IRC are deducted when arriving at the numerator of the AICR).

In response to this YW offered its debt investors a supplementary interest cover ratio covenant termed the Conformed Interest Cover Ratio ("CICR"), together with an associated additional information covenant. The CICR has been designed to provide a similar level of assurance to Yorkshire Water's bondholders as that originally provided by the AICR under the current regulatory regime.

On 18 June YW launched a formal creditor consent process (a "STID Proposal") to amend the securitisation documents with the inclusion of the CICR covenants and associated additional information covenant.

Voting on the proposal concluded on 9 July. The STID Proposal was passed by an overwhelming majority and of the £3.5bn of qualifying Class A debt, £2.9bn chose to vote, with 99.1% voting in favour. YW's financing documents have been amended to reflect the changes.

## 18. Ratios

The YW Financing Group confirms that in respect of the Calculation Date on 31 March 2015, by reference to the most recent financial statements that the YW Financing Group is obliged to deliver in accordance with Paragraph 1 (Financial Statements) of Part 1 (Information Covenants) of Schedule 4 (Covenants) to the Common Terms Agreement, the Ratios are as detailed in the table below.

Date	31/03/2015 Actual	31/03/2016 Forecast	31/03/2017 Forecast	31/03/2018 Forecast	31/03/2019 Forecast	31/03/2020 Forecast
Class A RAR	67.2%	68.7%	69.4%	74.2%	74.8%	74.4%
Senior RAR	77.2%	78.7%	78.8%	79.3%	79.7%	79.2%

Test Period	31/03/2015 Actual	31/03/2016 Forecast	31/03/2017 Forecast	31/03/2018 Forecast	31/03/2019 Forecast	31/03/2020 Forecast
Class A ICR	3.34x	2.91x	2.91x	2.98x	3.00x	3.04x
Class A Adjusted ICR	1.71x	2.91x	2.91x	2.98x	3.00x	3.04x
Senior Adjusted ICR	1.47x	2.50x	2.50x	2.58x	2.80x	2.84x
Class A Average Adjusted ICR	1.66x	2.93x	2.96x	3.01x	3.01x	3.26x
Senior Average Adjusted ICR	1.42x	2.53x	2.63x	2.74x	2.74x	2.95x
Conformed Class A Adjusted ICR		1.43x	1.44x	1.54x	1.50x	1.51x
Conformed Senior Adjusted ICR		1.22x	1.24x	1.33x	1.40x	1.42x
Conformed Class A Average Adjusted ICR		1.47x	1.49x	1.52x	1.52x	1.55x
Conformed Senior Average Adjusted ICR		1.27x	1.32x	1.38x	1.38x	1.40x

(together the “Ratios”).

YW is targeting a maintenance of gearing levels (ie its Class A RAR and Senior RAR percentages) no greater than circa 75% and 79% respectively for the 2015-2020 period. These levels of gearing will maintain the strength of the company’s balance sheet together with providing the necessary level of headroom in the company’s key interest cover ratios. This prudent approach also provides the company with the ability to manage the impact of any significant unforeseen events throughout the 2015-2020 period.

The YW Financing Group confirms that each of the above Ratios has been calculated in respect of each of the relevant periods for which it is required under the CTA and has not breached the Trigger Event Ratio Levels and has not caused Paragraph 17 (Ratios) of Part 2 (Events of Default - Non-YWH) of Schedule 6 (Events of Default) to the CTA to be breached.

For information, set out below are the computations of the ratios detailed overleaf.

Test Period		Year ending 31/03/2015 Actual	Year ending 31/03/2016 Forecast	Year ending 31/03/2017 Forecast	Year ending 31/03/2018 Forecast	Year ending 31/03/2019 Forecast	Year ending 31/03/2020 Forecast
Net Cash Flow divided by	£m	628.7	558.2	571.1	617.4	648.0	671.9
Class A Debt Interest	£m	188.1	192.0	196.4	207.0	216.0	220.9
<b>Class A ICR</b>	<b>times</b>	<b>3.34</b>	<b>2.91</b>	<b>2.91</b>	<b>2.98</b>	<b>3.00</b>	<b>3.04</b>
Net Cash Flow	£m	628.7	558.2	571.1	617.4	648.0	671.9
Less CCD and IRC	£m	<u>(306.3)</u>	<u>0.0</u>	<u>0.0</u>	<u>0.0</u>	<u>0.0</u>	<u>0.0</u>
Adjusted Cash Flow divided by	£m	322.4	558.2	571.1	617.4	648.0	671.9
Class A Debt Interest	£m	188.1	192.0	196.4	207.0	216.0	220.9
<b>Class A Adjusted ICR</b>	<b>times</b>	<b>1.71</b>	<b>2.91</b>	<b>2.91</b>	<b>2.98</b>	<b>3.00</b>	<b>3.04</b>
Net Cash Flow	£m	628.7	558.2	571.1	617.4	648.0	671.9
Less CCD and IRC	£m	<u>(306.3)</u>	<u>0.0</u>	<u>0.0</u>	<u>0.0</u>	<u>0.0</u>	<u>0.0</u>
Adjusted Cash Flow divided by	£m	322.4	558.2	571.1	617.4	648.0	671.9
Senior Debt Interest	£m	219.5	223.5	228.4	239.1	231.3	236.4
<b>Senior Adjusted ICR</b>	<b>times</b>	<b>1.47</b>	<b>2.50</b>	<b>2.50</b>	<b>2.58</b>	<b>2.80</b>	<b>2.84</b>
Year 1 Class A Average Adjusted ICR	times	1.65	2.91	2.91	2.98	3.00	3.04
Year 2 Class A Average Adjusted ICR	times	1.60	2.91	2.98	3.00	2.98	3.31
Year 3 Class A Average Adjusted ICR	times	1.71	2.98	3.00	3.04	3.04	3.41
<b>Class A Average Adjusted ICR</b>	<b>times</b>	<b>1.66</b>	<b>2.93</b>	<b>2.96</b>	<b>3.01</b>	<b>3.01</b>	<b>3.26</b>
Year 1 Senior Average Adjusted ICR	times	1.42	2.50	2.50	2.58	2.80	2.84
Year 2 Senior Average Adjusted ICR	times	1.38	2.50	2.58	2.80	2.58	3.08
Year 3 Senior Average Adjusted ICR	times	1.47	2.58	2.80	2.84	2.84	2.91
<b>Senior Average Adjusted ICR</b>	<b>times</b>	<b>1.42</b>	<b>2.53</b>	<b>2.63</b>	<b>2.74</b>	<b>2.74</b>	<b>2.95</b>
Net Cash Flow	£m		558.2	571.1	617.4	648.0	671.9
Less Depreciation	£m		(115.5)	(98.9)	(89.6)	(107.3)	(135.0)
Less IRE not already deducted in the calculation of Net Cash Flow or	£m		(211.0)	(248.3)	(257.8)	(255.7)	(215.9)
Fast/Slow Adjustment	£m		<u>42.1</u>	<u>59.7</u>	<u>48.8</u>	<u>38.5</u>	<u>13.5</u>
Adjusted Cash Flow divided by	£m		273.7	283.7	318.8	323.4	334.6
Class A Debt Interest	£m		192.0	196.4	207.0	216.0	220.9
<b>Conformed Class A Adjusted ICR</b>	<b>times</b>		<b>1.43</b>	<b>1.44</b>	<b>1.54</b>	<b>1.50</b>	<b>1.51</b>
Net Cash Flow	£m		558.2	571.1	617.4	648.0	671.9
Less Depreciation	£m		(115.5)	(98.9)	(89.6)	(107.3)	(135.0)
Less IRE not already deducted in the calculation of Net Cash Flow or	£m		(211.0)	(248.3)	(257.8)	(255.7)	(215.9)
Fast/Slow Adjustment	£m		<u>42.1</u>	<u>59.7</u>	<u>48.8</u>	<u>38.5</u>	<u>13.5</u>
Adjusted Cash Flow divided by	£m		273.7	283.7	318.8	323.4	334.6
Senior Debt Interest	£m		223.5	228.4	239.1	231.3	236.4
<b>Conformed Senior Adjusted ICR</b>	<b>times</b>		<b>1.22</b>	<b>1.24</b>	<b>1.33</b>	<b>1.40</b>	<b>1.42</b>

Test Period		Year ending 31/03/2015 Actual	Year ending 31/03/2016 Forecast	Year ending 31/03/2017 Forecast	Year ending 31/03/2018 Forecast	Year ending 31/03/2019 Forecast	Year ending 31/03/2020 Forecast
Year 1 Conformed Class A Average Adjusted ICR	times		1.43	1.44	1.54	1.50	1.51
Year 2 Conformed Class A Average Adjusted ICR	times		1.44	1.54	1.50	1.54	1.54
Year 3 Conformed Class A Average Adjusted ICR	times		1.54	1.50	1.51	1.51	1.59
<b>Conformed Class A Average Adjusted ICR</b>	<b>times</b>		<b>1.47</b>	<b>1.49</b>	<b>1.52</b>	<b>1.52</b>	<b>1.55</b>
Year 1 Conformed Senior Average Adjusted ICR	times		1.22	1.24	1.33	1.40	1.42
Year 2 Conformed Senior Average Adjusted ICR	times		1.24	1.33	1.40	1.33	1.43
Year 3 Conformed Senior Average Adjusted ICR	times		1.33	1.40	1.42	1.42	1.36
<b>Conformed Senior Average Adjusted ICR</b>	<b>times</b>		<b>1.27</b>	<b>1.32</b>	<b>1.38</b>	<b>1.38</b>	<b>1.40</b>
Class A Net Indebtedness divided by RCV	£m	3,970.9	4,039.5	4,306.8	4,838.9	5,103.1	5,304.5
	£m	5,907.2	5,879.8	6,208.7	6,524.6	6,824.5	7,126.4
<b>Class A RAR</b>	<b>%</b>	<b>67.2</b>	<b>68.7</b>	<b>69.4</b>	<b>74.2</b>	<b>74.8</b>	<b>74.4</b>
Senior Net Indebtedness divided by RCV	£m	4,558.1	4,626.7	4,893.9	5,176.1	5,440.3	5,641.6
	£m	5,907.2	5,879.8	6,208.7	6,524.6	6,824.5	7,126.4
<b>Senior RAR</b>	<b>%</b>	<b>77.2</b>	<b>78.7</b>	<b>78.8</b>	<b>79.3</b>	<b>79.7</b>	<b>79.2</b>

Under the terms of the CTA, Compliance Certificates are completed for the whole YW Financing Group and therefore certain adjustments are required to be made to the financial information contained within the financial statements of YW when calculating the ratios reported in the above table. The tables below details these necessary adjustments and reconciles the calculations of Senior Net Indebtedness, Net Cash Flow, and Class A and Senior Debt Interest contained within this report against the financial statements of YW for the 12 months ended 31 March 2015.

Net debt	£m
Net debt (note 12 to YW's statutory accounts)	3,482.1
Ring-fenced cash excluded for covenant calculation purposes (note 12 to YW's statutory accounts)	12.0
Intercompany loans to / (from) other members of the YW Financing Group that reverse on consolidation (note 12 to YW's statutory accounts)	(32.5)
Subordinated loans to Kelda Holdco Ltd (note 12 to YW's statutory accounts)	1,009.0
Discount on RPI accretion on index linked swaps excluded from debt covenants (note 13 to YW's statutory accounts)	85.1
Add back unamortised issue costs (note 12 to YW's statutory accounts)	2.4
<b>Senior Net Indebtedness</b>	<b>4,558.1</b>
<b>of which Class A Net Indebtedness</b>	<b>3,970.9</b>

<b>Net Cash Flow</b>	<b>£m</b>
Operating profit excluding exceptionals (YW's P&L account)	350.4
Depreciation & amortisation (note 2 to YW's statutory accounts)	273.6
Movements in working capital (note 8 to the YW's regulatory accounts)	4.9
Appointed company tax received / (paid) (YW's regulatory accounts - current cost cashflow statement for the appointed business)	18.1
Non-appointed company tax received / (paid) (note 4 to the YW's regulatory accounts)	(0.8)
Less one-off tax items (note 4 to the YW's regulatory accounts)	(17.5)
<b>Net Cash Flow</b>	<b>628.7</b>

<b>Class A / Senior Debt Interest</b>	<b>£m</b>
Returns on investments and servicing of finance (YW's regulatory accounts - current cost cashflow statement for the appointed business)	150.0
Add back interest received on subordinated loan to Kelda Holdco Ltd (note 3 to YW's statutory accounts)	41.6
Add back interest received on subordinated loan to Kelda Non-regulated Holdco Ltd (note 3 to YW's statutory accounts)	20.8
Add loan repayment from YW to YWSOFL recognised as interest within the YW Financing Group's interest cover ratios (note 15 to YWSOFL's statutory accounts)	5.9
Add back one off, non-recurring interest received (note 3 to YW's statutory accounts)	1.2
<b>Senior Debt Interest</b>	<b>219.5</b>
<b>of which Class A Debt Interest</b>	<b>188.1</b>

The YW Financing Group certifies that on 31 March 2015 the Annual Finance Charge for the twelve months to 31 March 2016 (excluding Finance Lease rental payments) is forecast at £223.5m. The Monthly Payment Amount is forecast at £14.8m, having been adjusted to cover the large interest payments made in April 2015 of circa £61m.

This Investors Report also confirms that:

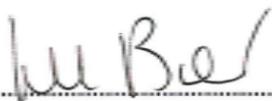
- (a) no Default or Potential Trigger Event is outstanding; and
- (b) that YW's insurances are being maintained in accordance with:
  - (i) the CTA; and
  - (ii) the provisions of the Finance Leases.

Yours faithfully

  
Liz Barber  
Group Director of Finance, Regulation & Markets

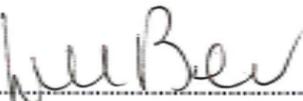
  
Richard Flint  
Chief Executive

*For and on behalf of*  
**YORKSHIRE WATER SERVICES LIMITED**

  
Liz Barber  
Director

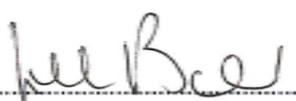
  
Chantal Forrest  
Director

*For and on behalf of*  
**YORKSHIRE WATER SERVICES BRADFORD FINANCE LIMITED**

  
Liz Barber  
Director

  
Chantal Forrest  
Director

*For and on behalf of*  
**YORKSHIRE WATER SERVICES FINANCE LIMITED**

  
Liz Barber  
Director

  
Chantal Forrest  
Director

*For and on behalf of*  
**YORKSHIRE WATER SERVICES ODSAL FINANCE LIMITED**

# Yorkshire Water Financing Group

## Investors Report

*For the period ended 31 March 2015*

For further information regarding this Investors Report please contact either:

- Adrian Hunt (Group Treasurer) or
- Matthew Cherrington (Group Borrowings Manager)

at:

Yorkshire Water Services Ltd  
Western House, Western Way  
Halifax Road (PO Box 500)  
Bradford BD6 2LZ

or E-mail:

- [adrian.hunt@yorkshirewater.co.uk](mailto:adrian.hunt@yorkshirewater.co.uk)
- [matthew.cherrington@yorkshirewater.co.uk](mailto:matthew.cherrington@yorkshirewater.co.uk)