

Kelda Finance (No.1) Limited

Consolidated Interim Financial Statements

For the 6 month period ended 30 September 2015

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Information to accompany the consolidated interim financial statements

Presented below are the consolidated results for Kelda Finance (No.1) Limited for the 6 month period ended 30 September 2015. These are prepared under International Financial Reporting Standards.

Kelda Finance (No.1) Limited is the holding company of a group including Kelda Finance (No.2) Limited, Kelda Finance (No.3) PLC, Yorkshire Water Services Holdings Limited and its subsidiary companies.

Group income statement

For the 6 month period ended 30 September 2015

		Unaudited 6 month period ended 30 Sep 2015 £m	Unaudited 6 month period ended 30 Sep 2014 £m	Audited Year ended 31 Mar 2015 £m
	Note			
Group revenue		493.5	508.5	1,006.1
Operating costs		(332.5)	(308.4)	(609.8)
Group operating profit from continuing operations		161.0	200.1	396.3
Finance income		41.9	41.0	85.1
Exceptional finance income	2	106.1	30.0	9.0
Finance costs		(140.7)	(145.6)	(294.0)
Exceptional finance costs	2	(20.1)	(126.6)	(378.5)
Profit/(loss) from continuing operations before taxation		148.2	(1.1)	(182.1)
Tax	3	(9.9)	30.0	76.6
Profit/(loss) for the period from continuing operations		138.3	28.9	(105.5)

Group statement of comprehensive income

For the 6 month period ended 30 September 2015

	Unaudited 6 month period ended 30 Sep 2015 £m	Unaudited 6 month period ended 30 Sep 2014 £m	Audited Year ended 31 Mar 2015 £m
Profit/(loss) for the period	138.3	28.9	(105.5)
Other comprehensive income for the period	-	-	187.8
Total comprehensive income for the period	138.3	28.9	82.3

Balance sheet

As at 30 September 2015

	Note	Unaudited At 30 Sep 2015 £m	Unaudited At 30 Sep 2014 £m	Audited At 31 Mar 2015 £m
Non-current assets				
Intangible assets		14.2	14.2	14.2
Property, plant and equipment		6,763.7	6,483.2	6,782.1
Financial assets	6	50.8	-	67.8
Trade and other receivables		1,261.0	1,261.0	1,256.9
		8,089.7	7,758.4	8,121.0
Current assets				
Inventories		1.9	0.8	1.3
Trade and other receivables		203.1	205.7	188.3
Tax assets		5.2	19.7	5.0
Cash and cash equivalents	5	44.1	40.8	37.0
		254.3	267.0	231.6
Total Assets		8,344.0	8,025.4	8,352.6
Current liabilities				
Trade and other payables		(470.5)	(457.2)	(496.2)
Tax liabilities		(0.1)	-	-
Short term borrowings	5	(125.3)	(216.4)	(140.1)
		(595.9)	(673.6)	(636.3)
Non-current liabilities				
Long term borrowings	5	(4,676.1)	(4,568.0)	(4,678.7)
Long-term payables		(33.5)	(45.2)	(31.4)
Financial liabilities		(1,661.2)	(1,481.6)	(1,739.3)
Deferred grants and contributions on depreciated assets	6	(47.2)	(49.7)	(48.9)
Provisions		(0.6)	(7.0)	(0.7)
Deferred tax liabilities		(499.5)	(486.5)	(489.7)
		(6,918.1)	(6,638.0)	(6,988.7)
Total liabilities		(7,514.0)	(7,311.6)	(7,625.0)
Net assets		830.0	713.8	727.6
Capital and reserves				
Ordinary shares	9	-	-	-
Hedging reserve		(13.9)	(13.2)	(13.2)
Revaluation reserve		201.6	13.8	201.6
Accumulated profit		642.3	713.2	539.2
Total shareholder's funds		830.0	713.8	727.6

Group cash flow statement

For the 6 month period ended 30 September 2015

	Note	Unaudited 6 month period ended 30 Sep 2015 £m	Unaudited 6 month period ended 30 Sep 2014 £m	Audited Year ended 31 Mar 2015 £m
Cash flows from operating activities	7	310.7	339.4	623.3
Income taxes (paid) / received		(0.2)	(0.2)	17.5
Interest paid	8	(168.3)	(160.7)	(255.6)
Net cash generated from operating activities		142.2	178.5	385.2
Cash flows from investing activities				
Interest received	8	41.7	34.7	84.3
Proceeds on disposals of property, plant and equipment		0.2	0.7	1.4
Purchases of property, plant and equipment		(131.4)	(123.2)	(268.4)
Capital grants and contributions		5.5	9.0	21.2
Net cash used in investing activities		(84.0)	(78.8)	(161.5)
Cash flows from financing activities				
Dividends paid	4	(35.2)	(39.3)	(78.4)
Borrowings raised (net of fees)		173.9	-	89.7
Repayment of borrowings		(158.2)	(23.4)	(199.3)
Repayments of obligations under finance leases and hire purchase agreements		(31.6)	(26.4)	(28.9)
Net cash used in financing activities		(51.1)	(89.1)	(216.9)
Net increase in cash and cash equivalents		7.1	10.6	6.8
Cash and cash equivalents at the start of the period		37.0	30.2	30.2
Cash and cash equivalents at the end of the period	5	44.1	40.8	37.0

Group statement of changes in equity

For the 6 month period ended 30 September 2015

	Ordinary shares	Hedging reserve	Revaluation reserve	Retained Earnings	Total equity
	£m	£m	£m	£m	£m
At 1 April 2014	-	(13.2)	13.8	723.6	724.2
Loss for the year	-	-	-	(105.5)	(105.5)
Dividends paid	-	-	-	(78.4)	(78.4)
Other movements	-	-	-	(0.5)	(0.5)
Other comprehensive income	-	-	187.8	-	187.8
At 31 March 2015	-	(13.2)	201.6	539.2	727.6
Profit for the period	-	-	-	138.3	138.3
Energy Swap	-	(0.7)	-	-	(0.7)
Dividends	-	-	-	(35.2)	(35.2)
At 30 September 2015	-	(13.9)	201.6	642.3	830.0

Notes to the financial statements

For the six months ended 30 September 2015

1. Basis of preparation and accounting

The financial statements are produced under International Financial Reporting Standards (IFRS).

The accounting policies, methods of computation and presentation are consistent with those used for the audited financial statements of Kelda Finance (No.1) Limited for the period ended 31 March 2015.

These interim accounts consolidate the results of Kelda Finance (No.1) Limited, Kelda Finance (No.2) Limited, Kelda Finance (No.3) PLC, Yorkshire Water Services Holdings Limited and its subsidiary companies for the six month period ending 30 September 2015.

2. Exceptional finance income and costs

	Unaudited 6 month period ended 30 Sept 2015 £m	Unaudited 6 month period ended 30 Sept 2014 £m	Audited Year ended 31 March 2015 £m
Interest receivable and similar income			
Movement of fair value of combined cross currency interest rate swaps	-	13.0	4.2
Movement in fair value of cross currency debt	6.7	-	-
Movement of fair value of fixed to floating interest rate swaps	-	17.0	4.8
Movement in fair value of associated bonds	17.5	-	-
Movement of fair value of finance lease interest rate swap	2.1	-	-
Movement of fair value of index linked swaps	79.8	-	-
	106.1	30.0	9.0
Interest payable and similar charges			
Movement of fair value of index linked swaps	-	(94.7)	(369.9)
Movement of fair value of finance lease interest rate swap	-	(2.4)	(8.6)
Movement in fair value of fixed to floating interest rate swaps	(10.4)	-	-
Movement in fair value of associated bonds	-	(17.4)	-
Movement of fair value of combined cross currency interest rate swaps	(9.7)	-	-
Movement in fair value of cross currency debt	-	(12.1)	-
	(20.1)	(126.6)	(378.5)

The movement in the fair value of index linked swaps is a result of swaps which were taken out by the Company during 2007/08. These swaps hedge against movements in the retail price index (RPI) by receiving interest based on LIBOR and accruing interest payable based on RPI. The swaps have been valued at the reporting date at fair value, which at 30 September 2015 resulted in a £1,771.5m liability (31 March 2015: £1,858.3m liability). Of this, £1,628.8m (31 March 2015: £1,708.6m) is recognised within other financial liabilities and £142.7m (31 March 2015: £149.7m) is recognised within long term borrowings.

Of the movement for the period of £86.8m income, a charge of £9.7m relating to RPI accretion has been recognised within finance costs, a credit of £79.8m has been recognised as an exceptional finance income and the net remaining movement of £16.7m was cash paid. Non cash changes in fair value of this instrument have been included in the profit and loss account as the specific circumstances which would allow it to be held in reserves have not been met and therefore hedge accounting has not been applied.

The movement in the fair value of finance lease swaps is a result of floating to fixed interest rate swaps taken out by the Company to hedge against movements in 12 month LIBOR interest rates on floating rate finance leases. The swaps hedge the movement in interest rates by receiving interest based on 12 month LIBOR and accruing interest payable at a fixed rate. The swaps have been valued at the reporting date at fair value, which at 30 September 2015 resulted in a £22.1m liability (31 March 2015: £24.2m). The decrease in the period in the liability of £2.1m has been recognised as an exceptional finance cost. This has been included in the profit and loss account as the specific circumstances which would allow it to be held in reserves were no longer met.

Notes to the financial statements

For the six months ended 30 September 2015

Exceptional finance payable includes the fair value movement of various combined cross currency interest rate swaps which were designated in fair value hedge relationships. The combined cross currency interest rate swaps have been valued at the reporting date at fair value. In line with FRS 102, the financial instruments to which the swaps relate have also been measured at fair value at 30 September 2015. The net impact of the fair value movement of the cross currency swaps and the associated bonds has resulted in a £3.0m charge to the profit and loss account.

Exceptional finance income includes the fair value movement of various fixed to floating interest rate swaps which were designated in fair value hedge relationships. These fair value interest rate swaps have been valued at the reporting date at fair value. In line with FRS102, the financial instruments to which the swaps relate have also been measured at fair value at 30 September 2015. The net impact of the fair value movement of the fixed to floating interest rate swaps and the associated bonds has resulted in a £7.1m credit to the profit and loss account.

3. Tax (charge)/credit

	Unaudited	Unaudited	Audited
	6 month	6 month	Year
	period ended	period ended	ended
	30 Sep 2015	30 Sep 2014	31 Mar 2015
	£m	£m	£m
Tax relating to continuing operations:			
Current tax	(0.1)	(0.2)	(0.3)
Deferred tax	(9.8)	20.2	60.9
Prior year tax	-	10.0	16.0
	(9.9)	30.0	76.6

The current tax (charge)/credit comprises corporation tax calculated at the estimated effective tax rates for the year.

4. Dividends paid

	Unaudited	Unaudited	Audited
	6 month	6 month	Year
	period ended	period ended	ended
	30 Sep 2015	30 Sep 2014	31 Mar 2015
	£m	£m	£m
Cash dividends	35.2	39.3	78.4
Total dividends	35.2	39.3	78.4

Notes to the financial statements

For the six months ended 30 September 2015

5. Analysis of net debt

	Unaudited At 30 Sep 2015 £m	Unaudited At 30 Sep 2014 £m	Audited At 31 Mar 2015 £m
Cash and cash equivalents:			
Cash at bank and in hand	24.8	26.1	23.3
Short term deposits	19.3	14.7	13.7
	44.1	40.8	37.0
Short term borrowings:			
Bank loans	(88.2)	(182.9)	(106.0)
Finance leases	(37.1)	(33.5)	(34.1)
	(125.3)	(216.4)	(140.1)
Long term borrowings:			
Bank loans	(262.4)	(291.6)	(277.1)
Bank loans under Kelda Finance facility	(65.0)	(65.0)	-
Fixed rate guaranteed bonds due in less than 5 years	(722.8)	(448.2)	(722.4)
Fixed rate guaranteed bonds due in more than 5 years	(1,507.4)	(1,915.2)	(1,778.6)
Index linked guaranteed bonds due in less than 5 years	(6.0)	-	-
Index linked guaranteed bonds due in more than 5 years	(1,468.9)	(1,212.7)	(1,208.7)
Fixed rate US Dollar bonds due in less than 5 years	(28.2)	(28.2)	(28.2)
Fixed rate US Dollar bonds due in more than 5 years	(282.1)	(249.6)	(285.8)
Fixed rate AUS Dollar bonds due in more than 5 years	(25.4)	(27.7)	(28.3)
Index linked swaps	(142.7)	(129.4)	(149.7)
Finance leases	(165.2)	(200.4)	(199.9)
	(4,676.1)	(4,568.0)	(4,678.7)
Amounts owed by parent entities	1,009.0	1,009.0	1,009.0
Total net debt	(3,748.3)	(3,734.6)	(3,772.8)

Included in long term bank loans stated above of £262.4m is £197.5m held by Kelda Finance (No.3) PLC and £65.0m held by Kelda Finance (No.2) Limited. With the exception of the £197.5m loan mentioned above and £65.0m held under the Kelda Finance facility, all long-term debt is held within the Yorkshire Water Services Holdings Limited group of companies.

Of the total net debt, £587.2m (31 March 2015: £587.2m) relates to Class B debt. Net debt at 30 September 2015 includes £1,009.0m of amounts due from group companies (31 March 2015: £1,009.0m).

Index linked swaps of £142.7m (31 March 2015: £149.7m), represent £226.7m (31 March 2015: £234.8m) of RPI accretion discounted by £84.0m (31 March 2015: £85.1m) to reflect the net present value of the future liability.

Included in net debt above are £5.5m (2013: £6.6m) of unamortised loan issue costs.

Notes to the financial statements

For the six months ended 30 September 2015

6. Other financial assets and liabilities

	Unaudited 6 month period ended 30 Sep 2015 £m	Unaudited 6 month period ended 30 Sep 2014 £m	Audited Year ended 31 March 2015 £m
Financial assets:			
Fixed to floating interest rate swaps	28.6	-	39.0
Combined cross currency interest rate swaps	22.2	-	28.8
	50.8	-	67.8
Financial liabilities:			
Finance lease interest swaps	(22.1)	(18.1)	(24.2)
Inflation linked swaps	(1,628.8)	(1,433.4)	(1,708.6)
Combined cross currency interest rate swaps	(9.6)	(17.8)	(6.5)
Fixed to floating interest rate swaps	-	(12.3)	-
Energy swap	(0.7)	-	-
	(1,661.2)	(1,481.6)	(1,739.3)

Interest rate swaps

Yorkshire Water holds £45.0m notional value of floating to fixed rate interest swaps. These swaps are recognised at a fair value liability of £22.1m at 30 September 2015 (31 March 2015: £24.2m). Hedge accounting has not been applied.

Yorkshire Water holds £430.0m notional value of fixed to floating rate interest swaps. These swaps are recognised at a fair value asset of £28.6m at 30 September 2015 (31 March 2015: £39.0m). Hedge accounting has been applied.

Cross currency interest rate swaps

Yorkshire Water hedges the fair value of the US dollar notes using a series of combined interest rate and foreign currency swaps that in combination form cross currency interest rate swaps, swapping dollar principal repayments into sterling and fixed rate dollar interest payments into floating rate sterling interest payments. These swaps are recognised at a fair value asset of £22.2m at 30 September 2015 (31 March 2015: £28.8m). Hedge accounting has been applied.

Yorkshire Water hedges the fair value of the Australian dollar bond using a combined interest rate and foreign currency swap, swapping Australian dollar principal repayments into sterling and fixed rate Australian dollar interest payments into floating rate sterling interest payments. These swaps are recognised at a fair value liability of £9.6m at 30 September 2015 (31 March 2015: £6.5m). Hedge accounting has been applied.

Index linked swaps

The Company holds a number of index linked swaps, with a notional value of £1,289.0m (31 March 2015: £1,289.0m).

There are three cash flows associated with the swaps:

- six monthly interest receivable linked to LIBOR;
- six monthly interest payable linked to RPI; and
- an RPI-linked bullet that is payable on maturity of the instruments or at certain predetermined dates over the duration of the swaps.

Interest payments and receipts are accrued in the profit and loss account. The RPI bullet accumulated at the balance sheet date has been discounted using an appropriate rate applied to the specific life of the future accretion pay downs of the index linked swaps. This is accrued in the profit and loss account and recognised within long term borrowings.

With six month LIBOR and applicable discount rates at historically low levels in the short term, these swaps gave rise to a fair value liability of £1,771.5m at 30 September 2015 (31 March 2015: £1,858.3m). Of this, £142.7m has been recognised within long term borrowings, and represents the discounted value of the RPI bullet accrued to 30 September 2015 (31 March 2015: £149.7m). The remaining £1,628.8m is recognised within other financial liabilities (31 March 2015: £1,708.6m). The RPI bullet

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For the six months ended 30 September 2015

accrued to 30 September 2015 was £142.7m (31 March 2015: £149.7m) which has been reduced by £84.0m (31 March 2015: £85.1m) when discounted to present values.

Under the index linked swaps, Yorkshire Water has contracted to pay a fixed rate on an inflation accreting notional and in return receives 6 month GBP LIBOR on a semi-annual basis. The contractual obligations of approximately two thirds of Yorkshire Water's portfolio of index linked swaps require Yorkshire Water to pay the inflation accretion of the notional amount at maturity as a single "bullet" payment. The remaining (ie one third) require Yorkshire Water to make periodic payments of the inflation accretion on the notional amount throughout the life of each swap.

This payment profile at maturity increases the potential credit exposure for the counterparties involved. In order to mitigate this credit exposure, a number of these swaps are subject to mandatory termination clauses ("MTC"). Under the MTC the inflation linked swaps will automatically be terminated for a cash settlement amount at each MTC date unless both Yorkshire Water and the respective counterparty agree to extend the MTC date or restructure the existing transactions.

As at 31 March 2015 Yorkshire Water's portfolio of index linked swaps had a total fixed notional value of £1,289m and a total fair value liability of £1,858.3m. Of this amount approximately 35% of the total notional value was subject to MTCs. As at 30 September 2015 Yorkshire Water's portfolio of index linked swaps had a total fixed notional of £1,289m and a total fair value liability of £1,771.5m. Of this amount approximately 23% of the total notional of the portfolio was subject to MTCs (with the mandatory breaks occurring in February 2020, February 2023 and February 2025).

During the reporting period Yorkshire Water executed a number of transactions with various counterparties to restructure a portion of Yorkshire Water's index linked swap portfolio with a total fixed notional value of £160 million which removed the MTCs effective in February 2018.

The transactions removed the MTCs in return for an increase in the fixed real rate and this gave rise to an increase in the net mark to market at execution of £50m which is to be recognised in the income statement over the remaining life of the inflation linked swaps.

The valuation model used by Yorkshire Water to determine the fair value of the inflation linked swap portfolio as at 30 September 2015 includes a funding valuation adjustment, credit valuation adjustment and debit valuation adjustment to reflect the long term credit risk of Yorkshire Water's index linked swap portfolio. Reflecting this model and the inputs involved, some of the inflation linked swaps are now considered a level 3 valuation under IFRS13 and are disclosed accordingly.

Notes to the financial statements

For the six months ended 30 September 2015

7. Reconciliation of profit/(loss) from continuing operations to cash generated by continuing operations

	Unaudited 6 month period ended 30 Sep 2015 £m	Unaudited 6 month period ended 30 Sep 2014 £m	Audited Year ended 31 Mar 2015 £m
Profit/(loss) from continuing operations before taxation	148.2	(1.1)	(182.1)
Finance income	(41.9)	(41.0)	(85.1)
Finance costs	140.7	145.6	294.0
Exceptional finance (income)/costs (non-cash)	(86.0)	96.6	369.5
Movements of fair value of derivative financial instrument (energy contracts)	-	-	(6.4)
Depreciation and amortisation of capital grants	125.2	118.8	221.4
Profit on disposal of property, plant and equipment	(0.2)	(0.3)	-
(Increase)/decrease in inventories	(0.6)	(0.1)	(0.5)
(Increase)/decrease in trade and other receivables	(19.2)	(17.7)	3.5
Increase in trade and other payables	44.5	38.7	9.7
Movement in provisions	-	(0.1)	-
Other non-cash movements	-	-	(0.7)
Cash generated from continuing operations	310.7	339.4	623.3

8. Cash interest

	Unaudited 6 month period ended 30 Sep 2015 £m	Unaudited 6 month period ended 30 Sep 2014 £m	Unaudited Year ended 31 Mar 2015 £m
Cash interest received:			
External interest received by Yorkshire Water financing group	10.0	4.0	21.6
Interest received from parent entities	31.7	30.7	62.7
	41.7	34.7	84.3
Cash interest paid:			
External interest on Kelda Finance facility	13.4	7.5	15.0
External interest paid by Yorkshire Water financing group	154.9	153.2	240.6
	168.3	160.7	255.6

Notes to the financial statements

For the six months ended 30 September 2015

9. Share capital

	Ordinary shares	
	Number	£
Closing balance at 31 March 2015 and 30 September 2015	100	100

10. Contingent liabilities

On 20 July 2015 an employee of the Company suffered a fatal accident while carrying out their duties. This is currently subject to a Police and Health and Safety Executive investigation. The duration, timing and outcome of this investigation are currently unknown.

Should the Company be found liable as a result of these investigations (which has not been intimated by any authority) it is possible it will be subject to fines, the size and timing of which are unknown due to the early stages of the investigation.

