FitchRatings

Corporates
Utilities - Non US
United Kingdom

Yorkshire Water Services Finance Limited; Yorkshire Water Finance Plc

The debt ratings of Yorkshire Water Services Finance Limited (YWSF) and Yorkshire Water Finance Plc's (YWF) reflect the group's commitment to restore about GBP940 million of equity at Yorkshire Water Services Limited operating company Yorkshire Water (YWS), largely by receiving repayments of legacy intercompany loans before the financial year to end-March 2027 (FYE27), resulting in an updated financial policy to target maximum regulatory gearing at YWS of 72% by FYE25.

The ratings also consider the operational and regulatory performance of YWS, and the secured nature of the group's financing structure. The latter benefits from structural enhancements, including trigger mechanisms (gearing and interest coverage covenants) and debt service reserve liquidity.

Key Rating Drivers

Gearing Headroom to Improve: Fitch Ratings expects adequate gearing headroom by FY25, mainly due to a gradual repayment of GBP940 million intercompany loans at YWS. This will largely support financial resilience through reduced debt funding requirements, while GBP100 million will be used to fund investment into the reduction of storm overflow spills. We forecast Yorkshire Water's adjusted class A net debt to regulated capital value (RCV) of about 70% against our negative rating sensitivity of 72%.

The Kelda corporate group publicly committed to the UK's water regulation authority (Ofwat) to repay its intercompany loans between Kelda Eurobond (borrower) and YWS (lender) following Ofwat's investigation on compliance of its intercompany loans with its licence requirements.

Kelda expects to repay its intercompany loans in three tranches across the price control periods ending March 2025 (AMP7) and ending March 2030 (AMP8): GBP400 million in FY24 (GBP100 million higher than agreed representing acceleration of commitment), GBP100 million in FY25 and the remaining GBP440 million in FY27.

Class B Deleveraging: We forecast YWS to maintain ample net debt to RCV headroom for the class B debt against our negative rating sensitivity of 82%, with strong cash and nominal PMICRs, on reduced class B debt, and comfortable headroom for class A debt. This may be positive for the class B debt rating if confirmed by AMP8 credit metrics.

Weaker, but Comfortable PMICRs Expected: About 60% of YWS's total debt is inflation-linked (IL), partly through swaps. While IL debt provides a hedge to RCV that grows with inflation over time, we expect the higher accretion on the IL debt and swaps to contribute to weak nominal post-maintenance interest coverage ratio (PMICR), reflecting overall cost of debt. However, we forecast average AMP7 class A nominal PMICR above our negative rating sensitivity of 1.7x.

We expect AMP7 average class A cash PMICR above our negative rating sensitivity of 1.4x, but regular accretion paydowns will weaken interest coverage towards the end of AMP7.

Totex Underperformance Expected: We expect YWS to underperform its total expenditure (totex) allowance by GBP340 million across AMP7, almost equally split between operating expenditure (opex) and capex underperformance. YWS is investing about GBP180 million (GBP80 million expected to be recovered through the cost-sharing mechanism) in combined storm overflows (CSO) to improve environmental outcomes and reduce penalties.

Ratings

Yorkshire Water Services Finance Limited

Senior Secured Debt – Long-Term Rating	A-

Click here for the full list of ratings

2035 Climate Vulnerability Signal: 14

Yorkshire Water Finance Plc

Senior Secured Debt - Long-Term Rating	A-
Subordinated Long-Term Rating	BBB-

Click here for the full list of ratings

2035 Climate Vulnerability Signal: 14

Applicable Criteria

Corporates Recovery Ratings and Instrument Ratings Criteria (October 2023)

Parent and Subsidiary Linkage Rating Criteria (June 2023)

Corporate Rating Criteria (November 2023)

Sector Navigators: Addendum to the Corporate Rating Criteria (November 2023)

Related Research

Global Corporates Macro and Sector Forecasts (June 2024)

UK Water - Relative Credit Analysis (June 2024)

Spotlight: UK Water Business Plans (October 2023)

What Investors Want to Know: UK Water Companies (April 2023)

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These investments, which are within our expectations, aim to meet a minimum 20% reduction in average number of discharges from CSOs by 2025 against the 2021 base year.

Subordinated Debt Rating: As YWF's class B debt is subordinated to class A debt and sizeable super-senior IL swap liabilities, we do not expect the recovery of class B debt to be above average in an event of default scenario and hence do not apply the one-notch sector-specific recovery uplift in the class B debt rating.

Reduced but Sizeable MTM Liability: YWS's negative mark-to-market (MTM) liability on IL swaps reduced to about GBP2 billion at FYE23 (about 23% of RCV) from about GBP3 billion (about 41% of RCV) from FYE22, mainly reflecting higher RPI and interest-rate expectations. Despite the reduction, YWS's exposure remains one of the largest in the UK water sector.

In our rating case, we do not assume crystallisation of the MTM liability nor do we adjust our debt to include it. The MTM liability would only crystallise in the event of a non-payment under the swaps, which we view as unlikely.

Swap Breaks Managed: YWS continues to proactively manage its IL swap breaks and accretion pay-downs. IL swap breaks due in 2023 have been extended by 5-17 years, and GBP177 million notional has been cancelled in 2024. Regular accretion paydowns avoid a documentary super-senior trigger event covenant of 6% RCV. If total accretion to notional value exceeds 6% of RCV, the amount above 6% would equal the accretion paydown.

Borrowing Through Swaps: Fitch treats re-couponing benefit funded through tenor extensions on out-of-money swaps as borrowing through swaps and adjusts its forecast net debt by the cumulative amount of the benefits received. Total debt adjustment amounts to about 2% of shadow RCV at FYE25.

Standalone Assessment under PSL: Fitch rates YWS on a standalone basis using the stronger subsidiary/weaker parent approach under its Parent and Subsidiary Linkage (PSL) Rating Criteria. This assessment reflects 'insulated' legal ring-fencing as underlined by a well-defined contractual framework, and tight financial controls imposed by Ofwat and designed to support YWS's financial profile. We view access and control as overall 'porous' as YWS operates with separate cash management and a mixture of external and intercompany funding.

Financial Summary

Yorkshire Water Services Limited	FY21	FY22	FY23	FY24F	FY25F
Class A net debt/RCV (%)	70.5	67.9	69.6	68.7	69.7
Total senior net debt/RCV (%)	78.4	74.5	73.4	71.9	72.8
Class A cash PMICR (x)	1.7	1.4	1.3	1.6	1.7
Senior cash PMICR (x) (class A & B)	1.5	1.3	1.2	1.5	1.6
Class A nominal PMICR (x)	1.6	1.5	1.7	2.7	2.2
Senior nominal PMICR (x) (class A & B)	1.5	1.4	1.6	2.6	2.0

F — Forecast
Source: Fitch Ratings, Fitch Solutions

Rating Derivation Relative to Peers

YWS's class A senior secured 'A-'/Stable rating reflects the highly geared nature of the company's secured covenanted structure, with gearing of about 70% at end of AMP7 compared with peer United Utilities Water Limited's (BBB+/Stable; senior unsecured debt: A-) lower gearing of about 66% (transition investments not fully reflected in shadow RCV), and its standard corporate structure. YWS's financing structure benefits from structural enhancements, including trigger mechanisms (such as class A dividend lock-up of 75%, senior gearing dividend lock-up of 85%, interest cover covenants) and debt-service reserve liquidity.

The non-participatory notes issued by YWSF are rated 'BBB+'/Stable, one notch lower than class A debt rating. The non-participatory note holders did not accept exchange for class A unwrapped bonds, and do not benefit from the YWS's share pledge. However, they benefit from other creditor protections and structural features of the overall covenant package from YWS and YWSF.

Rating Sensitivities

Factors that may, Individually or Collectively, Lead to Positive Rating Action/Upgrade

- Class A: adjusted net debt to RCV below 67%, cash and nominal PMICRs above 1.6x and 1.8x, respectively
- Class B: total senior adjusted net debt to RCV below 77%, total senior cash and nominal PMICRs above 1.3x and 1.6x, respectively, and substantial elimination of the negative MTM swap liability.

Factors that may, Individually or Collectively, Lead to Negative Rating Action/Downgrade

- Class A: adjusted net debt to RCV above 72%, cash and nominal PMICRs below 1.4x and 1.7x, respectively
- Class B: total senior adjusted net debt to RCV above 82%, total senior cash and nominal PMICRs below 1.2x and 1.5x, respectively

Liquidity and Debt Structure

Adequate Liquidity: As at FYE23, YWS held approximately GBP294 million in unrestricted cash and cash equivalents, alongside an undrawn committed revolving credit facility (RCF) of GBP560 million. In FY24, the RCF was increased to GBP630 million, with a potential to upsize by an additional GBP30 million. This RCF matures in November 2028 and includes a one-year extension option. Additionally, YWS has access to a bilateral RCF of GBP80 million maturing in July 2027, with two one-year extension option.

In addition, YWS benefits from a designated debt service reserve liquidity facility of GBP170 million (committed undrawn) increased to GBP182 million in March 2023, sized to cover 12 months of interest payments (including hedge payments), together with a committed undrawn operating and maintenance reserve facility of GBP90 million, increased to GBP120 million in March 2023 – both only available upon trigger event.

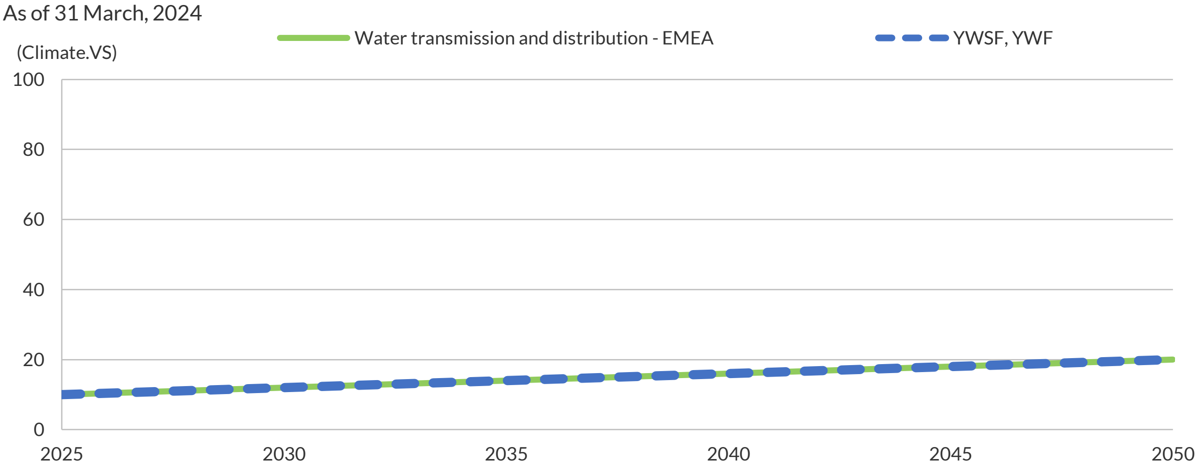
Climate Vulnerability Considerations

Fitch uses Climate Vulnerability Signals (Climate.VS) as a screening tool to identify sectors and Fitch-rated issuers that are potentially most exposed to credit-relevant climate transition risks and, therefore, require additional consideration of these risks in rating reviews. Climate.VS range from 0 (lowest risk) to 100 (highest risk). For more information on Climate.VS, see Fitch's Corporate Rating Criteria.

The FYE24 revenue-weighted Climate Vulnerability Signal for YWSF and YWSF for 2035 is 14 out of 100, suggesting low exposure to climate-related risks in that year. This is line with sector average signal of the water/wastewater utility sector.

Climate.VS Evolution

As of 31 March, 2024



Source: Fitch Ratings

Liquidity and Debt Maturities

Yorkshire Water Services Limited

Liquidity Analysis (GBPm)	FY24F	FY25F
Available liquidity		
Beginning cash balance	294	-186
Rating case FCF after acquisitions and divestitures	-331	-251
Total available liquidity (A)	**-37**	**-437**
Liquidity uses		
Debt maturities	-149	0
Total liquidity uses (B)	**-149**	**0**
Liquidity calculation		
Ending cash balance (A+B)	-186	-437
Revolver availability	710	710
Ending liquidity	**524**	**273**
Liquidity score (x)	4.5	Not meaningful

F – Forecast
Source: Fitch Ratings, Fitch Solutions, Yorkshire Water Services Limited

Scheduled debt maturities (GBPm)	2023
2024	149
2025	0
2026	0
2027	302
2028	145
Thereafter	6,120
Total	**6,716**

Source: Fitch Ratings, Fitch Solutions, Yorkshire Water Services Limited

Key Assumptions

Fitch's Key Assumptions Within Our Rating Case for the Issuer

- Ofwat's final determination financial model (after the Competition and Markets Authority outcome) is used as a main information source.
- Allowed wholesale weighted average cost of capital (WACC) of 2.12% (RPI-based) and 3.12% (CPIH-based) in real terms.
- Fifty percent of RCV is RPI-linked and another 50% plus capital additions is CPIH-linked, since FY21.
- RPI of 8% for FY24 and 3.9% for FY25.
- CPIH of 6% in FY24 and 2.8% in FY25.
- Fitch case assumes totex underperformance of about GBP340 million across AMP7.

Financial Data

Yorkshire Water Services Limited

(GBPm)	2021	2022	2023	2024F	2025F	2026F
Summary income statement						
Gross revenue	1,101	1,119	1,145	1,298	1,342	1,388
Revenue growth (%)	3.5	1.6	2.3	13.4	3.4	3.4
EBITDA before income from associates	565	576	577	605	629	651
EBITDA margin (%)	51.3	51.5	50.4	46.6	46.9	46.9
EBITDA after associates and minorities	565	576	577	605	629	651
EBITDAR	565	576	577	605	629	651
EBITDAR margin (%)	51.3	51.5	50.4	46.6	46.9	46.9
EBIT	241	242	237	212	228	224
EBIT margin (%)	21.9	21.7	20.7	16.3	17.0	16.1
Gross interest expense	-167	-174	-215	—	—	—
Pretax income including associate income/loss	18	-353	723	280	282	238
Summary balance sheet						
Readily available cash and equivalents	198	29	294	29	29	80
Debt	5,704	5,798	6,716	6,642	6,857	6,673
Lease-adjusted debt	5,704	5,798	6,716	6,642	6,857	6,673
Net debt	5,506	5,770	6,422	6,614	6,829	6,593
Summary cash flow statement						
EBITDA	565	576	577	605	629	651
Cash interest paid	-146	-160	-164	-135	-141	—
Cash tax	-14	-15	-4	-2	-20	—
Dividends received less dividends paid to minorities (inflow/outflow)	—	—	—	—	—	—
Other items before FFO	-4	-4	-21	—	—	—
FFO	446	437	414	522	508	651
FFO margin (%)	40.5	39.1	36.2	40.2	37.8	46.9
Change in working capital	32	18	34	—	—	-0
CFO (Fitch-defined)	478	455	448	522	508	650
Total non-operating/nonrecurring cash flow	-15	—	—	—	—	—
Capex	-447	-384	-507	—	—	—
Capital intensity (capex/revenue) (%)	40.6	34.3	44.3	—	—	—
Common dividends	-45	-53	-62	—	—	—
FCF	-30	19	-121	—	—	—
FCF margin (%)	-2.8	1.7	-10.6	—	—	—
Net acquisitions and divestitures	—	—	—	—	—	—
Other investing and financing cash flow items	4	—	6	—	—	—
Net debt proceeds	-64	-189	341	264	215	—
Net equity proceeds	—	—	—	—	—	—
Total change in cash	-90	-170	226	—	—	51
Leverage ratios (x)						
Class A net debt/RCV (%)	70.5	67.9	69.6	68.7	69.7	70.5
Total senior net debt/RCV (%)	78.4	74.5	73.4	71.9	72.8	78.4
EBITDA leverage	10.1	10.1	11.6	11.0	10.9	10.3
EBITDA net leverage	9.8	10.0	11.1	10.9	10.9	10.1
EBITDAR leverage	10.1	10.1	11.6	11.0	10.9	10.3
EBITDAR net leverage	9.8	10.0	11.1	10.9	10.9	10.1

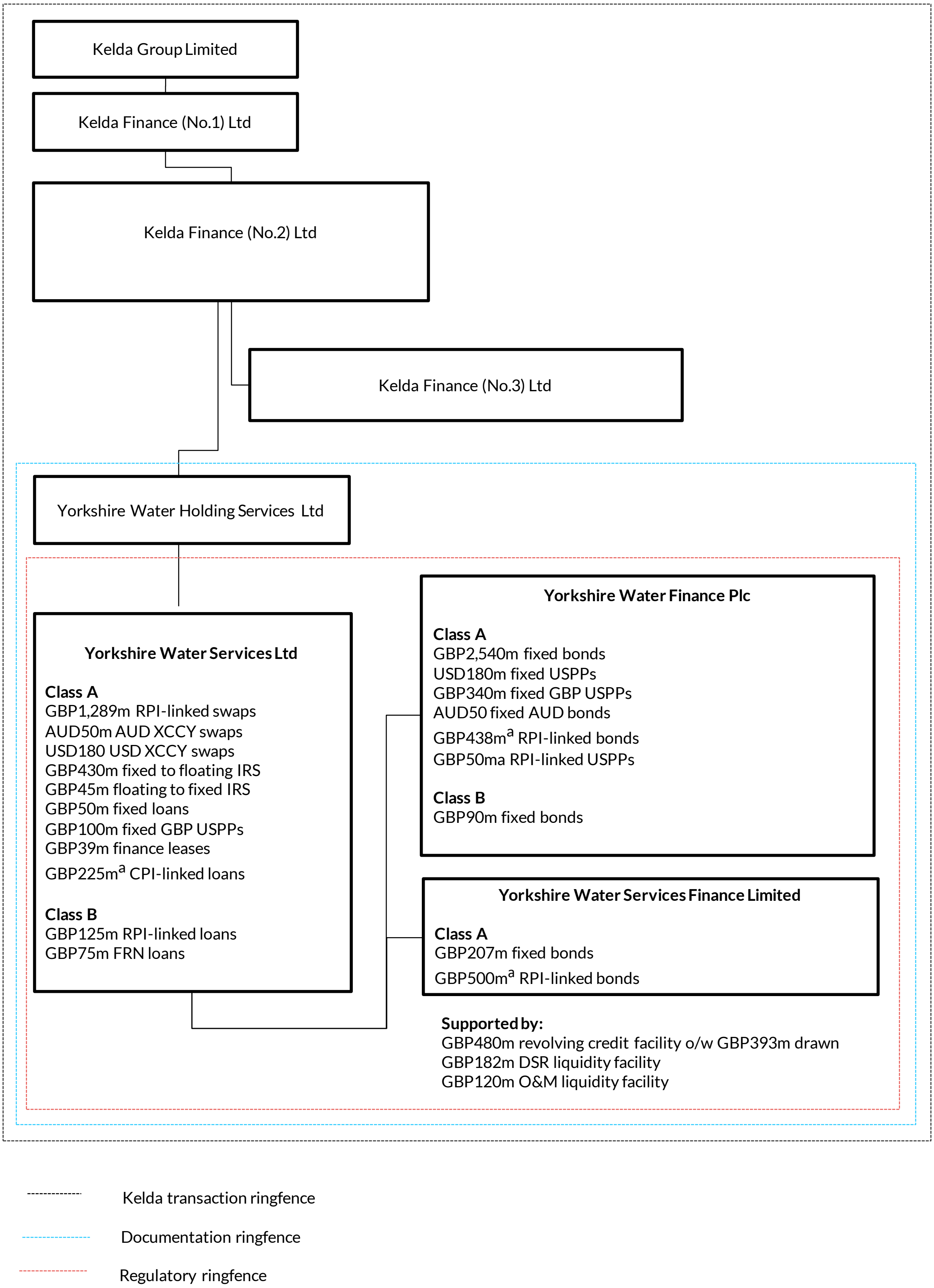
(GBPm)	2021	2022	2023	2024F	2025F	2026F
FFO adjusted leverage	10.4	10.4	12.2	11.0	11.3	10.3
FFO adjusted net leverage	—	—	—	11.0	11.2	10.1
FFO leverage	10.4	10.4	12.2	11.0	11.3	10.3
FFO net leverage	—	—	—	11.0	11.2	10.1
Calculations for forecast publication						
Capex, dividends, acquisitions and other items before FCF	-508	-436	-569	-853	-759	-599
FCF after acquisitions and divestitures	-30	19	-121	-331	-251	51
FCF margin after net acquisitions (%)	-2.8	1.7	-10.6	-25.5	-18.7	3.7
Coverage ratios (x)						
Class A cash PMICR (x)	1.7	1.4	1.3	1.6	1.7	1.7
Senior cash PMICR (x) (class A & B)	1.5	1.3	1.2	1.5	1.6	1.5
Class A nominal PMICR (x)	1.6	1.5	1.7	2.7	2.2	1.6
Senior nominal PMICR (x) (class A & B)	1.5	1.4	1.6	2.6	2.0	1.5
FFO interest coverage	3.7	3.5	3.4	4.5	4.3	—
FFO fixed-charge coverage	3.7	3.5	3.4	4.5	4.3	—
EBITDAR fixed-charge coverage	3.9	3.6	3.5	4.5	4.5	—
EBITDAR net fixed-charge coverage	5.6	4.8	4.2	7.4	6.2	—
EBITDA interest coverage	3.9	3.6	3.5	4.5	4.5	—
Additional metrics (%)						
CFO-capex/debt	0.5	1.2	-0.9	-3.0	-1.0	0.8
CFO-capex/net debt	0.5	1.2	-0.9	-3.0	-1.0	0.8
CFO/capex	106.8	118.6	88.4	72.6	87.7	108.6

CFO – Cash flow from operations
Source: Fitch Ratings, Fitch Solutions

How to Interpret the Forecast Presented

The forecast presented above is based on Fitch Ratings' internally produced, conservative rating case forecast. It does not represent the forecast of the rated issuer. The forecast set out above is only one component used by Fitch Ratings to assign a rating or determine a rating outlook, and the information in the forecast reflects material but not exhaustive elements of Fitch Ratings' rating assumptions for the issuer's financial performance. As such, it cannot be used to establish a rating, and it should not be relied on for that purpose. Fitch Ratings' forecasts are constructed using a proprietary internal forecasting tool, which employs Fitch Ratings' own assumptions on operating and financial performance that may not reflect the assumptions that you would make. Fitch Ratings' own definitions of financial terms such as EBITDA, debt or free cash flow may differ from your own such definitions. Fitch Ratings may be granted access, from time to time, to confidential information on certain elements of the issuer's forward planning. Certain elements of such information may be omitted from this forecast, even where they are included in Fitch Ratings' own internal deliberations, where Fitch Ratings, at its sole discretion, considers the data may be potentially sensitive in a commercial, legal or regulatory context. The forecast (as with the entirety of this report) is produced strictly subject to the disclaimers set out at the end of this report. Fitch Ratings may update the forecast in future reports but assumes no responsibility to do so. Original financial statement data for historical periods is processed by Fitch Solutions on behalf of Fitch Ratings. Key financial adjustments and all financial forecasts credited to Fitch Ratings are generated by rating agency staff.

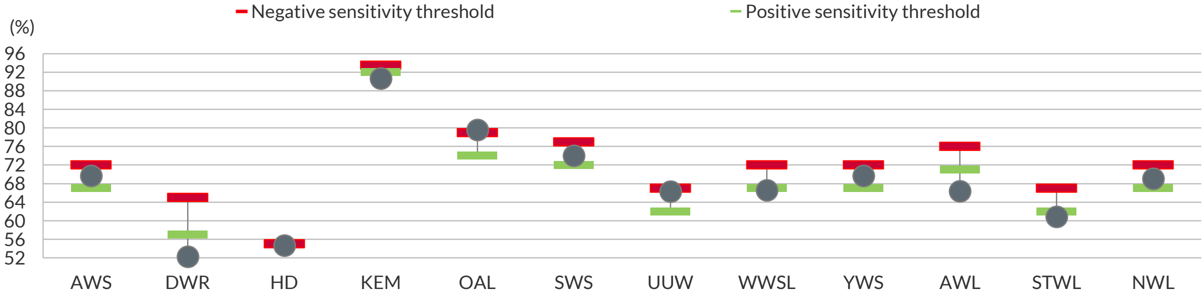
Simplified Group Structure Diagram



[a] Outstanding at time of issue
Source: Fitch Ratings, Fitch Solutions, Yorkshire Water Services, as of March 2023

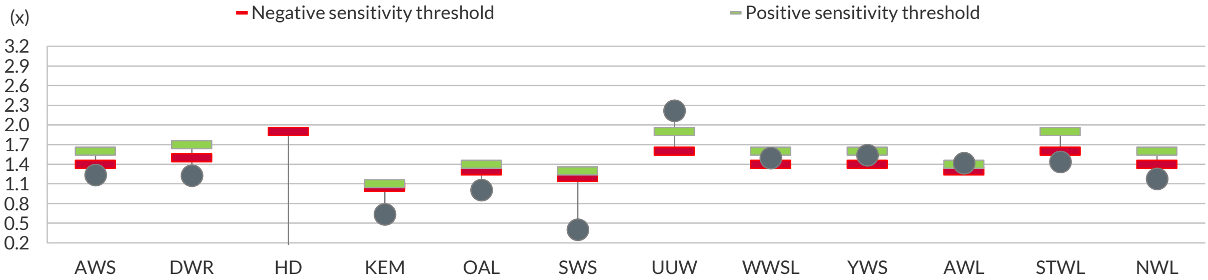
Peer Financial Summary

Rating Headroom by Gearing (FY25)



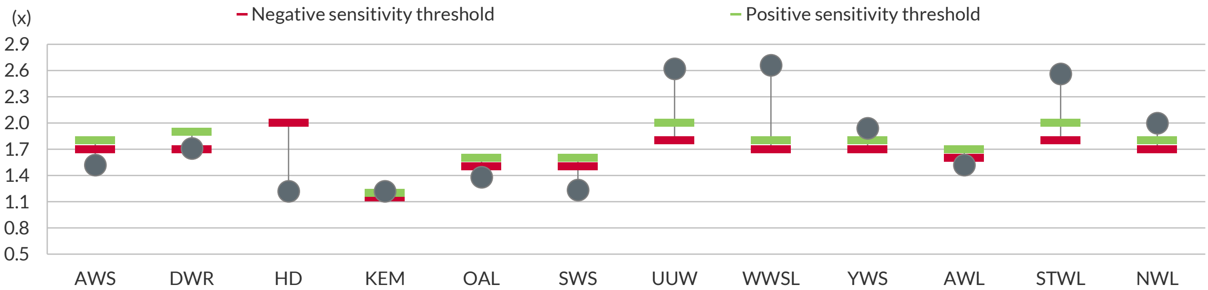
Ratios for DWR, SWS, YWS and reflect senior class A debt. Kemble sensitivities at 'B' before the downgrade to 'RD'.
Source: Fitch Ratings, Fitch Solutions , companies' data

Rating Headroom by Cash PMICR (Five-Year Average)



Ratios for DWR, YWS and AWL reflect senior class A interest. Kemble sensitivities at 'B' before the downgrade to 'RD
Source: Fitch Ratings, Fitch Solutions, companies' data

Rating Headroom by Nominal PMICR (Five-Year Average)



Ratios for DWR,YWS and AWL reflect senior class A interest. Kemble sensitvities at 'B' before the downgrade to 'RD'.
Source: Fitch Ratings, Fitch Solutions , companies' data

Key	
AWS	Anglian Water Services Limited
DWR	Dwr Cymru (Financing) UK Ltd
HD	Hafren Dyfrdwy
KEM	Kemble Water Finance Limited
OAL	Osprey Acquisitions Limited
SWS	Southern Water Services Limited
UUW	United Utilities Water Limited
WWSL	Wessex Water Services Limited
YWS	Yorkshire Water Services Limited
AWL	Affinity Water Limited
STWL	Severn Trent Water Limited
NWL	Northumbrian Water Limited

Source: Fitch Ratings

Fitch Adjusted Financials

Reconciliation of Key Financial Metrics for Yorkshire Water Services Ltd

(GBPm)	31 Mar 23
Interest bearing loans and borrowings class A and class B debt	6,598
- Cash and equivalents	294
= Net debt	6,304
+ Swap re-couponing adjustment	118
= Adjusted net debt class A and class B (a)	**6,422**
Economic regulatory asset value (b)	**8,751**
Net debt/RAV class A and class B (%)	**73.4**
Pension adjusted net debt/regulatory asset value(a/b)	
Operating EBITDA	577
- Regulatory depreciation	-331
- Taxation paid	-4
- Pension deficit	-
Post maintenance cash flow = EBITDA - regulatory depreciation - pension deficit (c)	**242**
Class A and class B cash interest (d)	**164**
50% accretion on IL swaps with 5-year APDs (e)	42
Post maintenance interest cover ratio class A and class B (x)	**1.2**
Post maintenance cash flow (c)	242
RCV indexation (f)	854
Total senior interest (g)	666
Nominal post-maintenance interest coverage ((c)+(f))/(g) (x)	**1.6**

Source: Fitch Ratings, based on company accounts and investor reports

Parent Subsidiary Linkage Analysis

Key Risk Factors and Notching Approach

Parent	Kelda Group Limited
Parent LT IDR	n.a.
Subsidiary	Yorkshire Water Services Limited
Subsidiary LT IDR	n.a.
Path	Stronger Subsidiary
Legal ring-fencing	Insulated
Access and control	Porous
Notching matrix outcome	Standalone
Override applied	No
Notching approach	—

LT IDR – Long-Term Issuer Default Rating
Source: Fitch Ratings

Stronger Subsidiary Notching Matrix

Access and control	Open	Porous	Insulated
With open ring-fencing	Consolidated	Consolidated+1	Consolidated+2[b]
With porous ring-fencing	Consolidated+1	Consolidated+2[b]	Consolidated+2[b]
With insulated ring-fencing	[a]	Standalone	Standalone

[a] It is unlikely that considerations for "insulated" legal ring-fencing would coexist with the conditions outlined under "open" for access and control. It is more likely that other factors relevant to legal ring-fencing or access and control, but not within this table, would move either one, or both, of the individual Linkage Factor Assessments (LFAs) to a "porous" level that would lead to a consolidated+1, consolidated+2 or standalone outcome.
[b] Notching is capped at the subsidiary's Standalone Credit Profile.
Source: Fitch Ratings

SOLICITATION & PARTICIPATION STATUS

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For information on the participation status in the rating process of an issuer listed in this report, please refer to the most recent rating action commentary for the relevant issuer, available on the Fitch Ratings website.

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