

# Investors Report

For the 12 months ending 31 March 2018

South East Water Financing Group:  
South East Water (Holdings) Limited  
South East Water Limited  
South East Water (Finance) Limited

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# General overview and business update

This Investors Report covers the twelve month period ending 31 March 2018. It also includes a summary of any subsequent material events in the period prior to the publication of this report.

## 1. Operational performance

The operations team works hard 24 hours a day, seven days a week to maintain our extensive network of underground pipes while also finding and fixing more than 30,000 leaks and bursts.

This year has been a particularly testing time for the operational teams as fluctuating winter temperatures and the dry autumn/winter caused ground movements. Despite this the number of burst water mains reduced from 3,032 in 2016/17 to 2,747.

In March 2018 we experienced a severe operational challenge caused by the “Beast from the East” (several days of freezing temperatures, high winds and significant snowfall), followed by a very rapid thaw. This led to a break out of burst pipes across the network at a scale we have never witnessed in our area, with around 70 per cent of the leaks on customer private plumbing. A dedicated team worked around the clock to get water supplies restored to around 20,000 properties, while distributing large volumes of bottled water to the public, focusing on vulnerable customers, and ensuring temporary supplies for livestock at affected farms. A major effort was made in communicating up-to-date information to our customers through our website, social media, TV and radio etc. We have now written to all customers impacted to apologise for the disruption and credited their account with above statutory compensation in recognition of the inconvenience that was caused. Our liaison with our local resilience forum made an important difference during the event.

We worked hard to reduce the length of any interruptions to supply from these bursts and had set ourselves a target for the year of an average interruption time of 12 minutes per property per year. During the period April 2017 to February 2018 we had met this target and were tracking at 5.6 minutes. Then at the end of February freezing temperatures hit our region and led to us missing the target with a final interruptions score of 44.6 minutes per property for the year. We can see the impact changing weather can make, not just to our customers’ properties, but also to our network and we need to ensure this is robust to these changing patterns.

The team had done a lot to prepare for the impact of the freeze and thaw on our network, and those bursts that occurred on our pipes were quickly identified and repaired. But the speed and scale of the upsurge in demand following the rapid thaw, due primarily to leaks on customer properties, is something we’ve never experienced before. That said we recognise that we must learn from the experience to identify opportunities to minimise the impact of such a severe incident in the future including what more we can do to proactively support customers so they can better protect their own properties’ pipes – in fact customers being part of the resilience solution will be a key part of our next five year business plan. Ofwat has completed its own review into the impact of the freeze/thaw across the whole country and the lessons to be learned therefrom. We will work closely with the industry to ensure best practice approaches are built into our emergency plans for future events.



We began the year with our non-household retail business, South East Water Choice operating within our supply region and the company had a good first year of trading. At the same time, Water Choice, owned by another company within our group of companies, Invicta Water Ltd, was offering water and wastewater retail services to all non-household customers across England. In April 2018 we transitioned South East Water Choice across to become one business owned by Invicta Water.

Invicta Water has subsequently sold the business to Castle Water with the completion of the sale on 1 July 2018. Castle Water has the scale and experience to build on the progress Water Choice has made since the market opened. South East Water is committed to providing an excellent wholesale service to all business retailers. We have worked closely with both Castle Water and Invicta Water during this period to ensure a smooth transition.

## 2. Water resources and leakage

During 2017/18 we received 98 per cent of the long term average rainfall across our supply area. This rainfall was especially welcome after a year of low rainfall during the critical autumn and winter recharge periods in 2016/17.

The rainfall during this winter period was above long term average levels and supported a stronger recovery of our water resources ahead of summer 2018. At the end of March 2018 groundwater levels recovered close to normal levels which means as we move into the summer our water resources are in a good position.

Average demand for 2017/18 was 517 Ml/d (slightly lower than last year's figure of 521 Ml/d) and slightly below the expected demand. Weather conditions during the summer 2017 were close to expected average normal year conditions, although during June we saw a period of high demand that coincided with a good spell of notably warm and sunny weather.

We have made good progress with our water efficiency strategy agreed with the regulator. Leakage levels continue to be maintained below the leakage target. Good progress is continuing with the planning of new water resource schemes required to maintain the supply demand balance during the period 2015 to 2020.

We published our draft 2019 water resources management plan in February 2018, for a 12 week consultation that ended on the 21 May 2018. We actively engaged with customers, regulators, key stakeholders, third parties and neighbouring water companies on the draft plan. We are now preparing a response to representations received on our draft plan and will submit a revised draft plan to Defra for their approval.

### 3. Customer service

Following our agreement with Southern Water earlier in the year, we have completed a project to jointly-bill around 500,000 customers, where we provide the water supply, and Southern Water provide the sewerage services. This mirrors the One Bill service we have provided for our shared Thames Water customers for some years. The project has been managed by our in-house IT and operations teams, with overall delivery exceeding all key customer performance indicators, while being managed within timescales and budget.

Our focus on delivering our five-out-of-five customer experience to every customer continues, through a full choice of contact channels – face to face, telephone, written, self-serve, web, email or social media. Our aim is to ensure that, whichever route they choose, customers get a consistently great service. This has helped our overall customer service performance, measured by the Service Incentive Mechanism (SIM), improve again this year to 85.6, and we are now above the industry average for our qualitative experience scores for our combined billing and water performance. During the year, we saw a small increase in written complaints from customers, the first such increase in six years, and predominantly caused by two events: the major freeze thaw event in March; and bill queries linked to the changes from the One Bill project. We are confident that with the account migrations now finished, we will see a return to falling complaint volumes.

Our focus on great service experience continues to support efficient operational performance, as measured through our cost to serve. We have continued to absorb the increased costs arising from a metered customer base that has risen to 86 per cent of households, as our customer metering programme approaches completion. We have also maintained our particularly strong cash collection performance, and have again reduced debt for outstanding charges over 12 months old, by over £1m within the year.

Our commitment to a five-out-of-five customer experience applies to every customer. Our approach to ensuring customers in vulnerable circumstances are also able access our services has seen growing numbers of customers register on our Priority Services Register (PSR). In addition to providing additional support to customers during supply interruptions such as during the March freeze, we are also supporting greater numbers of customers who may struggle with their water charges through our social tariff, with over 16,500 customers now benefiting from a discount on their water charges of 30 to 40 per cent. Building on our success in this area is one of the key elements within our price review submission (PR19).

#### 4. Health, safety and environment

The health, safety and wellbeing strategy Thrive 365! continues to progress well. The strategy is focused on eight safety goals and two key themes, safe people and safe working. Actions and projects that form a part of Thrive 365! are being implemented throughout the business. An external consultant has completed compliance audits for the operational departments; their final report supported the initiatives underway as part of Thrive 365!

The leakage and metering teams, and associated contractors, held a health and safety conference. The theme of the conference was 'Your Choice' and key topics included mobile phone use, dust inhalation and mental health.

A joint emergency exercise was held with the fire and rescue services at one of our major treatment works and a programme of smaller emergency drills were held throughout the business to ensure that all technicians were familiar with, and assessed against, the emergency plans for dealing with toxic gas escapes.

Unfortunately South East Water experienced two accidents reportable under RIDDOR during 2017/18; one slip on ice at a customer's premises and one manual strain when opening a gate. Overall performance remains positive.

#### 5. Financial performance in the 12 months ended 31 March 2018

The ring fenced South East Water Group includes the following companies:

*South East Water (Holdings) Limited ("SEWH")*

*South East Water Limited ("SEWL")*

*South East Water (Finance) Limited ("SEWF")*

SEWF is a 100 per cent owned subsidiary of SEWL and SEWL is a 100 per cent owned subsidiary of SEWH.

The accounts for the South East Water Group for the twelve months to 31 March 2018 have been prepared and these results are set out in the appendix. These accounts have been prepared under International Financial Reporting standards ("IFRS"); they are not published, but are prepared for internal use. The consolidated group accounts for SEWL, including SEWF but excluding SEWH, for the same twelve month period are published on the South East Water corporate website.

The entity accounts for SEWL are also prepared under IFRS. The entity accounts for SEWH and SEWF are prepared under FRS 101, taking advantage of the disclosure exemptions available under this standard.

##### Turnover

Turnover for the year to 31 March 2018 was slightly higher at £224.8m when compared to £218.9m for the previous year. The increased revenue is largely due to increased prices averaging five per cent for the year and the numbers of new properties in the area, offset by the impact of metering, where customers switch from unmeasured to measured supply.

## Operating costs

Net operating costs for the 12 months to 31 March 2018 were £159.0m compared to £147.4m in the prior year. The increase in costs of £11.6 million includes the additional costs in relation to the extreme weather incident in March 2018 of £2.1 million, increases in depreciation of £3.2 million in respect of new fixed assets introduced to operations and a £2.2 million increase in rates charges following the review by central government. Additionally, we have seen other operational and inflationary pressures on our costs, particularly with respect to employee costs.

## Interest

Interest payable for the group for the year to 31 March 2018 was £61.2m compared to £64.1m in the prior year. The reduction in interest payable is due to the significantly lower movement in the fair value of the interest rate swap in the year. This is offset by an increase in indexation on the index linked loans and bonds due to the higher level of inflation.

Interest payable includes the following:

- *£22.3m interest on listed debt/bonds (2017: £22.0m)*
- *£3.3m fair value movement on interest rate swap (2017: £13.7m)*
- *£5.7 indexation on index linked listed bonds (2017: £4.3m)*
- *£11.8m interest on Index linked loans (including Artesian Finance loans) (2017: £11.4m)*
- *£12.6m Indexation on Index linked loans (including Artesian Finance loans) (2017: £7.3m)*
- *£5.2m interest payable by SEWH to group companies (2017: £5.3m)*
- *£2.4m relating to other interest payable (2017: £2.4m)*
- *£(2.1)m capitalised interest (2017: £(2.3)m)*

## Taxation

The income statement shows a tax charge of £5.7m (2016: credit of £3.8m). The tax credit in the prior year was due to the effect of changes in future rates of tax on deferred tax. There have been no changes to tax rates in the current year. The current tax charge includes the utilisation of and payment for other group losses.

## Cash

The South East Water Group has cash and cash equivalent balances of £6.6m as at 31 March 2018 compared with £11.4m as at 31 March 2017. During the period £20.0m has been drawn down from the authorised credit facilities to fund the continuing capital programme.

The restricted cash balance as at 31 March 2018 was £0.3m compared to £0.7m as at 31 March 2017. This is held in designated bank accounts in order to meet interest and associated swap payments falling due in respect of the listed debt and interest payments on index linked loans.

## Debt funding

There has been no new debt funding in the period except the £20.0m drawn down from authorised credit facilities mentioned above.

## 6. Regulatory update

### Regulatory reporting

The 2017/18 Annual Report and Financial Statements which includes the Statutory Accounts, the Regulatory Accounts, the Ofwat prescribed Performance Report and the Risk and Compliance Statement has been published on our website.

In addition, we have also published on our website our Performance, People and Planet Report which gives further information about our performance against our agreed outcomes.

In 2017/18, our leakage team has detected a record number of leaks (1,300 higher than 2016/17). We know that customers expect to see us playing our part before we ask them to save water, which is why our leakage team has again strived to reduce leakage further than our target. Our increased investment in data loggers in the past two years has enabled us to detect more invisible leaks.

The changeable weather during the winter put particular pressure on our distribution teams as they managed the impact of

the various freeze/thaws on the network.

In March it was the speed of the thaw, and in particular the bursts and leaks on customers' private supply pipes and plumbing that drove a rapid increase in demand over a period of one day, which we have not witnessed before. This emptied a number of our service reservoirs and caused disruption to customers' supplies. This event contributed 37.8 minutes in total to our interruptions performance.

Outcome	FD Target	Performance	Reward / penalty if applicable	£m (if applicable)
Customer satisfaction				
A1. Appearance	4.6	4.5	No penalty	-
B1. Taste	4.3	4.2	No penalty	-
C1. Leakage	4.0	3.8	Penalty	-0.037
C1. Leakage	4.5	4.3	Penalty	-0.008
F1. Pressure	4.5	4.3	Penalty	-0.027
G1. Interruptions	4.7	4.6	No penalty	
H1. Water restrictions	4.1	4.4	Reward	0.048
C2. Leakage	90.0	87.7	Reward	0.189
D2. SIM score	N/A	85.6	N/A	N/A
E1. Customers consider bills to be value for money and affordable	N/A	71%	N/A	N/A
F2. Number of properties at risk of low pressure	60	47	Reward	0.004
G2. Average interruption time lost per property	12.0	44.6	Penalty	-1.331
H2. Meeting the water resource deficit	0	0	No penalty	N/A
I1. Mean zonal compliance	100	99.95	No penalty	N/A
J1. Number of breaches of abstraction licences, discharge consents and environmental permits	0	215	N/A	N/A
J2. Number of pollution incidents (Category 1-2)	0	1	N/A	N/A
K1. Number of compliance breaches of legislation	0	0	N/A	N/A
L1. Number of breaches of national security obligations	0	0	N/A	N/A
M1. Number of compliance breaches of other statutory obligations and licence conditions	0	0	N/A	N/A
N1. Discolouration contacts	0.58	0.82	Penalty	-0.358
N2. Above ground asset performance	Stable	Stable	No penalty	N/A
N3. Number of sites at risk of flooding	N/A	7	N/A	N/A
N4. Water mains bursts	2429	2747	No penalty	N/A
O1. KG of carbon emissions per customer per year	N/A	37.2	N/A	N/A
O2. We will monitor our abstractions at low flows at environmentally sensitive sites	N/A	-0.24	N/A	N/A



## 2020 to 2025 Price Review

In December 2017 Ofwat published the final methodology for PR19 which can be found using the following link:

[www.ofwat.gov.uk/regulated-companies/price-review/2019-price-review-final-methodology/](http://www.ofwat.gov.uk/regulated-companies/price-review/2019-price-review-final-methodology/)

In addition to the final methodology Ofwat published a further consultation entitled 'putting the sector back in balance' in April. The conclusion of this consultation can be found here:

[www.ofwat.gov.uk/publication/putting-sector-back-balance-summary-ofwats-decision-issues-pr19-business-plans/](http://www.ofwat.gov.uk/publication/putting-sector-back-balance-summary-ofwats-decision-issues-pr19-business-plans/)

We remain engaged with Ofwat and play an active role in industry workshops in relation to PR19 and we responded to the additional consultation highlighting areas of concern with the proposals.

The extensive customer research programme for PR19 is nearing completion and is now in the final stages of acceptability testing with customers. This programme of activity not only introduces a range of innovative research techniques but also brings together the learnings from daily interactions with customers and insight from research undertaken by other companies and industries.

## Tariffs

In line with guidance issued by Ofwat we published charges for 2018/19 which can be found using the following link:

[corporate.southeastwater.co.uk/news-info/publications/our-charges](http://corporate.southeastwater.co.uk/news-info/publications/our-charges)

## Instrument of appointment

On 27 March 2017, Ofwat introduced a new Condition S dealing with the possible introduction of water into an undertaker's supply system under the revised water supply licensing regime from 1 April 2017. It also modified Condition R deleting paragraph 1 to 4 of that condition containing provisions on access codes that are now part of the new Condition S.

Following consultation in November / December 2016, on proposed modifications required to enable Ofwat's approach for the next price review referred to as Water 2020, Ofwat modified the instruments of appointment of all companies on 6 April 2017. This gave effect from 15 April 2017 to changes to (i) Condition B in order to introduce separate wholesale price controls for "Water Resources" and for "Network Plus Water", (ii) Condition B in order to allow in-period reward or penalty adjustments in respect of outcome delivery incentives, (iii) Conditions A, B and K to replace the definition of "Retail Price Index" with "Relevant Index" allowing for the use of either CPI or CPI(H) rather than RPI for regulatory indexation, and (iv) a new Condition M1 (Information Remedies) requiring companies to make specified information available to specified third parties to support the development and operation of a market in the provision, management and development of water resources, demand management or leakage services.

On 19 October 2017 Ofwat amended Condition C of the instrument of appointment of all water and sewerage companies with effect from 20 October 2017 using powers under section 55 of the Water Act 2014. This modification was made in order to allow for the implementation of a new charging methodology for new connections and more specifically for setting infrastructure charges as set out in charging rules for new connections services that will come into effect on 1 April 2018. The modification provides that provisions which limit the amount of infrastructure charges will cease to have effect on 1 April 2018 subject to certain transitional provisions.

On 8 December 2017 Ofwat circulated a range of proposed licence amendments developed in collaboration with the water industry as part of a licence simplification project requesting companies to notify their consent in principle to the changes.

This phase of the project covered conditions:

- *D Charges Schemes*
- *E undue discrimination*
- *F as it relates to accounting information*
- *G code of practice for customers and relations with CCWater*
- *H code of practice and procedure on debt recovery*
- *I code of practice and procedure on leakage*
- *J levels of service and service targets*
- *L underground asset management plans*
- *M provision of information*
- *N licence fees*
- *O replacement appointment*
- *Q interruptions in supply because of drought*

We notified our agreement in principle to the changes on 1 February 2018. The implementation of the changes will require a further formal consultation by Ofwat.

On 14 February 2018 and 18 June 2018 Ofwat circulated drafts of two new licence conditions. The first relating to the prohibition of undue preference or undue discrimination being shown to inset appointees (water undertakers that may be appointed instead of the Company usually for supplies to a new development site), self-lay providers and entities that may submit bids for the provisions of water resources, demand management or leakage services as introduced in the new Condition M1 referred to above. The second imposing obligations to maintain confidentiality and to control the use and dissemination of the information provided by these third parties to water companies. On 18 June 2018 Ofwat also asked companies to provide an indicative consent to the new conditions and we responded that we agreed in principle to the inclusion of conditions for the intended purposes but submitted specific comments on how to improve the draft conditions that had been circulated.

## 7. Capital expenditure

South East Water's Final Determination (FD) capital expenditure for 2015 to 2020 is £488.1m (2017/18 price base). Net capital investment for 2017/18, the third year of the AMP6 five year programme, is £80.1m. Cumulative spend in this regulatory period is £227.0m.

2017/18 expenditure:

- *£34.7m (43%) of investment has been made in the development of new assets and the enhancement of existing assets, including £30.3m for the management of the supply demand balance and £4.4m to meet the company's legal undertakings with respect to drinking water quality standards*
- *£13.4m (17%) of investment has been made in the maintenance of our below ground assets. This investment is essential to maintain the performance of the mains network and maintain a stable level of service, thus preventing a rise in disruption to customers with the associated water quality and leakage issues. Investment in the period has been predominantly in the following key areas:*
  - *mains renewal programme*
  - *reactive mains burst repairs*
  - *reactive communication pipe and stop tap repairs and replacements*
- *£32.0m (40%) of investment has been made in the maintenance of our above ground assets. Again, this investment is essential in maintaining a stable level of service to our customers and has been targeted in the following key areas:*
  - *resource facilities*
  - *treatment works maintenance*
  - *service reservoirs and water towers*
  - *pumping stations*
  - *management and general spend such as IT infrastructure*

## 8. Water quality

Ensuring we continue to improve the quality of the water we supply is a key priority. Each year the Chief Inspector of the Drinking Water Inspectorate publishes a report summarising drinking water quality in England and Wales which includes a number of comparative compliance indices.

Our overall drinking water quality performance, as measured using the DWI's key performance indicator at the customer's tap "mean zonal compliance" is in line with our performance commitment at 99.95 per cent. A further indication of the high performance standards of our water treatment works is provided by the treatment process control index which was again maintained at 100.00 per cent and the disinfection index which improved on 2016 performance to 99.99 per cent. Performance against other water quality indices has been maintained at the high level demonstrated throughout 2016, with the exception of the reservoir integrity index which has dropped slightly to 99.94 per cent. These results are based on 195,587 tests measured against EU and UK mandatory standards.

In addition to these regulatory tests we carried out over 400,000 operational tests to ensure that our assets consistently performed to deliver excellent quality water to our customers.

## 9. Outsourcing

South East Water continues to deliver a competitive tendering/outsourcing programme using a number of standard tools including:

- *call for competition (OJEU)*
- *request for Information (RFI) and pre-qualification of potential vendors*
- *use of Achilles Utility Vendor Database (industry specific supplier database & qualification system)*
- *Invitation to tender*
- *contract negotiation*

All procurement activities are compliant with relevant laws and undertakings including EU Utilities Contracts Regulations and the Outsourcing Policy of the Common Terms Agreement.

Contracts awarded, extended and/or signed (during last 12 months) include:

Supplier	Description	Contract value
Elior	Canteen services	£450,000
Industrial Chemicals Limited	Supply of chemicals	£6,400,000
Brenntag	Supply of chemicals	£800,000
Stonbury	Reservoir cleaning of remedial works	£12,800,000
Hydrosave	Leakage detection services	£4,000,000

Tenders in hand	Estimated contract value
Ductile Iron Pipe Systems	£10,000,000
PE Pipes & Fittings	£7,000,000
Boundary Boxes	£4,131,680
Fire Systems, CCTV, Alarms, Door Access, ID Cards, Response Services (Security)	£4,000,000
Chamber Sections	£2,112,000
Building maintenance (inc Electrical, Fencing etc)	£2,000,000
Plastic Service Fittings	£1,600,000
PPE & Consumables	£1,440,000
Service Fittings	£1,416,000
Office Cleaning	£1,400,000
Fire Extinguishers	£1,000,000

South East Water operates a sustainable procurement policy whereby suppliers of goods and services are rated for whole life cost, environmental impact and sustainability as part of the contract award decision criteria.



## 10. Financing

The Group has strong liquidity with £6.6m on the balance sheet at the year end and a further £70m available to draw down on the authorised credit facility.

### Authorised credit facility

As explained in the September 2017 Investors Report, the £90m Authorised Credit Facility was extended to 18 June 2022. £20m is currently drawn on the facility.

### Liquidity facilities

The DSR and O&M facilities were renewed in June 2018 with Commonwealth Bank of Australia for the period to June 2019. The DSR liquidity facility has a commitment of £38m and the O&M facility has a commitment of £19m.

## 11. Credit ratings

The credit rating of South East Water is covered by Moody's Investor Service ("Moody's") and Standard and Poor's ("S&P"). Moody's and S&P issued credit opinions in October 2017. There was no change in South East Water's rating from either rating agency.

	Moody's	S&P
Credit rating	Baa2	BBB

## 12. Surplus

The SEWH Board approved £12.3m of dividends to Hastings Water (UK) Limited in the financial year.

## 13. Board / Management Changes

On 10 April 2018 Hastings Fund Managers Limited, who are the managers of the Group's ultimate holding company, changed its name to Vantage Infrastructure Holdings Limited.

The South East Water Board of directors is as follows:

### South East Water Limited

#### N Salmon

Independent Non-Executive Chairman

#### P Butler

Managing Director\*

#### A Farmer

Finance Director\*

#### D Hinton

Asset and Regulation Director\*

#### J Barnes

Independent Non-Executive Director

#### E Gilthorpe

Independent Non-Executive Director

#### C Girling

Independent Non-Executive Director

#### C Pronto

Non-Executive Director (appointed 1 June 2018)

#### O Schubert

Non-Executive Director (appointed 3 May 2017)\*\*

#### M Szczepaniak

Non-Executive Director\*\*

#### P Rich

Independent Non-Executive Director  
(resigned 3 July 2017)

#### P Dixon

Non-Executive Director (resigned 27 April 2017)\*\*

The Company Secretary is **Nicolas Truillet**

### South East Water (Holdings) Limited

#### O Schubert

Non-Executive Director (appointed 28 April 2017)\*

#### M Szczepaniak

Non-Executive Director\*\*

#### P Dixon

Non-Executive Director (resigned 27 April 2017)\*\*

### South East Water (Finance) Limited

#### P Butler

Executive Director

#### A Farmer

Executive Director

#### M Szczepaniak

Non-Executive Director\*\*

\* Denotes an Executive Director

\*\* Denotes a Vantage appointee

# Ratios

## 1. Historic

We confirm that in respect of the Calculation Date on 31 March 2018, by reference to the most recent financial statements that we are obliged to deliver to you in accordance with Paragraph 1 (Financial Statements) of Part 1

(Information Covenants) of Schedule 4 (Covenants) of the Common Terms Agreement that the ratios are as detailed in the table below in respect of the Calculation date on 31 March 2018.

Date	31-Mar-16	31-Mar-17	Calculation Date	31-Mar-19	31-Mar-20
RAR (at such Calculation Date or, in the case of forward-looking ratios, as at 31 March falling in the relevant Test Period)	80.8%	78.3%	77.7%	77.9%	80.0%
Test Period	1-Apr-15 to 31-Mar-16	1-Apr-16 to 31-Mar-17	1-Apr-17 to 31-Mar-18	1-Apr-18 to 31-Mar-19	1-Apr-19 to 31-Mar-20
ICR	3.56 x	3.76 x	3.52 x	3.40 x	2.97 x
Adjusted ICR	3.56 x	3.76 x	3.52 x	3.40 x	2.97 x
Average adjusted ICR	3.61 x	3.56 x	3.28 x	3.17 x	2.97 x
Conformed adjusted ICR	1.90 x	2.09 x	1.81 x	1.47 x	1.21 x
Conformed average adjusted ICR	1.93 x	1.78 x	1.48 x	1.33 x	1.21 x

2. We confirm that each of the above ratios has been calculated in respect of each of the relevant period(s) for which it is required under the Common Terms Agreement and has not breached the

Trigger Event Ratio Levels and has not caused Paragraph 17 (Ratios) of part 2 (Event of Default (South East Water)) of Schedule 6 of the Common Terms Agreement to be breached.

Ratios *continued*

3. We set out below the computation of the following ratios set out in the table in Paragraph 1 above for your information:

## a) RAR

Date	31-Mar-16 £m	31-Mar-17 £m	Calculation Date £m	31-Mar-19 £m	31-Mar-20 £m
<b>Senior Debt</b> (Closing Balances)					
Finance Leases	0.0	0.0	0.0	0.0	0.0
Debentures	1.0	1.0	1.0	1.0	1.0
Nominal Debt	166.0	166.0	166.0	166.0	166.0
Synthetic Index Linked Bonds	282.9	287.5	296.3	306.3	0.0
Index Linked Bonds	156.1	160.4	166.0	171.3	176.4
Fixed Rate Bonds	0.0	0.0	0.0	0.0	306.2
Index Linked Bonds	0.0	0.0	0.0	0.0	0.0
Index Linked Loans (USS)	107.2	109.9	113.5	117.4	121.2
Index Linked Loans	246.3	250.9	259.9	268.6	276.8
Capex Drawdown Facility	0.0	0.0	20.0	53.0	67.9
Total Senior Debt Closing Balance	959.5	975.7	1022.8	1083.5	1115.4
Less: Cash Balance	(17.0)	(11.4)	(6.5)	(12.5)	(3.7)
Senior Net Indebtedness	942.5	964.3	1016.2	1071.0	1111.7
Regulatory Capital Value	1166.6	1231.1	1307.5	1374.5	1389.1
RAR	80.8%	78.3%	77.7%	77.9%	80.0%

Ratios *continued*

## b) ICR

Date	1-Apr-15 to 31-Mar-16 £m	1-Apr-16 to 31-Mar-17 £m	1-Apr-17 to 31-Mar-18 £m	1-Apr-18 to 31-Mar-19 £m	1-Apr-19 to 31-Mar-20 £m
<b>Net Cash Flow</b>					
Net cash flow from operating activities	120.2	127.5	123.1	137.7	129.5
Exceptional items	0.0	0.0	0.0	(9.1)	0.0
Recoverable VAT	2.2	2.7	4.1	0.0	0.0
Corporation tax paid	0.0	0.0	0.0	0.0	0.0
Pension funding					
Non-appointed	0.0	0.0	(3.4)	(6.1)	(6.3)
Net Cash Flow	122.4	130.2	123.7	122.5	123.1
<b>Senior Debt Interest</b>					
Finance Leases	0.0	0.1	0.0	0.0	0.0
Debentures	0.0	0.0	0.0	0.0	0.0
Nominal Debt	9.3	9.3	9.3	9.3	19.4
Synthetic Index Linked Bonds	8.6	8.7	8.8	9.3	2.9
Index Linked Bonds	3.9	4.0	4.1	4.3	4.3
Index Linked Loans (USS)	2.6	2.6	2.7	2.8	2.8
Index Linked Loans	8.6	8.8	9.1	9.4	9.6
Drawdown Facilities	0.8	0.5	0.5	0.2	1.1
Ambac fee	0.7	0.8	0.8	0.7	1.3
Senior Debt Interest Payable	34.6	34.7	35.2	36.1	41.5
Interest Receivable	(0.2)	(0.1)	(0.1)	(0.0)	(0.0)
Senior Debt Interest	34.4	34.6	35.2	36.0	41.5
ICR	3.56 x	3.76 x	3.52 x	3.40 x	2.97 x



Ratios *continued*

## c) Adjusted ICR

Date	1-Apr-15 to 31-Mar-16 £m	1-Apr-16 to 31-Mar-17 £m	1-Apr-17 to 31-Mar-18 £m	1-Apr-18 to 31-Mar-19 £m	1-Apr-19 to 31-Mar-20 £m
Net Cash Flow	122.4	130.2	123.7	122.5	123.1
<b>CCD &amp; IRC</b>					
CCD	0.0	0.0	0.0	0.0	0.0
IRC	0.0	0.0	0.0	0.0	0.0
Total regulatory depreciation	0.0	0.0	0.0	0.0	0.0
Net Cash Flow after regulatory depreciation	122.4	130.2	123.7	122.5	123.1
Senior Debt Interest	34.4	34.6	35.2	36.0	41.5
Adjusted ICR	3.56 x	3.76 x	3.52 x	3.40 x	2.97 x

## d) Average Adjusted ICR

Date	1-Apr-15 to 31-Mar-16 £m	1-Apr-16 to 31-Mar-17 £m	1-Apr-17 to 31-Mar-18 £m	1-Apr-18 to 31-Mar-19 £m	1-Apr-19 to 31-Mar-20 £m
Net Cash Flow	122.4	130.2	123.7	122.5	123.1
<b>CCD &amp; IRC</b>					
CCD	0.0	0.0	0.0	0.0	0.0
IRC	0.0	0.0	0.0	0.0	0.0
Total regulatory depreciation	0.0	0.0	0.0	0.0	0.0
Net Cash Flow after regulatory depreciation	122.4	130.2	123.7	122.5	123.1
Senior Debt Interest	34.4	34.6	35.2	36.0	41.5
Adjusted ICR	3.56 x	3.76 x	3.52 x	3.40 x	2.97 x
Average Adjusted ICR	3.61 x	3.56 x	3.28 x	3.17 x	2.97 x

Ratios *continued***e) Conformed Adjusted ICR**

Date	1-Apr-15 to 31-Mar-16 £m	1-Apr-16 to 31-Mar-17 £m	1-Apr-17 to 31-Mar-18 £m	1-Apr-18 to 31-Mar-19 £m	1-Apr-19 to 31-Mar-20 £m
Net Cash Flow	122.4	130.2	123.7	122.5	123.1
RCV Depreciation	38.3	43.1	46.8	49.4	52.3
Capitalised IRE	18.9	14.7	13.4	20.2	20.4
Total regulatory depreciation	57.2	57.8	60.2	69.6	72.7
Net Cash Flow after regulatory depreciation	65.2	72.4	63.5	52.9	50.4
Senior Debt Interest	34.4	34.6	35.2	36.0	41.5
Conformed Adjusted ICR	1.90 x	2.09 x	1.81 x	1.47 x	1.21 x

**f) Conformed Average Adjusted ICR**

Date	1-Apr-15 to 31-Mar-16 £m	1-Apr-16 to 31-Mar-17 £m	1-Apr-17 to 31-Mar-18 £m	1-Apr-18 to 31-Mar-19 £m	1-Apr-19 to 31-Mar-20 £m
Net Cash Flow	122.4	130.2	123.7	122.5	123.1
<b>CCD &amp; IRC</b>					
CCD	38.3	43.1	46.8	49.4	52.3
IRC	18.9	14.7	13.4	20.2	20.4
Total regulatory depreciation	57.2	57.8	60.2	69.6	72.7
Net Cash Flow after regulatory depreciation	65.2	72.4	63.5	52.9	50.4
Senior Debt Interest	34.4	34.6	35.2	36.0	41.5
Conformed Adjusted ICR	1.90 x	2.09 x	1.81 x	1.47 x	1.21 x
Conformed Average Adjusted ICR	1.93 x	1.78 x	1.48 x	1.33 x	1.21 x

4. We certify that for the period to 31 March 2018 the Annual Finance Charge is £35.5m.

Ratios *continued*

## 5. Annual Finance Charge calculation:

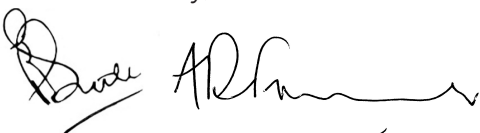
Date	to 31 March 2018 £m
<b>Senior Debt Interest</b>	
Finance Leases	0.0
Debentures	0.0
Nominal Debt (£166m)	9.3
Synthetic Index Linked Bonds (£200m)	9.0
Index Linked Bonds (£130m)	4.2
Index linked loans (USS)	2.7
Index Linked Loans	9.1
Working Capital Facility	0.1
Capex Drawdown Facility	0.0
Ambac fee	0.8
Commitment fee	0.4
	35.5
Less: interest earned	(0.1)
12 Months Total	35.5

Total payments into the DSR Accounts for the period to 31 March 2018 were £34.8m.

## 6. We also confirm that:

- (a) no Default of Potential Trigger Event is outstanding
- (b) that South East Water's insurance's are being maintained in accordance with:
  - (i) the Common Terms Agreement
  - (ii) the provisions of the Finance Leases

Yours faithfully,



Director  
For and on behalf of  
**SOUTH EAST WATER LIMITED**



Director  
For and on behalf of  
**SOUTH EAST WATER (FINANCE) LIMITED**



Director  
For and on behalf of  
**SOUTH EAST WATER (HOLDINGS) LIMITED**

# Appendix

## Financial Statements

### South East Water (Holdings) Limited

#### Consolidated profit & loss account for the period ended 31 March 2018

	Companies £000	Eliminations £000	Group £000
Turnover	224.8	-	224.8
Operating costs	(159.0)	-	(159.0)
Profit on disposal of fixed assets	0.3	-	0.3
Other operating income	8.9	-	8.9
<b>Operating profit</b>	75.0	-	75.0
Income from investments	18.0	(18.0)	-
Interest receivable - group	4.5	(4.5)	-
Interest receivable - other	0.1	-	0.1
Interest payable - group	(9.7)	4.5	(5.2)
Interest payable - other	(56.0)	-	(56.0)
Return on pension scheme assets	0.2	-	0.2
<b>Profit on ordinary activities before taxation</b>	32.0	(18.0)	14.0
Tax (charge)/credit on profit on ordinary activities	(5.7)	-	(5.7)
<b>Profit on ordinary activities after taxation</b>	26.3	(18.0)	8.3
<b>Dividends</b>	(30.3)	18.0	(12.3)
	(4.0)	-	(4.0)
STRGL- pension	7.8	-	7.8
<b>Profit/(loss) for period taken to P&amp;L reserves</b>	3.8	-	3.8



Appendix *continued*
**South East Water (Holdings) Limited**  
**Consolidated balance sheet at 31 March 2018**

	Companies £000	Eliminations £000	Group £000
Tangible assets	1,512.5	-	1,512.5
Investments	361.4	(361.4)	-
Net Current (liabilities)/assets	(10.0)	-	(10.0)
Creditors: amounts falling due after more than one year	(230.7)		(230.7)
Current asset investments	4.1	-	4.1
Cash and cash equivalents:			
Current accounts	2.2	-	2.2
DSR	0.3	-	0.3
O&M	-	-	-
Financing liabilities	-	-	-
Intra group loan creditors	(939.8)	939.8	-
Intra group loan debtors	939.8	(939.8)	-
Other HDF group loans	(82.2)	-	(82.2)
Debentures	(1.0)	-	(1.0)
Bonds	(496.0)	-	(496.0)
Indexation	(140.2)	-	(140.2)
Artesian loans	(269.0)	-	(269.0)
Indexation	(104.5)	-	(104.5)
Unamortised costs	5.6	-	5.6
Bank loans	(20.0)	-	(20.0)
Net pension liability	21.2	-	21.2
<b>Net assets</b>	<b>553.8</b>	<b>(361.4)</b>	<b>192.4</b>
<b>Capital and reserves</b>			
Called up share capital	140.7	(49.3)	91.4
Revaluation reserve	256.4	-	256.4
Profit and loss account b/fwd.	147.7	(312.1)	(164.4)
Loss for period	8.9	-	8.9
<b>Capital employed</b>	<b>553.8</b>	<b>(361.4)</b>	<b>192.4</b>

Appendix *continued***South East Water (Holdings) Limited****Consolidated movement in the profit and loss reserve for the year ended 31 March 2018**

	Companies £000	Eliminations £000	Group £000
At 1 April 2017	147.7	(312.1)	(164.4)
Profit for the year	26.3	(18.0)	8.3
Pension scheme in STRGL	7.8	-	7.8
Dividends	(30.3)	18.0	(12.3)
Movement through reserves	5.2	-	5.2
	8.9	-	8.9
At 31 March 2018	156.7	(312.1)	(155.4)