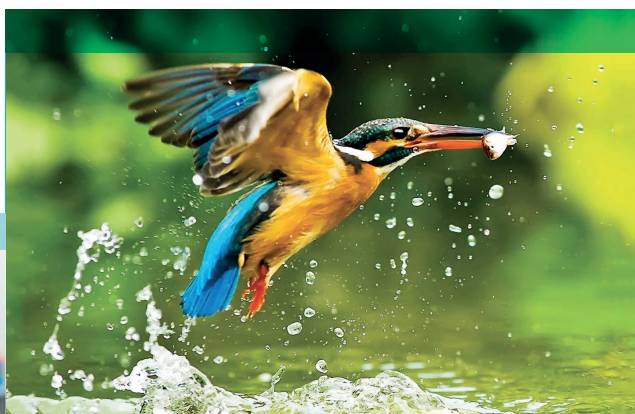


2021/22 Investor's Report

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



Investor's Report 2021/22



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General Overview and Business Update

This Investors Report covers the twelve month period ending 31 March 2022. It also includes a summary of any subsequent material events in the period prior to the publication of this report.

1.0 Environmental, social and governance framework

Climate change is – and will continue to be – a huge challenge for us. It's an area of uncertainty in terms of risk. We operate in an area of water-stress and in recent years have done a lot to overcome this, including our hugely successful Customer Metering Programme, where we have the highest level of meter penetration of any water company in the UK. However, as population growth continues we must make further changes and as new evidence and research emerges, we will use innovation and best practice to overcome the challenges that this will bring.

This year we have prepared our draft 25 year environment plan. This is a first in the water industry and we believe that this ambitious approach will make significant improvements to our environment within a generation. We have sought feedback from stakeholders and customers alike. We invited over 500,000 customers to give us their views, which is the largest consultation we have ever undertaken. This feedback will be vital in helping us to develop our plan, and protect the unique environment which is an integral part of everything we do. In addition, we have shown our commitment to working in partnership to make sure we secure our resources for the future by working with Water Resources in the South East (WRSE) to create a regional plan which looks forward to 2100. This will be the basis of our own water resources management plan, designed for the long-term.

For a long time, we've been talking to the farmers in our region to see how we can join together to keep our water sources and rivers cleaner, to reduce the amount of fertilisers going in to them in the first place. Our proactive approach is working in collaboration to clean our rivers.

Our commitment to achieve net zero carbon by 2030 is also on track. We will continue to track our progress and make robust decisions which will ensure we achieve our goal as it edges ever-closer. We are always looking towards renewable energy sources, as well as how nature-based accounting can improve the environment.

Of course, we consider ourselves a service industry and people are at the very heart of every area of service. We have committed to learn more about our customers, their expectations of us and how we can help them to reduce their water bills and play their part in water efficiency drives. We have continued to reach out to the sectors of the community that are more difficult to engage with and to learn more about how we can offer extra support. An industry-leading data share initiative, where we are working in partnership with two local authorities to auto enrol customers onto a social tariff, is a great example of this. We are actively seeking to offer assistance as an early intervention and prevention of being unable to pay bills, especially where there may be financial pressures for families and individuals.

Providing excellent customer service across the board is not just an ambition for us, it is embedded in our vision and values. That's why being awarded the ServiceMark Accreditation with Distinction from The Institute of Customer Service – one of only a handful of companies to receive it – was so important to us. We are extremely proud of that achievement and it is a reflection of the teamwork across the business.

Further details of our environmental, social and governance framework are available in our performance, people and planet report.

2.0 Operational performance

We are proud to supply high quality drinking water to our customers at a time when other water companies are under scrutiny regarding storm water overflows. Protecting and enhancing our local environment is integral to what we do and you will see in this report the industry leading commitment we have made to planning how we protect our environment over the next 25 years.

The impact of the Covid-19 global pandemic has continued to be felt, affecting everything we do. As we entered the second year of Covid-19, the depth of the strong foundations we set in 2020/21 has reaped huge benefits. However economic conditions have worsened impacting our costs and this is set to continue in 2022/23. High energy costs and the rising cost of living are affecting our customers.

We have a number of key engineering projects underway to deliver improved resilience across our network. The temporary water treatment works in Aylesford, Kent – built in just eight months to replace the loss of a key strategic service reservoir caused by a sinkhole that opened up – continues to support the area. Construction is now underway on a permanent water treatment works solution on the site. This project is just one of a number of significant investments we're making, such as the £11 million strategic pipeline being laid between Fleet and Greywell in Hampshire to enable more water to be pumped into the region as the population increases. We've also been working to upgrade our existing network. In Chilham we've invested £2.1 million installing new equipment in the area to prevent customers going without water during power cuts, and in Pluckley, Kent a £700,000 new 1.2 km water main will reduce the likelihood of bursts and supply interruptions. The multi-million-pound expansion of our flagship Keleher treatment site in Bray was officially unveiled in February by the Rt Hon Theresa May MP, in her role as constituency MP for Maidenhead. The site is now capable of pumping up to 68 million litres of water a day – a 50 per cent capacity increase and enough to fill 27 Olympic-sized swimming pools.

Our ability to respond to increased demand has improved, putting in place extra capacity where needed. We are particularly proud of our achievements in the environment area of our business, as we know our connection to the natural world is crucial.

Of course, the year was not without adversity, most notably Storm Eunice, the worst storm to hit our region in more than a generation. Sussex bore the brunt of the issues caused by the high winds, which hit again when Storm Franklin swept in immediately after. Despite significant planning for the storm, including the provision of alternative power sources, unprecedented power outages left us in a very difficult position. In the aftermath of the storms, over 100 assets were inoperable due to lack of power.

This represented the most significant loss of power in our company's history. Whilst we worked closely with UK Power Networks to restore electricity, the power cuts also caused damage to vital equipment in some areas, which meant we weren't able to pump water into the network as soon as power was restored. Once again, our colleagues rose to the challenges, but some customers were affected whilst power supplies were impacted. We were in direct contact with hospitals, supplying tankers to various NHS sites, and other healthcare centres to make sure they were prioritised, and supported our livestock farmers and their specialist needs. At the same time, we prioritised our vulnerable customers and made over 5,000 deliveries to customers for whom water is vital to their lives.

During the height of the emergency we set up and had volunteers at more bottled water stations than we have had in any previous incidents, the logistics of which alone were immense. We are very proud of the response by our teams on the ground, and among some of the inevitable, and understandable, complaints were also proud of some of the excellent feedback received.

Our early and intense engagement with our stakeholders was also crucial in our success in getting essential messages to our communities in extremely testing circumstances, especially where many were without power and internet access. We are doing all we can to support the communities worst affected and, as always, reflecting on any lessons to be learned, working with local stakeholders to gather feedback on how we can respond better in the future.

For impacted customers who fell outside our GSS, specifically those in East Grinstead, we set up a Community Fund of £100,000 to be distributed to charities, community groups & not for profit organisations, selected by the local community. Our customers are currently voting on how this fund should be distributed and we look forward to making a real difference in the community.

Overall we have made good progress against our plans set out under our four strategic themes. As we return to more normal times, with the pandemic behind us, we will continue to develop the positive outcomes that we have delivered in challenging times.

General overview and business update continued

3.0 Water resources and leakage

Demand patterns during 2021/22 represented something of a 'transition' from the high demand impacted by Covid-19 restrictions in 2020/21, decreasing progressively month on month throughout the year as restrictions were lifted and people became more mobile and travelled outside of our supply area. Overall we saw demand decrease by 1 per cent compared to the previous year.

We received 95 per cent of long term average (LTA) rainfall across our supply area. The winter months were drier than normal recording just 84 per cent of LTA rainfall while summer months were slightly wetter than normal with 107 per cent of LTA rainfall. Our water resources at the start of 2022/23 were good, with water resources close to normal expected levels for the time of year, putting us in a good position to accommodate high demand in summer 2022.

We have made good progress with implementing our customer water efficiency strategy agreed with the regulator. Leakage levels continue to be maintained below the leakage target.

In collaboration with the other Water Resources South East water companies, we consulted on an emerging regional water resources plan for the period 2025 to 2100. The emerging plan had a strong alignment with our own Water Resources Management plan published in 2018. The final regional plan will be completed in 2022/23 and will form the basis of our own draft Water Resources Management Plan 2024 which we will consult on in the autumn of 2022, with publication of a revised plan due in 2023.

In May we received confirmation from Defra to publish our tactical drought plan, to cover the period 2022 to 2027. The publication follows a positive engagement process with customers and stakeholders.

4.0 Our people (including Health and Safety)

Across the business our colleagues have continued to show dedication and agility, together with commitment and resilience. We are a 24/7, 365 day a year service and our teams rise to all the challenges that brings. We rely on the expertise of a huge range of professionals, including our scientists in our laboratory, specialists out in the field, operational site managers, highly-professional customer service teams, our environmental experts, and our support services behind the scenes.

We set out an ambitious five-year people plan to support our business objectives and to drive our ambition to be the company that people want to work for. Year two of our people plan has been a busy one with activities ongoing under each of the four key areas of focus.

To develop our thriving and diverse workforce, our activities have included using specialist skill sets to improve our attraction and recruitment process and to ensure each resourcing manager receives the best level of service and support in recruiting the skills and capabilities they need. We have broadened our channels of attraction to include Linked-In and Facebook.

Our gender pay gap has improved again this year, reducing by 2.7 per cent this year and by 5.2 per cent over the last two years. We have also increased the number of women in both senior and management roles as we concentrate on diversity of thinking throughout the company. We are committed to developing more equal presence of men and women at each and every opportunity we have, especially more women in our operational roles and indeed, men in our retail roles. South East Water has an overall female presence in the workforce of 43 per cent, which compares to the industry average of 20 per cent (EU skills data 2018) and gives us a strong talent base to improve over time.

In addition to our activities, as set out last year, we have taken advantage of the changes in the way of working that the pandemic has created and that has allowed us to promote and develop our agile working practices. We are continuing to improve diversity in parts of the business where there is weighted bias in either direction, through specialist recruitment techniques and broadening our application pool.

We have launched our new wellbeing strategy which focuses on physical, mental, social and financial wellbeing for all our employees. An annual diary of events has been created including lunch & learn activities with external speakers, opportunities to engage with specialist advisors, signposting to support and taking advantage of the great benefits package we offer. Across the business we now have 37 Wellbeing Champions in the business who have all undertaken level two Understanding Health Improvement training to complement our 42 Mental Health First Aiders who support employees and signpost to our internal and external help. We are proud to be a UK safe space employer which demonstrates we provide exceptional support for those employees and family members suffering from domestic abuse.

This year we have engaged with the Leonard Cheshire Foundation and its Change 100 programme. This involves talented graduates who have a disability, but have yet to enter the job market, undertaking an internship for 100 days. We have launched our apprentice plan which increases the number of apprenticeships by 250 per cent. Made up of new apprentices across the business and apprentice and training opportunities to existing colleagues, this equates to approximately 10 per cent of our workforce undertaking an apprenticeship, which supports our future proofing and engagement with our industry.

To engage our talented workforce, we have invested in a new learning management system, entitled TAP. It encourages personal development and supports performance across the business. TAP houses more than 5,000 pieces of training collateral which supports that development. In addition, TAP allows us to issue, report and bespoke all mandatory and compliance training which can be completed via e-learning, face-to-face or a combination of the two.

For the first time all our employees will have a performance development plan which supports their personal and professional development. This is supported by the launch of our new career development opportunities via our Aspire, Inspire and Lead portals which provide training, guidance, courses and professional qualifications at each level of our employees' development, whether they aspire to develop through our business, seek to inspire their teams or lead from the front. We have redesigned our performance management process, using leadership behaviours and linking performance objectives to company objectives. This has helped our colleagues understand how they help the business to deliver our key targets and make a difference to our customers.

Our 2021 employee survey provided great insight and results. Action plans completed from the six pulse surveys carried out during the pandemic were shared with 'You said, we did' and we were pleased to see confidence in the company taking action from the results increased. Our 79 per cent response rate yielded an employee engagement score of 89 per cent and empowering our employees sits at 90 per cent. Our employees felt we responded to the different needs of our customers with a score of 96 per cent, and 94 per cent believed we were committed to being ethical and responsible. Our company values also scored highly, amongst others at 94 per cent.

Future proofing our business activities has included formulating our hybrid working plan across the business as we come out of the pandemic and move to a more formal agile working approach. We also improved the level of self-service which supports all our colleagues, especially those out in the field.

As always, the health and safety of our colleagues is our number one priority. We have reinforced the message 'no job is too urgent not to be done safely' with internal communications throughout the year. There were five reportable accidents during the year. We traditionally consider not only the actual harm recorded but also the potential for harm. Often the greatest benefit can come from a thorough investigation of events that do not result in injury but have high potential to have done so.

General overview and business update continued

5.0 Financial performance in the 12 months ended 31 March 2022

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

- South East Water (Holdings) Limited ("SEWH").
- South East Water Limited ("SEWL" or "South East Water").
- South East Water (Finance) Limited ("SEWF").
- South East Water (Finance) Limited is a 100 per cent subsidiary of South East Water Limited and South East Water Limited is a 100 per cent subsidiary of South East Water (Holdings) Limited.

The accounts for the South East Water Group for the year to 31 March 2022 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 year are published on the company's website.

The entity accounts for SEWL, which are included in the published group accounts, 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.

Revenue

Turnover for the year to 31 March 2022 was higher at £251.3 million when compared to £248.2 million for the previous year. The increase of £3.1 million included an increase in water revenue of £0.4 million and increased non-water income of £2.7 million. The increased water revenue included higher consumption in the year of £1.6 million due to historic non-household settlement adjustments reported by retailers for 2020/21. The revenue from higher consumption was offset by a lower turnover of £1.2 million due to a reduction in average prices in the year. Under the regulatory price control mechanism, the tariffs are adjusted to recognise the movements in projected consumption against the revenue set at the publication of the Final Determination. For 2021/22 our tariffs decreased by 0.5 per cent, reflecting the increase in consumption driven by Covid-19 in 2020/21. The increased turnover from non-water sales is mainly due to increased demand from developers as they recover from the pandemic.

Other operating income has increased by £10.5 million to £21.9 million during the year. Other income includes the receipt of £6 million of insurance receipts in respect of the damage to the reservoirs at Aylesford in 2020/21 and £4 million of insurance receipts for business interruption to cover the increased costs incurred by the failure of these reservoirs. The other income stream that has increased year on year is laboratory income which has returned to the pre-pandemic levels with an increase of £0.4 million to £2.7 million.

Operating costs

Our operating costs for the year, including charges for doubtful debts, have increased from £181.4 million to £188.5 million, an increase in costs of £7.1 million in the year.

The main driver of the increase is an adjustment which was made to past service costs on one of the group's defined benefit pension schemes in the financial year 2020/21 as a result of changes the index used for measuring future liabilities. This reduced staff benefit costs in the prior year by £7.8 million. No similar adjustment has been made in the year ended 31 March 2022. This is partially offset by a £2.3 million impairment of the Aylesford reservoirs having been charged in the financial year 2020/21, which has not been repeated this year.

Depreciation increased in the year by £2.3 million, which is consistent with previous years as new assets brought into operation during the year. Another significant impact on costs in the year was Storm Eunice, which generated £1.6 million of operating expenditure, primarily on contractors' costs and customer compensation payments. Energy costs increased by £1.1 million due to the impact of inflationary pressures on the cost of energy. The group had largely protected itself from increased energy costs during the year, but the continued higher than expected demand for water due to customer behaviour following the pandemic required additional energy being purchased at the higher prices.

The charge for bad debts in the year was £5.0 million compared to £3.8 million in the prior year. The provision is based on our revised policy adopted in 2020/21 using the cash collection history for the past three years. This places greater emphasis on our recent cash collection history and better reflects the current economic circumstances. The increase in bad debt shows the continuing problems in the collection of older debts through the year, coupled with the increasing inflationary pressures on household finances and the prospective view on future expectations.

Off-setting the increases in costs were reductions in reactive maintenance costs of £2.6 million after a year without extreme temperature events leading to historically low burst and communication pipe repair activity. A further benefit of the more usual temperatures in the summer was a reduction in the costs of bulks supplies of water from other companies of £1.0 million.

Finance costs

Interest payable for the group for the year to 31 March 2022 was £72.6 million compared to £48.1 million in the prior year. The increase in finance costs is mainly due to higher indexation charges in the year on our index linked debt. Higher RPI inflation has resulted in an increase of £23.1 million in the indexation attaching to the index linked loans.

Interest payable includes the following:

- **£14.0 million interest on listed debt/bonds (2021: £13.8 million).**
- **£13.6 million indexation on index linked listed bonds (2021: £2.4 million).**
- **£13.1 million interest on Index linked loans (including Artesian Finance loans) (2021: £12.7 million).**
- **£18.6 million indexation on Index linked loans (including Artesian Finance loans) (2021: £6.7 million).**
- **£5.8 million interest on loan notes (2021: £5.4 million).**
- **£1.7 million interest on variable rate loan (2021: £1.7 million).**
- **£5.0 million interest payable by SEWH to group companies (2021: £5.1 million).**
- **£3.0 million relating to other interest payable (2021: £3.0 million).**
- **£(2.2) million capitalised interest (2021: £(2.7) million).**

Taxation

Taxation for the year was £ 44.9 million (2021: £5.0 million). Our tax charge comprises:

- **Current tax credit of £0.4 million (2021: £2.6 million). The decrease in current tax reflects the decrease in taxable profit after allowing for appropriate tax deductions.**
- **Deferred tax of £4.5 million (2021: £3.7 million). The increase in deferred tax is due to a charge for the prior year as a result of changes between the prior year financial statements and the tax computations submitted.**
- **Deferred tax of £40.8 million as a result of the increase in tax rate from 19 per cent to 25 per cent with effect from 1 April 2023.**

Cash

The SEW Group has cash and cash equivalent balances of £14.5 million as at 31 March 2022 compared with £41.7 million as at 31 March 2021.

The restricted cash balance as at 31 March 2022 was £3.1 million compared to £0.8 million as at 31 March 2021. Cash held in these designated bank accounts are to meet interest and other related finance costs falling due in respect of the group's senior debt.

General overview and business update continued

6.0 Regulatory update

Regulatory reporting

The 2021/22 Annual Report and Financial Statements which includes the Statutory Accounts, the Regulatory Accounts, the Ofwat prescribed Performance Report and the Risk and Compliance Statement are published on our website.

In addition, we also publish on our website our performance, people and planet report for 2021/22 which gives further information about our performance against our agreed outcomes. Overall, we incurred a net penalty of £0.8 million in 2021/22

(excluding C-MeX and D-MeX as the assessment of these two measures has not yet been carried out by Ofwat, and excluding the impact of Storm Eunice on our interruption performance as an application for an exemption was made to Ofwat due to the exceptional nature of this event). This compares with a net penalty of £3.8 million in 2020/21 (also excluding C-MeX and D-MeX).

2021/22 performance for Outcome Delivery Incentives are summarised in the table below:

| Performance Commitment | Unit | Target in 2021/22 | Actual performance in 2021/22 | Penalty or Reward (£m) |
|--|------------------------|-------------------|-------------------------------|------------------------|
| ■ Leakage | % reduction | 0.4 | 3.3 | 1.023 |
| ■ Mains repairs | Per 1,000 km of main 1 | 171.5 | 129.3 | 0.000 |
| ■ CRI | Score | 0 | 1.21 | 0.000 |
| ■ Unplanned outage | % | 3.76 | 3.44 | 0.000 |
| ■ PCC | % reduction | 2.9 | -8.3 | (2.190) |
| ■ Supply interruptions | Min : Sec | 00:6:08 | 01:12:33 | (3.157) |
| ■ C-MeX* | Score out of 100 | N/A | 76.59 | (0.770) |
| ■ D-MeX* | Score out of 100 | N/A | 81.34 | (0.194) |
| ■ AIM | ML/d | 0 | -148 | 0.000 |
| ■ Appearance of water | Per 10,000 population | 1.02 | 0.98 | 0.038 |
| ■ Taste and odour of water | Per 10,000 population | 0.38 | 0.36 | 0.016 |
| ■ Properties at risk of low pressure | Per 10,000 population | 0.5 | 0.3 | 0.015 |
| ■ Household voids | % | 2.1 | 1.97 | 0.111 |
| ■ Non-Household voids | % | 8.1 | 10.24 | (0.717) |
| ■ WINEP | Schemes | 43 | 38 | (0.325) |
| ■ Engaging and working with land owners | Hectares | 5,687 | 5,986 | N/A |
| ■ Protecting wildlife and increasing biodiversity | Hectares | 1,218 | 1,427 | N/A |
| ■ Sites protected from flooding | Number of sites | 0 | 20 | N/A |
| ■ Strategic main Wellwood to Potters Corner | % delivered | 0 | 9.45 | N/A |
| ■ Customer satisfaction by segment 1 - 'mindful optimists' | Score out of 5 | 4.2 | 4.0 | N/A |
| ■ Customer satisfaction by segment 2 - 'global advocates' | Score out of 5 | 4.4 | 4.2 | N/A |

| Performance Commitment | Unit | Target in 2021/22 | Actual performance in 2021/22 | Penalty or Reward (£m) |
|---|------------------------|-------------------|-------------------------------|------------------------|
| ■ Customer satisfaction by segment 3 - 'just me and mine' | Score out of 5 | 4.3 | 4.0 | N/A |
| ■ Customer satisfaction by segment 4 - 'careful neighbours' | Score out of 5 | 4.3 | 4.2 | N/A |
| ■ Customer satisfaction by segment 5 - 'busy juggler' | Score out of 5 | 4.4 | 4.1 | N/A |
| ■ Customer satisfaction by segment 6 - 'living for today' | Score out of 5 | 4.3 | 4.0 | N/A |
| ■ Value for money | Score out of 5 | 3.8 | 3.6 | N/A |
| ■ Satisfaction of household customers who are experiencing payment difficulties | Score out of 5 | 4.3 | 4.3 | N/A |
| ■ Satisfaction of household customers who are receiving, or applying for, non-financial support | Score out of 5 | 4.2 | 4.3 | N/A |
| ■ Satisfaction of household customers on our vulnerability schemes during a supply interruption | Score out of 5 | 3.8 | 3.2 | N/A |
| ■ Household customers receiving financial support | Number | 58,000 | 53,981 | N/A |
| ■ Satisfaction of stakeholders in relation to assistance offered | Score out of 5 | 3.7 | 3.8 | N/A |
| ■ Priority Services for customers in vulnerable circumstances – Reach | % | 5 | 5.2 | N/A |
| ■ Priority Services for customers in vulnerable circumstances – Actual Contact | % | 35 | 57.5 | N/A |
| ■ Priority Services for customers in vulnerable circumstances – Attempted Contact | % | 90 | 93.5 | N/A |
| ■ Gap sites | Number of sites | 25 | 42 | N/A |
| ■ Risk of severe restrictions in a drought | % | 0 | 0 | N/A |
| ■ ERI (Event Risk Index) | Score | 0 | 20.463 | N/A |
| ■ Delivery of water industry environment programme requirements | Met / Not met | Met | Not Met | N/A |
| ■ Greenhouse gas emissions | kgCO ₂ e/MI | 119.9 | 30.4 | N/A |
| ■ Engaging and working with abstractors to improve catchment resilience to low flows | % | 0 | 0 | N/A |

* These are relative measures and because of Ofwat's processes, the penalty and reward numbers will not be completely finalised at the time of publication. (estimates are shown).

■ Target met

■ Target not met

General overview and business update continued

PR24 price review

Ofwat published its draft methodology for the PR24 price review process on 7 July, with a consultation period of two months. South East Water is reviewing the documentation and will submit a response. The final methodology for the PR24 process will be published in December 2022, with the final determination published in December 2024.

Ofwat appointments

Ofwat has appointed Iain Coucher as its new chairman to replace Jonson Cox, effective 1 July. Ofwat has also confirmed its interim CEO, David Black as a permanent appointment.

7.0 Capital expenditure

Net capital investment for 2021/22 is £96.8 million, of which £96.5 million relates to wholesale activity. The remaining £0.3 million relates to investment in our IT systems to support customer billing, collection and debt management.

2021/22 wholesale capital expenditure:

- £18.0 million (19 per cent) of investment has been made in the development of new assets and the enhancement of existing assets, including management of the supply demand balance and the company's legal undertakings with respect to drinking water quality standards.
- £23.1 million (24 per cent) relates to new mains and boosters on housing development and supporting infrastructure.

- £13.6 million (14 per cent) 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.

- £41.8 million (43 per cent) 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.

8.0 Water quality

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. These are also used by Ofwat to assess asset performance.

The company's overall Drinking Water Quality performance, as measured using the DWI's key performance indicator, the Compliance Risk Index (CRI), which assesses performance across all final water samples has improved year on year from 3.4 in calendar year 2018 to 1.21 in 2021 and is now significantly below the industry average of 3.56 for 2021. We have continued to drive improvements in performance across all of our assets through a combination of targeted investment and process optimisation.

The Event Risk Index (ERI) monitors how we proactively reduce the risk of water quality incidents across the supply network, including within customer properties. Our ERI result for the year was 20.5, well below the industry average of 535 as a result of targeted investment and process optimisation at our treatment works and improved planning and risk assessment approach for our network operations.

These results are based on 214,674 tests measured against EU and UK mandatory standards.

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

9.0 Outsourcing

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

- Call for competition (Find a Tender).
- 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 |
|----------------|--|----------------|
| Atkins | Consultancy Services Framework | £56,000,000 |
| Vauxhall | Commercial Vehicles | £4,200,000 |
| AVK | Couplings, Clamps, Flange Adaptors, Underpressure Tees | £2,400,000 |
| Kings Security | Man Guarding Services | £2,000,000 |
| Wolseley | Chamber Sections | £1,900,000 |
| Kebrell | Bolt Sets | £1,600,000 |
| Ford | Commercial Vehicles | £1,000,000 |

Tenders in preparation and/or issued include:

| Tenders in hand | Estimated contract value |
|---|--------------------------|
| Green Energy Power Purchasing Agreement | £10,000,000 |
| IT Cloud Services Provider | £8,000,000 |
| Sludge Removal Services | £8,000,000 |
| Leakage Detection Services | £7,500,000 |
| Bill Print | £5,000,000 |
| PAC 18% | £3,900,000 |
| Building Maintenance | £2,000,000 |
| Boundary Boxes | £1,400,000 |
| Clothing, PPE & Consumables | £1,400,000 |

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.

General overview and business update continued

10.0 Financing

The group had strong liquidity with £11.4 million on the balance sheet at the year end and a further £125 million available to draw down on the authorised credit facility.

Authorised Credit Facility

In September 2021, we renewed the Authorised Credit Facility for a further five years and increased the size of the facility from £90 million to £125 million. The facility is undrawn as of the financial year end.

Liquidity facilities

The DSR and O&M facilities were renewed in June 2021 for the period to June 2022. The DSR liquidity facility has a commitment of £38 million and the O&M facility has a commitment of £22 million.

Refinancing process

A new £50 million 14 year USPP loan was drawn on 2 December 2021. The proceeds funded the repayment of drawings on the Authorised Credit Facility.

SONIA migration

All external LIBOR-linked loans have been successfully transitioned to SONIA. This follows confirmation from the Financial Conduct Authority that all LIBOR settings will either cease to be provided by any administrator or no longer be representative immediately after 31 December 2021. The overall commercial terms of the facilities are unchanged.

11.0 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 issued its credit opinion in November 2021. S&P issued its most recent credit opinion in December 2021. There was no change in South East Water's rating from either rating agency.

| | Moody's | S&P |
|---------------|---------|-----|
| Credit rating | Baa2 | BBB |

12.0 Surplus

The SEWH Board approved £5.2 million of dividends to Hastings Water (UK) Limited in the financial year.

13.0 Board / management changes

South East Water has appointed Chris Train OBE as a new independent non-executive director and Chair. Chris Train succeeded Nick Salmon as independent Chair on 1 April. Nick joined the Board as Chairman in April 2015 and is stepping down as Chair as part of the regular renewal of independent non-executive directors on the Board.

Chris has extensive experience in the utilities industry having been Chief Executive Officer of Cadent Gas Limited and is at present Executive and Senior Adviser at CT Energy. Chris is an experienced Executive and Board Director and is currently Non-Executive Chair of Clean Power Hydrogen and a Non-Executive Director of The Nuclear Decommissioning Authority.

Another change to the Board of South East Water is the arrival of Mark McArdle from H.R.L. Morrison & Co as the UTA shareholder representative, replacing Rachel Drew who will remain a director of HDF (UK) Holdings Ltd, the group's ultimate parent company in the UK.

Anne-Noëlle Le Gal has replaced Marissa Szczepaniak as a shareholder representative on the Board.

The South East Water Board of directors is as follows:

South East Water Limited

| | |
|----------------------|---|
| N Salmon | Independent Non-Executive Chair (resigned 31 March 2022) |
| C Train | Independent Non-Executive Chair (appointed 24 February 2022) |
| D Hinton | Chief Executive Officer* |
| A Farmer | Chief Financial Officer* |
| J Barnes | Independent Non-Executive Director |
| C Pronto | Independent Non-Executive Director |
| C Girling | Independent Non-Executive Director |
| M Szczepaniak | Non-Executive Director (resigned 18 June 2021)** |
| A Le Gal | Non-Executive Director (appointed 18 June 2021)** |
| R Drew | Non-Executive Director (resigned 09 February 2022)*** |
| M McArdle | Non-Executive Director (appointed 09 February 2022)*** |

The Company Secretary is Nicolas Truillet

South East Water (Holdings) Limited

| | |
|----------------------|--|
| M Szczepaniak | Non-Executive Director (resigned 19 June 2021)** |
| A Le Gal | Non-Executive Director (appointed 19 June 2021)** |
| R Drew | Non-Executive Director (resigned 17 March 2022)*** |
| M McArdle | Non-Executive Director (appointed 17 March 2022)*** |

South East Water (Finance) Limited

| | |
|----------------------|--|
| D Hinton | Executive Director (appointed 05 March 2021) |
| A Farmer | Executive Director |
| M Szczepaniak | Non-Executive Director (resigned 19 June 2021)** |
| A Le Gal | Non-Executive Director (appointed 19 June 2021)** |
| R Drew | Non-Executive Director (resigned 17 March 2022)*** |
| M McArdle | Non-Executive Director (appointed 17 March 2022)*** |

* Denotes an Executive Director

** Denotes a Vantage appointee

*** Denotes a H.R.L. Morrison & Co. appointee

Ratios

1. Historic

We confirm that in respect of the Calculation Date on 31 March 2022, 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 2022.

| Date | 31-Mar-21 | Calculation date | 31-Mar-23 | 31-Mar-24 | 31-Mar-25 |
|--|-----------------------|-----------------------|-----------------------|-----------------------|-----------------------|
| RAR (at such Calculation Date or, in the case of forward-looking ratios, as at 31 March falling in the relevant Test Period) | 78.4% | 74.6% | 73.4% | 74.8% | 74.6% |
| Test Period | 1-Apr-20 to 31-Mar-21 | 1-Apr-21 to 31-Mar-22 | 1-Apr-22 to 31-Mar-23 | 1-Apr-23 to 31-Mar-24 | 1-Apr-24 to 31-Mar-25 |
| ICR | 3.55 x | 3.96 x | 2.92 x | 3.04 x | 3.02 x |
| Adjusted ICR | 3.55 x | 3.96 x | 2.92 x | 3.04 x | 3.02 x |
| Average Adjusted ICR | 3.45 x | 3.27 x | 2.99 x | 2.99 x | 2.99 x |
| Conformed Adjusted ICR | 1.59 x | 1.97 x | 1.19 x | 1.31 x | 1.30 x |
| Conformed Average Adjusted ICR | 1.56 x | 1.46 x | 1.27 x | 1.27 x | 1.27 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.

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-21 | Calculation date | 31-Mar-23 | 31-Mar-24 | 31-Mar-25 |
|---------------------------------------|-----------|------------------|-----------|-----------|-----------|
| Senior Debt (Closing Balances) | | | | | |
| Finance Leases | 3.9 | 1.0 | 3.2 | 2.9 | 2.6 |
| Debentures | 1.0 | 3.5 | 1.0 | 1.0 | 1.0 |
| Nominal Debt | 166.0 | 166.0 | 166.0 | 166.0 | 166.0 |
| Index Linked Bonds | 177.4 | 190.9 | 202.5 | 206.4 | 211.5 |
| Fixed Rate Loan Notes | 175.0 | 225.0 | 225.0 | 225.0 | 225.0 |
| Variable rate loans | 120.0 | 120.0 | 120.0 | 120.0 | 120.0 |
| Index Linked Loans | 121.9 | 129.7 | 134.6 | 146.6 | 149.4 |
| Index Linked Loans | 280.2 | 291.0 | 317.0 | 323.2 | 331.2 |
| Authorised Credit Facility | 80.0 | 0.0 | 40.5 | 60.8 | 60.8 |
| Total Senior Debt Closing Balance | 1125.4 | 1127.1 | 1209.8 | 1251.9 | 1267.5 |
| Less: Cash Balance | (41.7) | (14.5) | (7.1) | (10.0) | (4.8) |
| Senior Net Indebtedness | 1083.7 | 1112.6 | 1202.7 | 1241.9 | 1262.7 |
| Regulatory Capital Value | 1382.0 | 1490.9 | 1637.9 | 1659.2 | 1692.7 |
| RAR | 78.4% | 74.6% | 73.4% | 74.8% | 74.6% |

b) ICR

| Date | 1-Apr-20 to 31-Mar-21 £m | 1-Apr-21 to 31-Mar-22 £m | 1-Apr-22 to 31-Mar-23 £m | 1-Apr-23 to 31-Mar-24 £m | 1-Apr-24 to 31-Mar-25 £m |
|---|--------------------------------|--------------------------------|--------------------------------|--------------------------------|--------------------------------|
| Net Cash Flow | | | | | |
| Net cash flow from operating activities | 119.9 | 135.9 | 122.6 | 135.3 | 137.8 |
| Exceptional items | 0.0 | 0.0 | (1.0) | 0.0 | 0.0 |
| Recoverable VAT | 1.9 | 1.7 | 0.0 | 0.0 | 0.0 |
| Corporation tax paid | 0.1 | 0.1 | 0.0 | 0.0 | 0.0 |
| Pension funding | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Non-appointed | 0.0 | 0.0 | (3.6) | (5.3) | (5.8) |
| Net Cash Flow | 121.9 | 137.6 | 118.0 | 130.0 | 132.0 |
| Senior Debt Interest | | | | | |
| Leases | 0.1 | 0.1 | 0.5 | 0.5 | 0.4 |
| Debentures | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Nominal Debt | 14.7 | 14.7 | 15.7 | 15.7 | 15.7 |
| Variable rate loan facility | 2.1 | 1.6 | 4.5 | 5.7 | 6.3 |
| Index Linked Debt | 17.2 | 17.6 | 19.1 | 20.3 | 20.7 |
| Financial Guarantor fees | 0.3 | 0.6 | 0.6 | 0.6 | 0.6 |
| Senior Debt Interest Payable | 34.5 | 34.7 | 40.5 | 42.8 | 43.7 |
| Interest Receivable | (0.1) | (0.0) | 0.0 | 0.0 | 0.0 |
| Senior Debt Interest | 34.4 | 34.7 | 40.5 | 42.8 | 43.7 |
| ICR | 3.55 x | 3.96 x | 2.92 x | 3.04 x | 3.02 x |

c) Adjusted ICR

| Date | 1-Apr-20 to 31-Mar-21 £m | 1-Apr-21 to 31-Mar-22 £m | 1-Apr-22 to 31-Mar-23 £m | 1-Apr-23 to 31-Mar-24 £m | 1-Apr-24 to 31-Mar-25 £m |
|---|--------------------------------|--------------------------------|--------------------------------|--------------------------------|--------------------------------|
| Net Cash Flow | 121.9 | 137.6 | 118.0 | 130.0 | 132.0 |
| CCD & IRC | | | | | |
| 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 | 121.9 | 137.6 | 118.0 | 130.0 | 132.0 |
| Senior Debt Interest | 34.4 | 34.7 | 40.5 | 42.8 | 43.7 |
| Adjusted ICR | 3.55 x | 3.96 x | 2.92 x | 3.04 x | 3.02 x |

Ratios continued

d) Average Adjusted ICR

| Date | 1-Apr-20 to 31-Mar-21 £m | 1-Apr-21 to 31-Mar-22 £m | 1-Apr-22 to 31-Mar-23 £m | 1-Apr-23 to 31-Mar-24 £m | 1-Apr-24 to 31-Mar-25 £m |
|---|--------------------------------|--------------------------------|--------------------------------|--------------------------------|--------------------------------|
| Net Cash Flow | 121.9 | 137.6 | 118.0 | 130.0 | 132.0 |
| CCD & IRC | | | | | |
| 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 | 121.9 | 137.6 | 118.0 | 130.0 | 132.0 |
| Senior Debt Interest | 34.4 | 34.7 | 40.5 | 42.8 | 43.7 |
| Adjusted ICR | 3.55 x | 3.96 x | 2.92 x | 3.04 x | 3.02 x |
| Average Adjusted ICR | 3.45 x | 3.27 x | 2.99 x | 2.99 x | 2.99 x |

e) Conformed Adjusted ICR

| Date | 1-Apr-20 to 31-Mar-21 £m | 1-Apr-21 to 31-Mar-22 £m | 1-Apr-22 to 31-Mar-23 £m | 1-Apr-23 to 31-Mar-24 £m | 1-Apr-24 to 31-Mar-25 £m |
|---|--------------------------------|--------------------------------|--------------------------------|--------------------------------|--------------------------------|
| Net Cash Flow | 121.9 | 137.6 | 118.0 | 130.0 | 132.0 |
| RCV Depreciation | 51.7 | 55.6 | 58.5 | 59.8 | 61.0 |
| Capitalised IRE | 15.5 | 13.6 | 11.3 | 14.3 | 14.4 |
| Total regulatory depreciation | 67.2 | 69.2 | 69.8 | 74.1 | 75.4 |
| Net Cash Flow after regulatory depreciation | 54.7 | 68.4 | 48.2 | 55.9 | 56.6 |
| Senior Debt Interest | 34.4 | 34.7 | 40.5 | 42.8 | 43.7 |
| Conformed Adjusted ICR | 1.59 x | 1.97 x | 1.19 x | 1.31 x | 1.30 x |

f) Conformed Average Adjusted ICR

| Date | 1-Apr-20 to 31-Mar-21 £m | 1-Apr-21 to 31-Mar-22 £m | 1-Apr-22 to 31-Mar-23 £m | 1-Apr-23 to 31-Mar-24 £m | 1-Apr-24 to 31-Mar-25 £m |
|---|--------------------------------|--------------------------------|--------------------------------|--------------------------------|--------------------------------|
| Net Cash Flow | 121.9 | 137.6 | 118.0 | 130.0 | 132.0 |
| RCV Depreciation | 51.7 | 55.6 | 58.5 | 59.8 | 61.0 |
| Capitalised IRE | 15.5 | 13.6 | 11.3 | 14.3 | 14.4 |
| Total regulatory depreciation | 67.2 | 69.2 | 69.8 | 74.1 | 75.4 |
| Net Cash Flow after regulatory depreciation | 54.7 | 68.4 | 48.2 | 55.9 | 56.6 |
| Senior Debt Interest | 34.4 | 34.7 | 40.5 | 42.8 | 43.7 |
| Conformed Adjusted ICR | 1.59 x | 1.97 x | 1.19 x | 1.31 x | 1.30 x |
| Conformed Average Adjusted ICR | 1.56 x | 1.46 x | 1.27 x | 1.27 x | 1.27 x |

4. We certify that for the period to 31 March 2022 the Annual Finance Charge is £35.3 million.

5. Annual Finance Charge calculation:



| Date | 31 March 2022 £m |
|--------------------------------------|---------------------|
| Senior Debt Interest | |
| Finance Leases | 0.1 |
| Debentures | 0.0 |
| Nominal Debt (£166m) | 9.3 |
| Fixed rate loan notes | 5.8 |
| Variable rate loan | 1.7 |
| Synthetic Index Linked Bonds (£200m) | 0.0 |
| Index Linked Bonds (£130m) | 4.7 |
| Index linked loans (USS) | 3.0 |
| Index Linked Loans | 10.1 |
| Working Capital Facility | 0.3 |
| Ambac fee | 0.3 |
| Net Cash Flow | 35.3 |
| Less: interest earned | (0.0) |
| 12 Months Total | 35.3 |

Total payments into the DSR Accounts for the period to 31 March 2022 were £38.9 million.

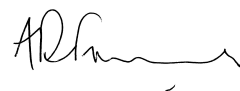

6. We also confirm that:

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

Appendix

Financial statements

South East Water (Holdings) Limited

Consolidated profit & loss account for the period ended 31 March 2022

| | Companies £'m | Eliminations £'m | Group £'m |
|---|------------------|---------------------|--------------|
| Turnover | 251.3 | - | 251.3 |
| Operating costs | (188.5) | - | (188.5) |
| Profit/(loss) on disposal of fixed assets | 0.9 | - | 0.9 |
| Other operating income | 21.9 | - | 21.9 |
| Operating profit | 83.8 | - | 83.8 |
| Income from investments | 9.0 | (9.0) | - |
| Interest receivable – group | - | - | - |
| Interest receivable – other | 0.0 | - | 0.0 |
| Interest payable – group | (5.0) | - | (5.0) |
| Interest payable – other | (67.6) | - | (67.6) |
| Return on pension scheme assets | 0.7 | - | 0.7 |
| Profit on sale of intangible assets | - | - | - |
| Profit on ordinary activities before taxation | 21.0 | (9.0) | 12.0 |
| Tax (charge)/credit on profit on ordinary activities | (44.9) | - | (44.9) |
| Profit on ordinary activities after taxation | (24.0) | (9.0) | (33.0) |
| Dividends | (14.2) | 9.0 | (5.2) |
| STRGL – pension | (38.2) | - | (38.2) |
| | 14.7 | - | 14.7 |
| Profit/(loss) for period taken to p&l reserves | (23.5) | - | (23.5) |

South East Water (Holdings) Limited

Consolidated balance sheet as at 31 March 2022

| | Companies £'m | Eliminations £'m | Group £'m |
|---|------------------|---------------------|--------------|
| Tangible assets | 1,697.4 | - | 1,697.4 |
| Investments | 361.4 | (361.4) | - |
| Net Current (liabilities)/assets | (17.4) | - | (17.4) |
| Creditors: amounts falling due after more than one year | (241.3) | - | (241.3) |
| Current asset investments | - | - | - |
| Cash and cash equivalents: | | | |
| Current accounts | 11.4 | - | 11.4 |
| DSR | 0.1 | - | 0.1 |
| O&M | 1.0 | - | 1.0 |
| First loss account | 2.0 | - | 2.0 |
| Financing liabilities | | | |
| Intra group loan creditors | (486.6) | 486.6 | - |
| Intra group loan debtors | 486.6 | (486.6) | - |
| Other HDF group loans | (82.2) | - | (82.2) |
| Debentures | (1.0) | - | (1.0) |
| Finance leases | (3.5) | - | (3.5) |
| Bonds | (296.0) | - | (296.0) |
| Indexation | (60.9) | - | (60.9) |
| Artesian loans | (269.0) | - | (269.0) |
| Indexation | (151.7) | - | (151.7) |
| Loan notes | (225.0) | - | (225.0) |
| Variable rate loan | (120.0) | - | (120.0) |
| Unamortised costs | 6.3 | - | 6.3 |
| Bank loans | - | - | - |
| Net pension liability | 54.5 | - | 54.5 |
| Net assets | 666.2 | (361.4) | 304.8 |
| Capital and reserves | | | |
| Called up share capital | 194.7 | (49.3) | 145.4 |
| Revaluation reserve | 217.9 | - | 217.9 |
| Profit and loss account b/fwd. | 272.5 | (312.1) | (39.6) |
| Profit for period | (18.9) | - | (18.9) |
| Capital employed | 666.2 | (361.4) | 304.8 |

South East Water (Holdings) Limited

Consolidated movement in the profit and loss reserve for the period ended 31 March 2022

| | Companies £'m | Eliminations £'m | Group £'m |
|---------------------------|------------------|---------------------|--------------|
| At 1 April 2021 | 272.5 | (312.1) | (39.6) |
| Profit for the year | (24.0) | (9.0) | (33.0) |
| Pension scheme in STRGL | 14.7 | - | 14.7 |
| Dividends | (14.2) | 9.0 | (5.2) |
| Movement through reserves | 4.6 | - | 4.6 |
| | (18.9) | - | (18.9) |
| At 31 March 2022 | 253.6 | (312.1) | (58.5) |