Registered number: 07516930 (England & Wales)

Thames Water (Kemble) Finance Plc

Interim report and financial statements

For the six month period ended 30 September 2020

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Directors' Report

Introduction

This report comprises a business and financial overview of Thames Water (Kemble) Finance Plc ("the Company") for the six month period ended 30 September 2020 and constitutes unaudited key financial data and a narrative review of performance over this period. This report has been prepared solely to provide additional information to the Company's shareholders to assess the performance and future outlook of the Company, and should not be relied upon by any other party or for any other purpose.

The Company is party to various financing agreements which require the Company to prepare unaudited financial statements. This interim report and financial overview has been prepared to meet these requirements and has been approved by the Company's Board as fairly representing the Company's financial position as at 30 September 2020 and its performance for the six month period ended 30 September 2020.

Business review

The Company was established to make certain financing arrangements on behalf of its immediate parent undertaking Kemble Water Finance Limited ("KWF"). As at 30 September 2020, the Company had raised a total of £175.0 million of external debt which it has subsequently on-lent under mirrored terms to KWF along with an additional annual margin of £10,000. The Directors consider the ultimate parent undertaking to be Kemble Water Holdings Limited ("KWH") and the largest group consolidating the Company is the Kemble Water Holdings Limited Group ("the Group"). This remains unchanged from the previous year.

During the period, the Company raised no new debt (30 September 2019: £nil). At 30 September 2020, the Company had in issue £175.0 million of listed debt (31 March 2020: £175.0 million) in the form of bonds.

All bonds issued by the Company are rated B1 by Moody's with a stable outlook (30 September 2019: B1 with a negative outlook). On 9th April 2020, Fitch downgraded the Company's senior secured debt Long-Term Rating to B+ with negative outlook (30 September 2019: BB- with a credit watch negative). The Directors do not consider that the change in rating reflects a material change in credit risk or significantly impacts the ability of the Company to issue debt via the capital markets.

Principal risks and uncertainties

During the six months ended 30 September 2020, the principal risks and uncertainties that were disclosed in the Annual Report and Financial Statements for the year ended 31 March 2020 remain largely unchanged.

Going Concern

The Directors have assessed the Company's ability to continue as a going concern recognising it is a special purpose financing entity with no business operations other than raising external funding for its Guarantor, Kemble Water Finance Limited ("KWF"). As such the Company is wholly reliant on KWF as a source of income. KWF is a holding company with no material, direct business operations and is therefore mainly dependent on its operating subsidiary, Thames Water Utilities Limited Group ("TWUL Group") to generate the funds necessary for both TW(K)F and KWF to meet their respective financial obligations.

Given the dependency on TWUL Group, the Directors have considered the going concern assessment made by the TWUL Group directors as well as the actions taken by TWUL Group post the balance sheet date of 30 September 2020. The section below, "Summary of TWUL Group going concern assessment" outlines this assessment where the TWUL Group Board has concluded it appropriate to prepare the financial statements for TWUL Group on a going concern basis. Further details of this assessment and the post balance sheet events are contained within the TWUL Group interim report for 2020/21, copies of which may be obtained from the Company Secretary's Office at The Company Secretarial Department, Thames Water Group, Clearwater Court, Vastern Road, Reading, Berkshire, RG1 8DB.

Summary of TWUL Group going concern assessment

TWUL is the monopoly provider of the public water supply and wastewater treatment to areas including most of London and the Thames Valley. The regulatory regime in England and Wales provides water companies with stable and predictable revenues over an Asset Management Plan (AMP). The framework ensures protection against reduced revenues arising from lower consumption and the regulatory recovery mechanisms ensure that the economic value impact is generally immaterial. In addition, the impact of Covid-19 on the TWUL Group's ability to provide essential water and wastewater services has been mitigated through the Government's recognition that these services are essential and the TWUL Group's quick response to enable effective working practices in the challenging operational environment.

The TWUL Group's liquidity position and cashflow projections are closely monitored and updated regularly. Mitigating measures are also continually reviewed and actioned where appropriate. The potential impact of Covid-19 on the TWUL Group's financial performance has been assessed with a particular focus on operational cashflows and capital expenditure. Lower operational cashflows are expected mainly due to deferred payments and increases in bad debt from household customers and lower billable volumes in the non-household sector due to reduced consumption.

Directors' Report (continued)

Going Concern

Summary of TWUL Group going concern assessment (continued)

Various scenarios have been assessed, all of which show the TWUL Group having significant liquidity headroom. A severe but plausible downside case has been developed which assumes a prolonged period of lockdown due to Covid-19 in excess of the lockdown measures announced by the UK Government on 31 October 2020. In this scenario, operational cashflows would be temporarily lower in 2020/21, resulting in a TWUL Group Trigger Event, but would recover in subsequent years. Despite this being an undesirable outcome, the TWUL Group has material headroom against the Event of Default threshold, as such this does not impact the going concern assumption for the reasons outlined below.

The main consequences of a TWUL Group Trigger Event include, but are not limited to, a cash lockup and a prohibition from incurring additional debt other than utilisations from the existing bank facilities. The TWUL Directors do not consider this scenario to cause a material uncertainty with regards to the going concern assumption. The Trigger Event is a feature of the TWUL Group's Whole Business Securitisation ("WBS") structure and acts as an early warning sign that is structured to provide additional creditor protections. It is designed to maintain the TWUL Group's creditworthiness as such, it does not affect the TWUL Group's continued access to its significant existing bank facilities nor would it disrupt the TWUL Group's ability to trade. The cash lockup preserves the value of the TWUL Group which is in the interest of TWUL Group creditors and customers. Whilst prohibited from accessing new funding, the TWUL Group has significant bank facilities which are sufficient to fund its programme and meet its obligations for the duration of the Trigger Event.

However, various remedial actions have been identified and could be implemented to avoid / reduce the occurrence of a TWUL Group Trigger Event if such a scenario were to materialise.

Conclusion

The conclusion from the TWUL Group Board helps to underpin the Directors' belief that TW(K)F has the ability to meet its financial obligations over the assessment period. To provide additional comfort, the Directors have also sought support from Kemble Water Holdings Limited ("KWH"), the ultimate parent of TW(K)F. KWH has confirmed that it will continue to provide support to TW(K)F, to enable the Company to meet its liabilities as they fall due for a period of at least twelve months from the date of signing of the condensed interim financial statements.

The Directors have assessed the Company's liquidity position and ability to comply with its financial covenants which differ from those of TWUL Group. The financial covenants for TW(K)F take into account the effects of the aggregate net debt outstanding as well as the operational cashflows and profits from KWF and its subsidiaries on a consolidated basis. The main relevant subsidiaries include TWUL Group and TW(K)F. In addition to the cash balances available to KWF, the guarantor of the Company's debt, KWF also has in place a committed undrawn working capital facility which can fund at least 18 months of interest payments on the external debt held by KWF and TW(K)F. The Directors have considered projected cashflows and forecast compliance with the financial covenants during the assessment period.

A severe but plausible downside case has been developed which assumes a prolonged period of lockdown which would result in operational cashflows at TWUL Group being temporarily lower in 2020/21 due to Covid-19. Under this scenario, a Trigger Event would take place at TWUL Group and it would be prohibited from paying out distributions for the duration of the Trigger Event. Such distributions would typically be used to service the interest payments on the external debt held by KWF and TW(K)F. The Directors believe that the sources of liquidity mentioned above are sufficient to allow KWF and TW(K)F to service the external debt interest for the duration of the cash lockup at TWUL Group.

Taking into consideration the above factors, the Board is satisfied that TW(K)F has adequate resources for a period of at least 12 months from the date of approval of the condensed interim financial statements to continue operations and discharge the Company's obligations as they fall due. For this reason, the Board considers it is appropriate to adopt the going concern basis in preparing the financial statements.

Financial review

The key measures of financial performance of the Company are detailed below, all of which are used by the Board of Directors in assessing performance.

	Six month period ended 30 September 2020	Six month period ended 30 September 2019
Net finance income (£'000)	**5**	5
Profit on ordinary activities before taxation (£'000)	**5**	-
Profit/(loss) on ordinary activities after taxation (£'000)	**4**	(1)
Net assets (£'000)	**120**	112
Credit rating*	**Baa2 Stable**	Baa1 negative

* Representing the consolidated Corporate Family Rating assigned by Moody's to Thames Water Utilities Limited.

Directors' Report (continued)

Net finance income

Net finance income comprises of finance income offset by finance expense. Finance income represents interest receivable on external borrowings that are lent on identical terms to KWF, with an additional £10,000 annual margin (30 September 2019: annual margin £10,000).

Finance expense represents interest payable on external borrowings. As at 30 September 2020, the Company had raised a total of £175.0 million of external debt.

Credit rating

In July 2020, Moody's completed its periodic review and re-affirmed their March 2020 assignment of Thames Water Utilities Limited's Corporate Family Rating ("CFR") as Baa2 with stable outlook (30 September 2019: Baa1 with negative outlook). Moody's also re-affirmed their March 2020 assignment of Thames Water Utilities Limited's senior secured (Class A) debt rating as Baa1 with stable outlook (30 September 2019: A3 with negative outlook) and subordinated (Class B) debt rating as Ba1 with stable outlook (30 September 2019: Baa3 with negative outlook).

In February 2020, S&P affirmed Thames Water Utilities Limited's credit rating of BBB+ and BBB- (2019: BBB+ & BBB-) in respect of senior secured (Class A) debt and subordinated (Class B) debt respectively, with negative outlook (30 September 2019: negative outlook).

These investment grade credit ratings continue to enable Thames Water to access efficiently priced debt to fund the investment programme, which is an important factor in keeping bills affordable for our customers.

Separately during March 2020, Moody's concluded their review of ratings for the Group, moving KWF guaranteed debt from negative to stable outlook (still rated B1). During April 2020 Fitch downgraded KWF's rating from BB- to B+ (negative outlook). The directors do not consider that the change in rating reflects a material change in credit risk or impacts the ability of KWF or the Company to issue debt via the capital markets.

Dividends

In the six months to 30 September 2020 the Company has not paid any dividends (30 September 2019: £nil) and the Directors do not recommend the payment of a dividend (30 September 2019: £nil).

Directors

The Directors who held office during the period ended 30 September 2020 and at the date of this report were:

T Bolton
D Manuelpillai
M Bamford

During the period under review, none of the Directors had significant contracts with the Company or any other body corporate other than their contracts of service (30 September 2019: none).

T Bolton
Director

Clearwater Court
Vastern Road
Reading
Berkshire
RG1 8DB

30 November 2020

Condensed income statement

For the six month period ended

	30 September 2020 £'000	30 September 2019 £'000
Operating expenses	**-**	(5)
Operating loss	**-**	(5)
Finance income	**5,305**	5,269
Finance expense	**(5,300)**	(5,264)
Profit on ordinary activities before taxation	**5**	-
Taxation on profit on ordinary activities	**(1)**	(1)
Profit/(loss) on ordinary activities after taxation	**4**	(1)

The Company's activities above are derived from continuing activities.

The Company has no other recognised gains or losses in either period and therefore no separate statement of comprehensive income has been presented.

Condensed statement of financial position

As at

	30 September 2020 £'000	31 March 2020 £'000
Non-current assets		
Intercompany loans receivable	**174,443**	174,254
Other financial assets	**37**	37
	174,480	174,291
Current assets		
Intercompany loans receivable	**2,170**	2,200
Other financial assets	**96**	91
	2,266	2,291
Current liabilities		
Borrowings	**(2,170)**	(2,200)
Group relief payable	**(13)**	(12)
	(2,183)	(2,212)
Net current assets	**83**	79
Non-current liabilities		
Borrowings	**(174,443)**	(174,254)
	(174,443)	(174,254)
Net assets	**120**	116
Equity		
Called up share capital	**50**	50
Retained earnings	**70**	66
Total equity	**120**	116

Condensed statement of changes in equity

For the six month period ended

	Called up share capital £'000	Retained earnings £'000	**Total equity/ (deficit) £'000**
1 April 2019	50	63	**113**
Loss on ordinary activities after taxation	-	(1)	**(1)**
30 September 2019	50	62	**112**
Profit on ordinary activities after taxation	-	4	**4**
31 March 2020	50	66	**116**
Profit on ordinary activities after taxation	-	4	**4**
30 September 2020	50	70	**120**

Condensed statement of cash flows

For the six month period ended

	30 September 2020 £'000	30 September 2019 £'000
Cash flows from operating activities		
Profit/(loss) on ordinary activities after taxation	**4**	(1)
Less finance income	**(5,305)**	(5,269)
Add finance expense	**5,300**	5,264
Add tax charge	**1**	1
Net cash generated/(used in) by operating activities	**-**	(5)
Investing activities		
Interest received	**5,141**	20,619
Loans repaid by group companies	**-**	399,310
Net cash generated by investing activities	**5,141**	419,929
Financing activities		
Repayment of borrowings	**-**	(399,310)
Interest paid	**(5,141)**	(20,614)
Net cash outflow used in financing activities	**(5,141)**	(419,924)
Net movement in cash and cash equivalents	**-**	-
Cash and cash equivalents at beginning of year	**-**	-
Cash and cash equivalents at end of year	**-**	-

Notes to the condensed financial statements

1. Post balance sheet events

In November 2020, the Company issued £250.0 million Notes with a maturity of 2026. The proceeds were on lent to KWF at a margin of 0.10%. The Company received £62.5 million plus accrued interest from KWF towards repayment of £59.9 million principal of the £175.0 million intercompany loan at a re-purchase price of 104.5%. These proceeds were used by the Company to repay £59.9 million principal of the £175.0 million external Notes due in 2022 at a re-purchase price of 104.5% plus accrued interest.