

MOODY'S

RATINGS

Rating Action: Moody's Ratings deems Thames Water's restructuring to be a distressed exchange

25 Feb 2025

London, February 25, 2025 -- Moody's Ratings (Moody's) has today downgraded Thames Water Utilities Ltd.'s (Thames Water) Probability of Default (PDR) rating to D-PD from Ca-PD. The rating action coincides with the effective date of Thames Water's restructuring plan, as announced by the company on 21 February 2025[1].

We have additionally affirmed Thames Water Utilities Ltd.'s Corporate Family Rating (CFR) at Caa3, and Thames Water Utilities Finance Plc's backed senior secured debt (referred to as Class A under its finance documents) ratings at Caa3, backed subordinate debt (referred to as Class B under its finance documents) rating at C, and backed senior secured and subordinate MTN programme ratings at (P)Caa3 and (P)C respectively; the outlook on all entities remains stable.

RATINGS RATIONALE

RATIONALE FOR PROBABILITY OF DEFAULT RATING

The restructuring plan extends the final maturities and scheduled amortization payments of all existing debt obligations by two years, as well as structurally subordinating all existing creditors behind a soon-to-be-issued £1.5 billion super senior tranche (with a further £1.5 billion accessible later this year).

We regard the restructuring plan to be a distressed exchange, and hence a default under our definitions. An amendment or extension of credit terms that results in a loss relative to the original promise to pay constitutes a distressed exchange.

The effective date of the restructuring plan follows the sanctioning of the restructuring plan by the High Court on 18 February 2025[2]. Certain dissenting creditors have appealed the decision, with an appeal hearing due to conclude by 13 March 2025. All actions taken by Thames Water to implement the restructuring plan prior to the conclusion of the appeal must be reversible in case the appeal is successful.

In a few business days, we will upgrade the PDR to Ca-PD, consistent with the probability of default expectation embedded in Thames Water Utilities Ltd.'s CFR of Caa3.

RATIONALE FOR ALL OTHER RATINGS

Thames Water's CFR reflects the challenges in Ofwat's final determination for the regulatory period running from 1 April 2025 to 30 March 2030 as well as our expectation of haircuts for existing creditors through either a further restructuring process within the next 12 months or as part of a special administration process. Today's restructuring and the upcoming super senior issuance provides the company with emergency liquidity. However, the company will only establish a more sustainable capital structure and funding position after a second debt restructuring, expected to take place later this year and involving the raise of new equity.

Thames Water, along with five other water utilities, has appealed its final determination to the Competition and Markets Authority (CMA) for a redetermination. This is expected to conclude within 12 months of the formal referral by Ofwat.

The senior secured Caa3 rating of the Class A bonds issued by Thames Water's finance subsidiary, in line with the CFR, reflects their senior ranking in the cashflow waterfall and after any enforcement of security. However, it also takes into account additional super-senior obligations, including derivative liabilities with a mark-to-market value of around £1.9 billion (excluding credit value adjustment; £1.3 billion adjusted) at September 2024, as well as the expected issuance of £1.5-3.0 billion to be provided on a super-senior basis, the servicing of which could further reduce cash flows available to service Class A creditors.

The C rating of the Class B bonds reflects our expectation of a heightened expected loss severity for the Class B lenders, given their deeply subordinated position in the cash flow waterfall.

The rating action reflects materially negative financial strategy and risk management risk under our governance considerations and regulatory risk as part of demographic and societal trends under social considerations of our framework for environmental, social and governance risks.

RATING OUTLOOK

Thames Water's outlook is stable reflecting that it will take time to establish a more sustainable capital structure, which will ultimately determine recovery for senior lenders. However, the currently expected recovery rate is unlikely to change in the short term.

FACTORS THAT COULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS

An upgrade of the ratings is unlikely in the near term. However, upward pressure could arise in the medium to long term if there was a substantial deleveraging, either as a result of a significant equity injection or following a debt restructuring process.

Thames Water's ratings, specifically its CFR or senior secured Class A debt ratings, could be downgraded further if creditors incurred more significant losses than embedded within current ratings.

PRINCIPAL METHODOLOGY

The principal methodology used in these ratings was Regulated Water Utilities published in August 2023 and available at <https://ratings.moodys.com/rmc-documents/406788>. Alternatively, please see the Rating Methodologies page on <https://ratings.moodys.com> for a copy of this methodology.

Thames Water is the largest of the ten main water and sewerage companies in England and Wales by both RCV (£20 billion at March 2024) and number of customers served. The company provides drinking water to around nine million customers and sewerage services to around 15 million customers in London and the Thames Valley.

REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found on <https://ratings.moodys.com/rating-definitions>.

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At least one ESG consideration was material to the credit rating action(s) announced and described above. Moody's general principles for assessing environmental, social and governance (ESG) risks in our credit analysis can be found at <https://ratings.moodys.com/rmc-documents/435880>.

The Global Scale Credit Rating(s) discussed in this Credit Rating Announcement was(were) issued by one of Moody's affiliates outside the EU and is(are) endorsed for use in the EU in accordance with the EU CRA Regulation.

REFERENCES/CITATIONS

[1] Thames Water Utilities Ltd. RNS Number: 0862Y 21-Feb-2025

[2] High Court of Justice Re Thames Water Utilities Holdings Ltd Approved Judgement [2025] EWHC 338 (Ch)

Please see <https://ratings.moodys.com> for any updates on changes to the lead rating analyst and to the Moody's legal entity that has issued the rating.

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