ACT LEADING TREASURY PROFESSIONALS

The Association of Corporate Treasurers

# MCT ADVANCED DIPLOMA

# CASE STUDY EXAMINATION

## 07 April 2016 09.30 – 13.00

## Instructions:

Answer **NINE COMPULSORY** questions.

Time allowed: **3 hours + 30 minutes reading time.**

During the reading time you may annotate the examination paper but you may not write in your answer booklet or use your calculator.

- Enter your student number on the answer booklet: **do NOT write your name**
- You must write in blue or black ink and ensure your handwriting is legible.
- Enter the order in which questions are answered in the box provided on the front of the answer booklet.
- Ensure that all additional submissions (if applicable) are attached to the answer booklet by the tag provided and write your student number on all items to be marked.
- Show all your workings and state your assumptions in all questions, as appropriate.

## QUESTION 1

**Required:**

**Review and comment on the main non-financial considerations affecting the credit status of WWC and WWBS.**

**(7 marks)**

## QUESTION 2

**Required:**

**a) Review and comment on the trends in the group's main credit ratios.**

**(4 marks)**

**b) Summarise the main reasons for any differences between the credit ratings of WWC and WWBS and assess their respective credit ratings.**

**(3 marks)**

**(Total 7 marks)**

## QUESTION 3

**Required:**

**a) Looking ahead five years, identify four areas of treasury and corporate finance for the Group Treasury to focus its attention on.**

**Justify your choices and rank them 1 to 4, with 1 being the most important.**

**(8 marks)**

**b) If the non-regulated business (WWBS) was to become significant in size relative to the regulated (WWC), state the commercial and financial arguments for and against separating the two businesses by floating off one of them.**

**(5 marks)**

**c) Assume that it is decided to separate WWC from WWBS by floating off one of them. Which would you chose to float? Explain your choice.**

**(2 marks)**

**d) Explain how you would finance each entity post the separation.**

**(5 marks)**

**(Total 20 marks)**

## QUESTION 4

**Required:**

**Starting with the Cash Generated from Operations over the 5-year period (as per the "UK-Style Cash Flow Statement" in the Financials Appendix 5.0 of the Case Study), summarise the changing pattern of cash uses and identify any emerging issues or problems.**

**(6 marks)**

## QUESTION 5

In addition to the company's recent changes in dividend policy and its proposed £100 million share buy-back, it has been suggested that Waterwise should go even further and cut dividends by half. This would enable a reduction in gearing, and reduce the cash drain to interest payments.

**Required:**

**Assess the pros and cons of the recent, proposed and suggested changes and their implications for capital structure.**

**(10 marks)**

## QUESTION 6

In the regulated water sector Capital expenditure (Capex) and operating expenditure (Opex) projects were previously dealt with separately. Capex projects were undertaken to earn a return on capital while Opex projects were pursued to achieve operating efficiencies. The projects are now considered on a total expenditure basis (Totex) by the company and by the regulator.

**Required:**

**a)** **Set out the essential differences between Opex and Capex, considering both accounting conventions and economic/financial fundamentals.**

**(4 marks)**

**b)** **State your views as to what criteria should be used for appraisal of both Capex and Opex projects, given that the company spends many GBP billions on Totex in each 5-year cycle.**

**(7 marks)**

**c)** **Summarise some of the difficulties in carrying out DCF analysis on both Capex and Opex projects in this industry.**

**(3 marks)**

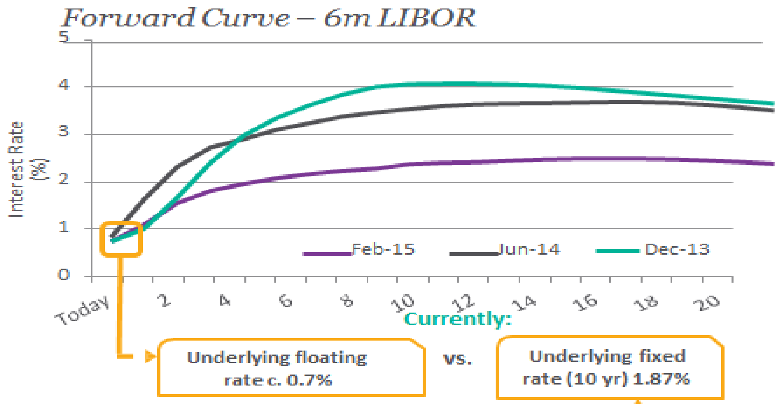
**(Total 14 marks)**

## QUESTION 7

Ofwat's current Asset Management Programme (AMP6) allows for a cost of new debt of 2% in real terms. Rates below that represent a saving on interest cost and rates above represent a cost.

The real interest rate is equal to the nominal rate adjusted downward for inflation. So if nominal rates are 3% and inflation is 1% then the real rate is approximately 2%.

It is February 2015. The graph shows the downward movement of the forward curve for 6m GBP LIBOR for the past few years up to February 2015. The table shows the spot and forward swap rate for tenors out to 12 years also at February 2015.




| GBP | | Underlying swap tenor | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | | 1y | 2y | 3y | 5y | 7y | 10y | 12y |
| | Spot | 0.74 | 0.97 | 1.18 | 1.48 | 1.67 | 1.87 | 1.96 |
| Forward Start | 1y | 1.20 | 1.41 | 1.56 | 1.76 | 1.90 | 2.04 | 2.11 |
| | 2y | 1.62 | 1.75 | 1.84 | 1.97 | 2.07 | 2.18 | 2.23 |
| | 3y | 1.87 | 1.95 | 2.00 | 2.10 | 2.19 | 2.27 | 2.31 |
| | 4y | 2.02 | 2.07 | 2.12 | 2.20 | 2.27 | 2.34 | 2.37 |
| | 5y | 2.12 | 2.17 | 2.21 | 2.29 | 2.34 | 2.39 | 2.42 |

Source: BNP Paribas – Feb 2015

These conditions are the context for the decision about how to hedge interest risk on new debt during and beyond the current AMP6 period.

The Chief Financial Officer has put this item on the next Board Agenda for a decision. You have been asked to prepare a note for discussion with the CFO so that a recommendation can be prepared ahead of the board meeting. This should include consideration as a minimum of loan covenants, current and future likely real rates versus nominal rates, and the feasibility of dynamic hedging for WWC.

**Required:**

**a)** **Draft a note for the CFO listing a range of approaches and explaining the risks associated with each approach.**

**(9 marks)**

**b)** **Recommend and justify a course of action.**

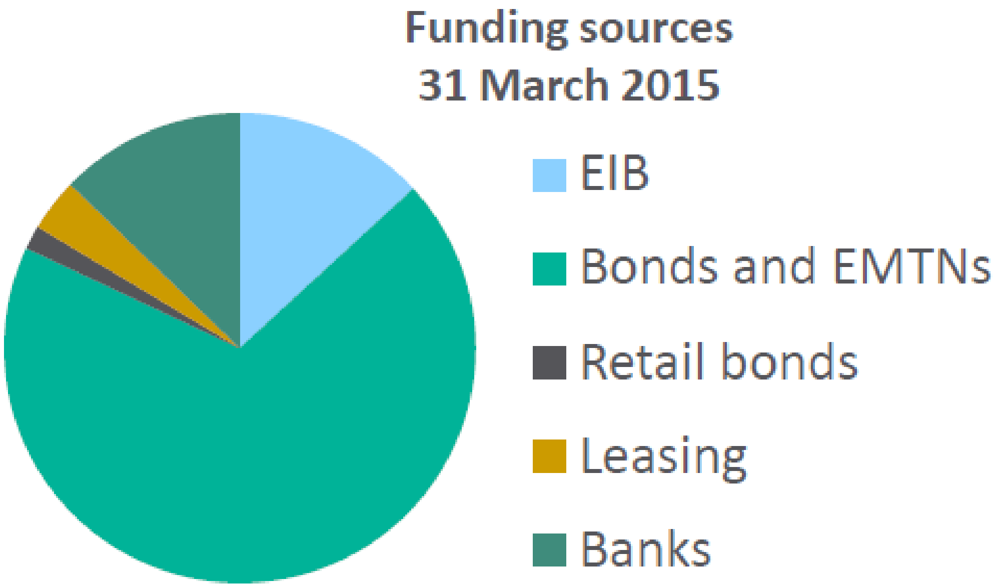
**(3 marks)**

**(Total 12 marks)**

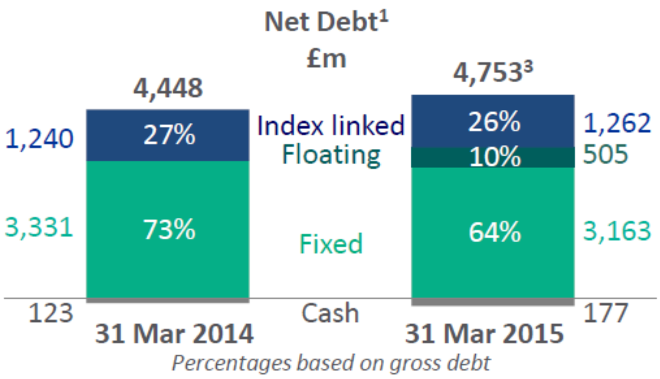
## QUESTION 8

The two charts below show at year-end 2015 (a) Funding sources and (b) Net Debt/Gross Debt and the amounts which are on fixed, floating and index-linked interest rates.    EIB = European Investment Bank

**(a)**




**(b)**




There is a requirement for new finance over the AMP6 five years of circa. £1bn.

So the financing requirement during 2016-2020 is:

| | 2016 £ | 2017 £ | 2018 £ | 2019 £ | 2020 £ | TOTAL £ |
|---|---|---|---|---|---|---|
| Refinance | 475 | 175 | 550 | - | 485 | 1,685 |
| New | 200 | 200 | 200 | 200 | 200 | 1,000 |
| **Total** | **675** | **375** | **750** | **200** | **685** | **2,685** |

At year end 2015 there was £745m headroom on facilities (2014: £500m), comprising £415m RCF undrawns and £330m EIB undrawns.

It is April 2015 and you are beginning to plan how you will execute the AMP6 funding requirement.

**Required:**

**a) List and explain the funding goals which you would want to achieve.**

**(5 marks)**

**b) Along the 5-year timeline, draft a plan to execute the funding, indicating instrument, source, tenor, amount, currency and interest basis.**

**(7 marks)**

**(Total 12 marks)**

## QUESTION 9

It has been decided NOT to float off one or other of WWC & WWBS. Instead the plan is to develop the non-regulated WWBS in order to provide long-term sustainable growth in shareholder value. The majority of that development will be overseas including investment in operating assets on both a wholly owned and Joint Venture basis.

**Required:**

**a) List and explain the principal implications for the management of Group Treasury.**

**(4 marks)**

**b) Propose and justify an outline organisation structure for Group Treasury.**

**(4 marks)**

**c) State and briefly explain the changes you would wish to make to existing foreign exchange policies.**

**(4 marks)**

**(Total 12 marks)**

The Association of Corporate Treasurers

# *MCT ADVANCED DIPLOMA*
# *CASE STUDY*
# *BACKGROUND INFORMATION*

## Based on Waterwise

## April 2016

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# 1.0 INTRODUCTION

## 1.1 Group Overview

Waterwise plc (WWplc) provides clean water and waste water services in the UK and internationally through its regulated and non-regulated businesses – Waterwise Company and Waterwise Business Services respectively. The group has 7,398 employees.

| **Summary Financials** | **2014 GBPm** | **2015 GBPm** |
|---|---|---|
| Turnover | 1,756.7 | 1,801.3 |
| EBIT | 508.8 | 521.6 |
| PAT | 471.8 | 115.5 |
| Gross debt | 4,622.1 | 4,926.7 |
| Net debt | 4,498.9 | 4,750.0 |
| Shareholders' funds | 1,090.1 | 823.3 |
| Average market cap. | 4,540.6 | 4,804.6 |

Waterwise Company (WWC) is one of 10 regulated water and sewerage companies in England and Wales with 3.3 million households and business customers. WWC's turnover is £1,581m with 5,181 employees.

Waterwise Business Services (WWBS) provides contract services to community, municipal, industrial and government clients for the design, build and operation of water and waste water facilities and networks in the UK and US. WWBS also has a renewable energy business using wind turbines, hydro power and anaerobic digestion of crops and food waste, with plans to add solar power as a fifth source of energy generation. WWBS turnover is £216m with 1,853 employees.

A new Chief Executive has been in place for a year and there is also a new Chief Financial Officer. The strategy is to drive growth by achieving operational excellence and continuous innovation in regulated markets and by developing new water markets and green energy operations in non-regulated markets. Analysts have commented that the business re-structuring and cultural change implemented by management, characterised as "embedding commerciality", are clearly paying off.

The Asset Management Programme (AMP6) for the next five years has been determined for WWC by OFWAT, the sector regulator and agreed by the company. This sets the parameters for the value which WWC must provide for its customers in terms of pricing and service and for the return on assets which WWC can realise, depending on how successful it is in achieving efficiencies to which it has committed.

WWBS is positioning for growth in non-regulated water and waste water operations and in renewable energy development.

| 2015 | WWC | WWBS | WWplc * |
|---|---|---|---|
| Turnover | £1581.2m | £216.3m | £1801.3m |
| PBIT + Exceptionals | £539.0m | £9.7m | £521.7m |
| PAT | - | - | £115.5m |
| Employees @ y/e | 5,181 | 1,873 | 7,398 |
| Geography | England | UK, US, Europe | - |

* WWplc numbers include Group adjustments.

## 1.2 Group Governance

WWplc and WWC are distinct legal entities: WWplc being a listed company and WWC its regulated subsidiary.

The Board Directors of WWplc are also the Board Directors of WWC. This structure was introduced in 2007 to ensure that the highest standards of corporate governance are applied at the subsidiary level and also to promote greater visibility and supervision of the regulated subsidiary by WWplc.

WWBS is a subsidiary within WWplc. Subsidiary company boards are required to be managed scrupulously with respect for legal, fiscal and administrative matters. In particular, the relationships between WWC and other businesses such as WWBS are monitored and controlled to ensure that obligations under competition law and regulatory requirements are complied with in respect of all transactions between or with third parties.

# 2.0 BUSINESS PROFILE & ANALYSIS

## 2.1 The Business Model: Regulated-Waterwise Company

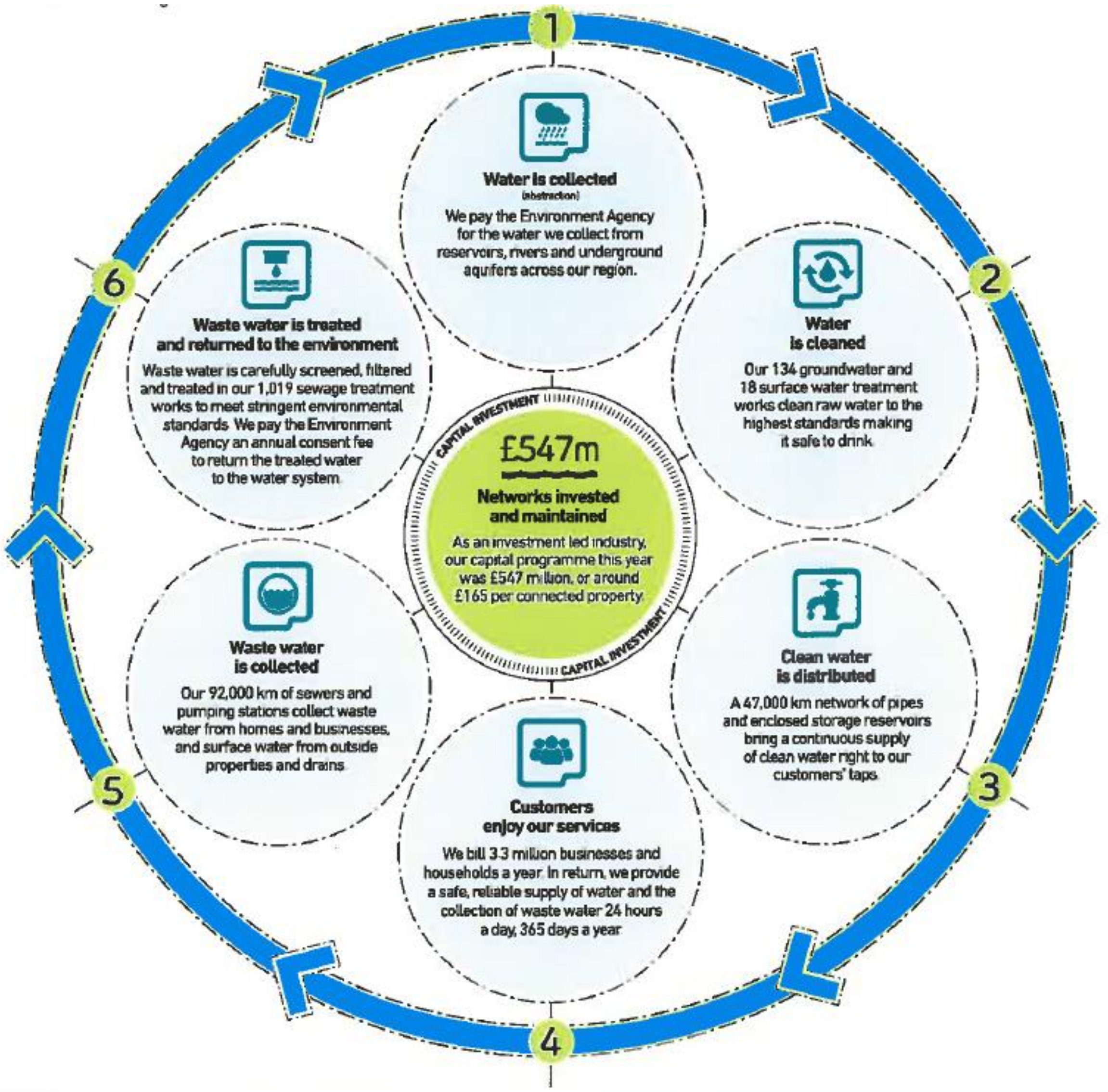
The following sections articulating the company's strategy have been extracted from company presentations.

Waterwise Company is a regulated business. We work within five year planning cycles, with customer prices set by our economic regulator, Ofwat. This allows us to fund our investment programme and cover an efficient level of operating costs.

We are also subject to regulation by two quality regulators – the Drinking Water Inspectorate and the Environment Agency.

Our prices and asset base are adjusted by RPI inflation each year. In certain circumstances we can ask for prices to be reviewed within the five-year period due to costs associated with 'notified items' or 'relevant changes of circumstance'. Customer bad debt and the adoption of private drains and sewers (PDaS) are included in these categories for the current five year period. Waterwise has absorbed the costs associated with PDaS and has not sought to review prices for this reason during 2010–2015.

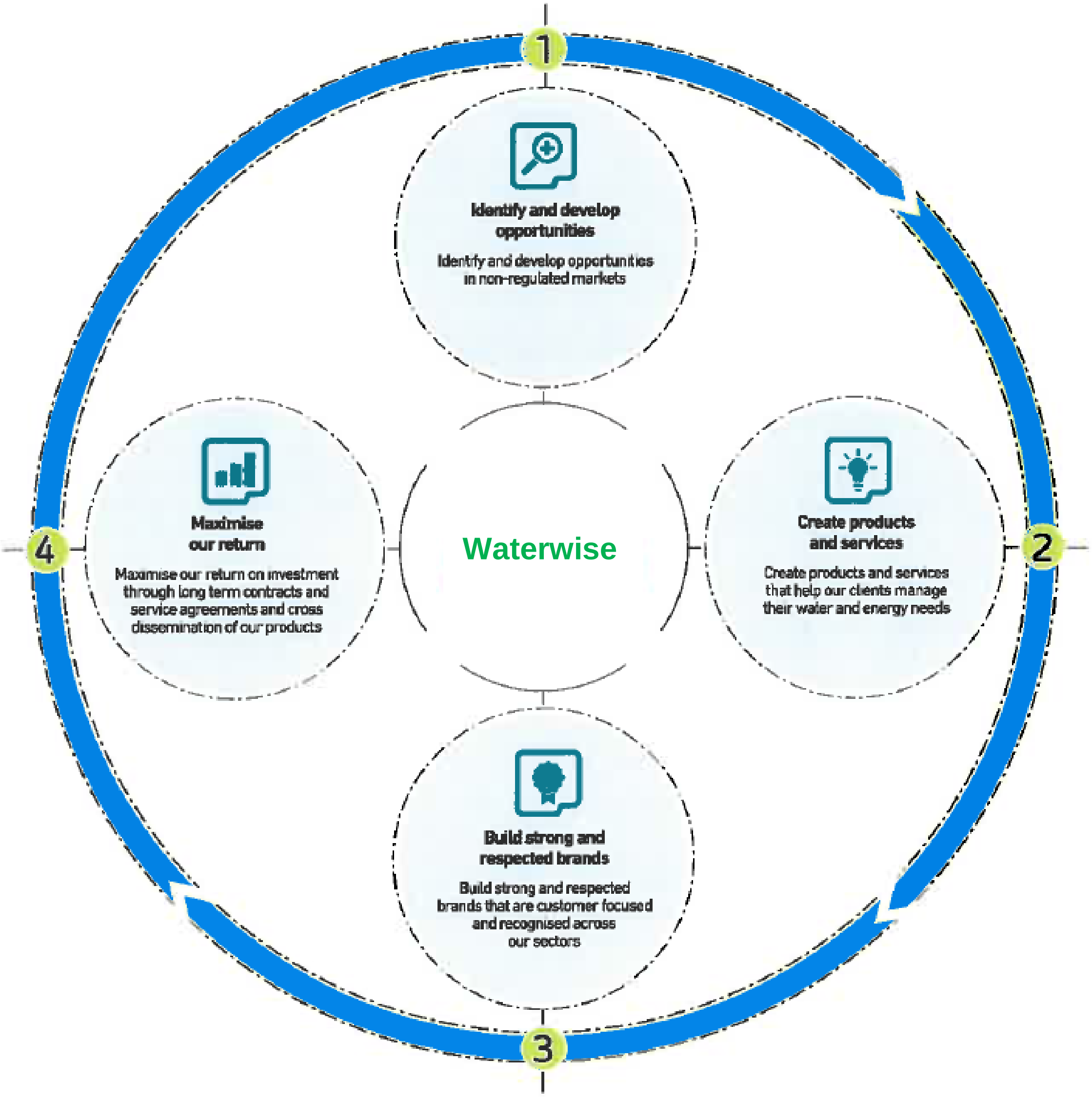
The company earns a return on its asset base. We can generate additional returns if we outperform Ofwat's assumptions by becoming more efficient in the delivery of our capital programme, managing our operational costs more effectively, and by financing our business at a lower cost. Our operating performance is assessed and benchmarked against the sector by Ofwat. Over the period 2015 – 2020 there will be scope to earn additional income, or incur penalties, based on our performance.


1
Water is collected
(abstraction)
We pay the Environment Agency for the water we collect from reservoirs, rivers and underground aquifers across our region.
2
Water is cleaned
Our 134 groundwater and 18 surface water treatment works clean raw water to the highest standards making it safe to drink.
3
Clean water is distributed
A 47,000 km network of pipes and enclosed storage reservoirs bring a continuous supply of clean water right to our customers' taps.
4
Customers enjoy our services
We bill 3.3 million businesses and households a year. In return, we provide a safe, reliable supply of water and the collection of waste water 24 hours a day, 365 days a year.
5
Waste water is collected
Our 92,000 km of sewers and pumping stations collect waste water from homes and businesses, and surface water from outside properties and drains.
6
Waste water is treated and returned to the environment
Waste water is carefully screened, filtered and treated in our 1,019 sewage treatment works to meet stringent environmental standards. We pay the Environment Agency an annual consent fee to return the treated water to the water system.
CAPITAL INVESTMENT
£547m
Networks invested and maintained
As an investment led industry, our capital programme this year was £547 million, or around £165 per connected property.
CAPITAL INVESTMENT

## 2.2 The Business Model: Non-regulated-Waterwise Business Services

Our non-regulated business allows us to apply our water and waste water services knowledge to create and deliver services and products to UK and global municipal, industrial and commercial customers.

We also provide renewable energy to the group and are looking to identify new opportunities in energy generation.



## 3.0 COMPETITIVE ENVIRONMENT

### 3.1 Market & Industry Overview [1]

**The water and sewerage industry**

The industry in England and Wales delivers services to homes and businesses of over 50 million people.

There are 19 regional suppliers, who serve the majority of these customers. 10 of the regional companies – including Waterwise – provide water and sewerage services. The other nine provide water services only.

The UK water industry was privatised in 1989 and has made significant progress since, attracting more than £4 billion of private investment every year to improve operational performance and make customer service improvements. As a result, drinking water quality in the UK is among the highest in the world. The industry also makes a substantial contribution to the economy, estimated at £15 billion a year for the UK as a whole, and directly or indirectly supports the equivalent of 127,000 full-time jobs.

Despite the sector's progress since privatisation, it still faces substantial challenges that must be tackled in the coming years. These must be met whilst still keeping bills affordable for customers, both now and in the future. In particular:

- Much of the sector's infrastructure is ageing. For example, approximately 20% of Waterwise's sewers and 10% of our water mains are more than 100 years old, which means we need to continue to reinvest in the renewal of our networks.
- We can expect to see more extreme weather. This means we need to build resilience, so we can cope with increased flooding and periods of droughts.
- The UK's population is growing, which is adding to the pressure on water resources and our networks. Waterwise serves 3.1 million households, a total that's increasing by about 12,500 households each year. That's the equivalent of adding a city the size of Plymouth every seven years, in our region alone. We need to make sure we have the infrastructure in place to serve these people.
- Customers quite rightly expect better levels of service, making it ever more challenging for all organisations to meet their customers' expectations. Water companies know they've got to work harder at improving customer service.
- Our industry has to compete for global capital to invest for the future. The sector must remain an attractive investment opportunity. Otherwise the only way we'll be able to attract investment is by having to pay more for it, which will push up customers' bills.

Waterwise has always contributed to the debate about our industry's future, including through our series of Changing Course publications. We'll continue to be an active participant in these conversations, so we can help shape thinking about how to best serve our customers in the future.

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1. Sections 3.1, 3.2, 3.3 are quoted from WWplc Report & Accounts

## 3.2 How the Industry is Regulated

Waterwise is a regulated business. We work within five year regulatory planning cycles, known as Asset Management Plan (AMP) periods. This financial year was the last in AMP5, with AMP6 starting on 1 April 2015.

The industry operates within the following policy and regulatory framework:

- The European Union (EU) sets water, waste water and environmental standards across member countries.

- Government sets the overall water and sewerage policy framework. This is done by the Department for Environment, Food and Rural Affairs (Defra) in England, and by the Welsh Government in Wales.

- Ofwat is our economic regulator, which means that it sets the prices we can charge our customers in each AMP period, and ensures that we carry out our functions properly and are appropriately financed.

- The Drinking Water Inspectorate (DWI) is the drinking water quality regulator and makes sure we comply with the water quality regulations.

- The Environment Agency (EA) is the environmental regulator in England. It controls water abstraction, river pollution and flooding.

- Natural Resources Wales is the environmental regulator in Wales. It ensures that the country's natural resources are sustainably maintained, enhanced and used.

We also work with other agencies, including:

- The Consumer Council for Water (CCW), which represents the industry's customers; and

- Natural England, which protects and improves England's natural environment.

**The regulatory regime for AMP6**

During the year, Ofwat concluded its price review for AMP6, which runs from 2015 to 2020. Most of the companies have agreed business plans with Ofwat, setting out what they commit to deliver during the period and the bills that customers will pay.

The AMP6 business plans are designed to deliver what customers say they value most, in terms of the service they receive and the benefits to the environment and society.

Across the industry, water companies engaged with more than 250,000 customers – the largest ever consultation in the utilities sector – to get a clear understanding of what they were willing to pay for.

Key features of the regulatory regime for AMP6 include:

- **Greater flexibility to spend money where it's most needed.**
  In previous AMPs, spending was regulated between capital expenditure (Capex) to meet long term investment needs, and operating expenditure (Opex) to meet day-to-day running costs. The ability to earn a return on Capex arguably incentivised companies to seek Capex type solutions to issues, even if Opex might be more efficient. In AMP6 Ofwat has considered expenditure on a total expenditure (Totex) basis, so we can choose the most cost-effective and innovative solutions to meet our commitments.

- **Aligning the interests of customers and investors.** In AMP6, company performance is measured against metrics called Outcome Delivery Incentives (ODIs). While failure to achieve targets can lead to penalties, as in previous AMPs, many of these ODIs also include incentives for companies to outperform. As the ODIs are based on what is important to customers, outperformance means that both customers and companies benefit. Companies can also do better if they deliver their investment programme for less than their plan, sharing the savings with customers.

- **A better environment**. Several ODIs are designed to deliver important environmental improvements, such as better river quality, which focuses companies on achieving their environmental commitments over the next five years.

- **Reduced bills for customers**. Customers must be willing and able to pay for the costs of the programmes we'll deliver during AMP6. They'll benefit from rising standards and an average reduction in bills of 5% across the industry, over the five years. Companies will also be doing more to help people who struggle to pay their bills, for example by enhancing the social tariffs they offer.

### An evolving industry

We expect the industry landscape to continue to evolve in the coming years. In addition to the opening up of non-household retail competition, as discussed under 'The non-regulated market', there's scope for more competition in the wholesale business. For example, we believe customers would benefit from a greater role for water trading, which would allow companies with surplus water to sell it to those with resource constraints, saving the significant capital investment required for capital solutions such as desalination plants.

The regulatory regime also makes consolidation less difficult than before. This could encourage companies to take innovative approaches to consolidation, for example by merging their wholesale operations to deliver efficiencies, while demerging their retail businesses.

## 3.3 The Non-Regulated Market

Our non-regulated markets provide additional opportunities for growth in the next few years. We are already active in the UK operating services market providing waste water and water treatment for clients. We also have a small presence in the Scottish water retail market. Competition for non-household retail in England will open up in April 2017 and we are preparing for this. This will give business customers increased choice and encourage companies to provide a better service to them.

We are positioning our business to succeed in this market and working with the rest of the industry to support OpenWater. OpenWater is the body charged by the government with developing the market rules, framework and systems that will be needed for effective non-household retail competition.

In the US operating services market, the large majority of customers are municipalities which are looking to outsource the management of their treatment facilities to companies such as Severn Trent. There are signs that the market could create new opportunities, as municipalities turn to the private sector for expertise and funding in response to increasing demands from customers and regulators. We are looking at how we can take part in this market, as it develops.

The renewable energy market also has growth potential for us. We see scope to increase our electricity generation from sources such as food waste digestion and solar, allowing us to sell any electricity not used by our regulated business to National Grid. Similarly, we can sell surplus gas generated by our waste treatment works to the grid.

## 3.4 Current Performance of Waterwise

Waterwise recently announced out-performance against the regulatory allowances, already locked in operationally through 1) totex and efficiency savings, 2) benefits on ODIs and 3) financing costs. All totex savings, i.e. reductions in opex and capex spend, will translate directly into out-performance against ODIs. Analysts comment that further savings would mean that Waterwise is well on its way to meeting their base-case expectations on totex out-performance of 100bps on Return on Regulated equity (RoRE), their base case for RoRE being 5.7%.

The analysts further comment that management deserves credit for re-vitalising the business, adding commercial rigour and a sharper customer focus. Creating value in the services and Renewables businesses could deliver an impressive 10% IRR (un-levered, post-tax, nominal).

# 4.0 FINANCE AND TREASURY

## 4.1. Segmental Analysis

The group has two reportable segments: Waterwise and Waterwise Services. The key factor determining the identification of reportable segments is the regulatory environment in which the businesses operate. Waterwise is subject to economic regulation by Ofwat and operates under a licence to provide water and sewerage services within a defined geographical region in England and Wales. Waterwise Services is not subject to economic regulation and operates in markets in the USA, Europe and Asia. Interests in joint ventures and associates are not material and are not included in the segmental reports reviewed by WEC.

The Waterwise Executive Committee (WEC) is considered to be the group’s chief operating decision maker. The reports provided to WEC include segmental information prepared on the basis described above.

Transactions between reportable segments are included within segmental results, assets and liabilities in accordance with group accounting policies. These are eliminated on consolidation.

The group has a large and diverse customer base and there is no significant reliance on any single customer.

The measure of profit or loss that is reported to WEC for the segments is underlying PBIT (profit before interest, tax and exceptional items). A segmental analysis of sales and underlying PBIT is presented below.

The results from the Water Purification business have been excluded from the Waterwise Services segment, in both the current and prior year, as it has been classified as a discontinued operation.

## 4a) Segmental Results

| | 2015 | | 2014 | |
|---|---|---|---|---|
| | WWC £m | WWBS £m | WWC £m | WWBS £m Restated |
| External sales | 1,579.1 | 216.2 | 1,542.6 | 209.9 |
| Inter-segment sales | 2.1 | 0.1 | 2.2 | 0.3 |
| Total sales | 1,581.2 | 216.3 | 1,544.8 | 210.2 |
| Profit before interest, tax and exceptional items | 539.0 | 9.7 | 518.6 | 13.3 |
| Exceptional items | (20.6) | 1.9 | 8.2 | (2.3) |
| Profit before interest and tax | 518.4 | 11.6 | 526.8 | 11.0 |
| Profit before interest, tax and exceptional items is stated after: | | | | |
| Amortisation of intangible assets | 22.2 | 1.0 | 28.0 | 0.9 |
| Depreciation of property, plant and equipment | 276.7 | 3.5 | 267.5 | 3.2 |
| Profit on disposal of fixed assets | (0.4) | (0.1) | (0.3) | (0.2) |

The reportable segments' revenue is reconciled to group turnover as follows:

| | 2015 £m | 2014 Restated £m |
|---|---|---|
| WWC | 1,581.2 | 1,544.8 |
| WWBS | 216.3 | 210.2 |
| Other | 15.8 | 13.1 |
| Inter-segment sales | (12.0) | (11.4) |
| Group turnover | 1,801.3 | 1,756.7 |

Segmental underlying PBIT is reconciled to the group's profit before tax and discontinued operations as follows:

| | 2015 £m | 2014 Restate |
|---|---|---|
| Underlying PBIT | | |
| – WWC | 539.0 | 518.6 |
| – WWBS | 9.7 | 13.3 |
| – Corporate and other costs | (12.1) | (11.5) |
| Consolidation adjustments | 3.7 | 3.4 |
| Group underlying PBIT | 540.3 | 523.8 |
| Exceptional items allocated to segments | | |
| – WWC | (20.6) | 8.2 |
| – WWBS | 1.9 | (2.3) |
| – Corporate and other | – | (21.1) |
| Share of results of associates and joint ventures | 0.1 | 0.2 |
| Net finance costs | (240.0) | (247.9) |
| (Losses)/gains on financial instruments | (133.5) | 58.0 |
| Profit before tax and discontinued operations | 148.2 | 318.9 |

The group's treasury and tax affairs are managed centrally by the Group Treasury and tax departments. Finance costs are managed on a group basis and hence interest income and costs are not reported at the segmental level. Tax is not reported to WEC on a segmental basis.

## 4b) Segmental Capital Employed

Separate segmental analyses of assets and liabilities are not reviewed by WEC. The balance sheet measure reviewed by WEC on a segmental basis is capital employed which includes the following components:

| | 2015 | | 2014 | |
|---|---|---|---|---|
| | WWC £m | WWBS £m | WWC £m | WWBS £m |
| | £m | £m | £m | £m |
| Operating assets | 7,679.9 | 100.9 | 7,442.2 | 172.8 |
| Goodwill | 1.3 | 14.3 | 1.3 | 14.8 |
| Interests in joint ventures and associates | 0.1 | 4.5 | 0.1 | 5.0 |
| Segment assets | 7,681.3 | 119.7 | 7,443.6 | 192.6 |
| Segment operating liabilities | (1,350.1) | (58.8) | (1,155.7) | (92.2) |
| Capital employed | 6,331.2 | 60.9 | 6,287.9 | 100.4 |

Operating assets comprise other intangible assets, property, plant and equipment, inventory and trade and other receivables. Operating liabilities comprise trade and other payables, retirement benefit obligations and provisions.

Capital employed does not include assets held for sale or liabilities associated with assets held for sale.

Additions to other intangible assets and property, plant and equipment were as follows:

| | | | | |
|---|---|---|---|---|
| Other intangible assets | 15.4 | 1.0 | 8.2 | 5.5 |
| Property, plant and equipment | 481.3 | 2.7 | 519.6 | 6.9 |

The reportable segments' assets are reconciled to the group's total assets as follows:

| | Note | 2015 £m | 2014 £m |
|---|---|---|---|
| Segment assets | | | |
| – WWC | | 7,681.3 | 7,443.6 |
| – WWBS | | 119.7 | 192.6 |
| Corporate assets | | 78.6 | 68.2 |
| Other financial assets | | 203.8 | 208.6 |
| Current tax receivable | | 11.2 | 16.5 |
| Assets held for sale | 38 | 107.9 | – |
| Consolidation adjustments | | (45.5) | (40.3) |
| Total assets | | 8,157.0 | 7,889.2 |

The consolidation adjustments comprise elimination of intra-group debtors and unrealised profits on fixed assets.
The reportable segments' liabilities are reconciled to the group's total liabilities as follows:

| | Note | 2015 £m | 2014 £m |
|---|---|---|---|
| Segment liabilities | | | |
| – WWC | | (1,350.1) | (1,155.7) |
| – WWBS | | (58.8) | (92.2) |
| Corporate liabilities | | (149.1) | (60.1) |
| Other financial liabilities | | (5,134.0) | (4,853.1) |
| Deferred tax | | (625.1) | (654.0) |
| Liabilities associated with assets held for sale | 38 | (35.3) | – |
| Consolidation adjustments | | 18.7 | 16.0 |
| Total liabilities | | (7,333.7) | (6,799.1) |

The consolidation adjustments comprise elimination of intra-group creditors.

## 4 c) Geographical Areas

The group's sales were derived from the following countries:

| | 2015 £m | 2014 Restated £m |
|---|---|---|
| UK | 1,649.4 | 1,610.9 |
| USA | 129.3 | 120.1 |
| Other | 22.6 | 25.7 |
| | 1,801.3 | 1,756.7 |

The group's non-current assets (excluding financial instruments, deferred tax assets and post employment benefit assets) were located in the following countries:

| | 2015 £m | 2014 £m |
|---|---|---|
| UK | 7,299.2 | 7,084.8 |
| USA | 25.2 | 36.1 |
| Other | 1.1 | 2.9 |
| | 7,325.5 | 7,123.8 |

6 Revenue

| | 2015 £m | 2014 Restated £m |
|---|---|---|
| Regulated water and sewerage services | 1,570.5 | 1,534.5 |
| Other services | 187.3 | 180.0 |
| Service concession arrangements (note 41) | 43.5 | 42.2 |
| **Total turnover** | 1,801.3 | 1,756.7 |
| Interest receivable (note 10) | 1.6 | 4.8 |
| | 1,802.9 | 1,761.5 |

## 4.2. Dividend Policy and Ofwat's Financial Parameters.

Waterwise has announced that it will reduce its 2015/16 dividend by 5% to 80.66p per share. Thereafter dividends will be increased by the RPI inflation rate instead of the previous RPI plus 3%, through to 2020. The company is also launching a GBP 100 million share buy-back programme to re-align its capital structure.

Ofwat's regulatory and pricing framework uses key financial assumptions for all water companies, such as a real cost of new debt at 2.0%, a real WACC of 2.72%, a target gearing figure of Net Debt / Regulated Capital Value (RCV) of 62.5%.

## 4.3. Totex Projects

In 2015 capex was GBP 547 millions and opex 589 millions. Included in this capex total was 137.8 millions of infrastructure maintenance expenditure which is charged to the income statement under FRS principles. The remaining capex is added to the asset base (Regulated Capital Value). Opex is usually charged to customers effectively, spread over a number of years.

Typical totex projects include replacing and refurbishing of ageing water quality assets, enhancement of the capacity and resilience of the water supply network through new reservoirs, pipelines, pumping stations etc, and catchment management e.g. improving run-off from farmland.

Key AMP6 capex projects typically range from GBP 26 million to 50 million, but with one at 242 million. Despite the essential nature of totex, absolutely central to the maintenance and growth of this business, there is always a strong ODI incentive to reduce the capital cost of projects.

Continuous attention is given to operating improvements in areas like water supply interruptions, sewage blockages, leakage reduction, environmental performance and customer service performance. There has also been considerable investment in education and training of staff as well as operating systems, equipment and technology to improve service efficiency and reduce operating expenditure.

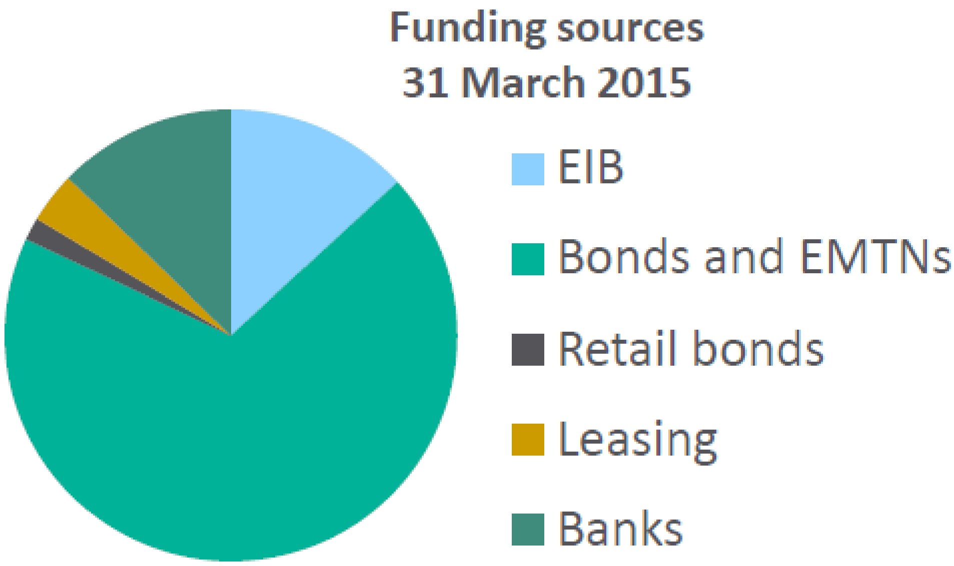
In the non-regulated businesses the largest current project is a GBP 13 million aerobic digestion plant for renewable energy. Solar, sewage, wind and food waste investments in this area typically have double-digit IRRs. The Operating Services business provides design, build and contract operation services, relating to water and waste water treatment, for a variety of industrial sectors both throughout the UK and internationally.

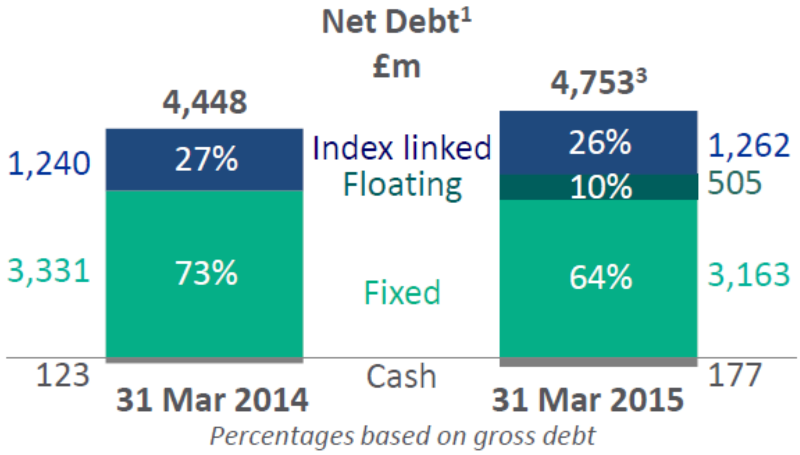
### 4..4 Funding

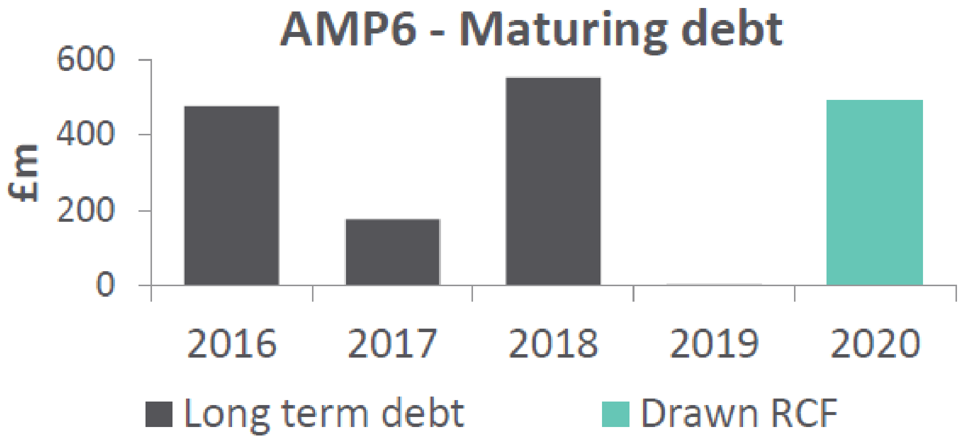
Summary funding and net debt:

| | |
|---|---|
| Bank | £1279.2m |
| Other Loans | £3467.5m |
| Leasing | £ 180.0m |
| Total | £4926.7m |
| Cash | £176.7m |
| Net debt | £4750.0m |

The three charts below show funding sources [EIB is European Investment Bank], mix of interest bases and maturing debt during the AMP6 period: EIB = European Investment Bank.


Funding sources
31 March 2015
EIB
Bonds and EMTNs
Retail bonds
Leasing
Banks




There is a requirement for new finance over the AMP6 period of circa. £1bn.

So the financing requirements during 2016-2020 are:

| | 2016<br>£ | 2017<br>£ | 2018<br>£ | 2019<br>£ | 2020<br>£ | TOTAL<br>£ |
|---|---|---|---|---|---|---|
| Refinance | 475 | 175 | 550 | - | 485 | 1,685 |
| New | 200 | 200 | 200 | 200 | 200 | 1,000 |
| **Total** | **675** | **375** | **750** | **200** | **685** | **2,685** |

Just prior to y/e 2015, there were two funding events:

- EIB: arranged a new £530m floating rate nine year loan, of which £200m was drawn at y/e 2015.

- RCF: amendment and extension of the revolving credit facility which had been due to mature in 2018. The new five year facility is for £900m, of which £485m was drawn at y/e 2015.

So at y/e 2015 there was £745m headroom on facilities (2014: £500m), comprising
the undrawn balances of the EIB loan and the RCF [£330m + £415m].

## 4.5. Currency Risk

Except for debt raised in foreign currency, which is fully hedged, the business does not involve significant exposure to foreign exchange transactions. WWplc has investments in various assets denominated in foreign currencies, principally the US dollar and the euro. The current policy is to hedge an element of the currency translation risk associated with certain foreign currency denominated assets.

The group issues notes in foreign currency under its European Medium Term Note (EMTN) programme and uses cross currency swaps to convert the proceeds to sterling. The effect of these swaps is that interest and principal payments on the borrowings are denominated in sterling and hence the currency risk is eliminated. The foreign currency notes and the cross currency swaps are recorded in the balance sheet at their fair values and the changes in fair values are taken to gains/(losses) on financial instruments in the income statement. Since the terms of the swaps closely match those of the underlying notes, such changes tend to be broadly equal and opposite.

## 4.6 Treasury

The firm has a central treasury function servicing all of the Group. There are two front office and two back office staff in addition to the Group Treasurer.

The treasury operates under a licence from the regulator Ofwat. The substance of the licence is that transactions between the regulated and the non-regulated parts of the business operate on an arms-length basis.

All of the group debt is with the regulated entity (WWC) apart from a £75m retail bond and £100m of bank bilaterals at holding company level (WWplc).

# 5.0 FINANCIALS

**Equity Analysis Model**
**Waterwise plc**
**Income Statement**

| | | | Historical Data | | | | |
|---|---|---|---|---|---|---|---|
| **Month** | | *Accounts date* | **2011** | **2012** | **2013** | **2014** | **2015** |
| **March** | | *Currency / units* | **GBP mill** | **GBP mill** | **GBP mill** | **GBP mill** | **GBP mill** |
| | | *Audit / man / fcst* | **audited** | **audited** | **audited** | **audited** | **audited** |
| | | *Number of months* | **12** | **12** | **12** | **12** | **12** |
| **Sales Revenue** | | | **1,711.3** | **1,770.6** | **1,831.6** | **1,756.7** | **1,801.3** |
| a | Total Operating (Costs) & Revenues +/- | | (1,192.2) | (1,266.4) | (1,333.6) | (1,232.9) | (1,261.0) |
| a | Exceptionals etc. +/- | | (21.4) | (34.4) | (5.8) | (15.2) | (18.7) |
| b | (Cost of Materials, Other External Purchases) | | (193.8) | (200.3) | (202.3) | (149.6) | (151.8) |
| **Other Expenditure Details (for information)** | | | | | | | |
| b | (Personnel Costs) | | (315.9) | (293.1) | (340.9) | (327.8) | (368.3) |
| b | (Depreciation & Impairment of Tangible Assets) | | (251.5) | (256.0) | (264.4) | (270.0) | (281.6) |
| b | (Amortisation & Impairment of Goodwill) | | | (22.9) | (4.6) | | |
| b | (Amortisation & Impairment of Intangibles) | | (25.4) | (30.8) | (34.1) | (28.9) | (23.4) |
| b | (Infrastructure Maintenance Expenditure) | | (96.9) | (128.9) | (147.7) | (140.3) | (134.8) |
| b | (Hired and Contracted Services) | | (184.8) | (223.5) | (199.9) | (227.4) | (223.5) |
| **Operating Profit** | | | **497.7** | **469.8** | **492.2** | **508.6** | **521.6** |
| **Investment Income Income** | | | | | | | |
| | Income from Investments, Participations etc | | 0.1 | 0.1 | 0.2 | 0.2 | 0.1 |
| **EBIT** | | | **497.8** | **469.9** | **492.4** | **508.8** | **521.7** |
| **Interest Received & Paid** | | | | | | | |
| | Exceptional (Losses)/Gains on Financial Instruments | | (14.2) | (84.2) | (45.3) | 58.0 | (133.5) |
| | Other Financial Income & Expenditure | | (6.0) | 1.5 | (6.7) | (18.0) | (15.8) |
| | Interest Received | | 7.5 | 7.0 | 2.6 | 4.8 | 1.6 |
| | (Gross Interest Paid) | | (232.1) | (237.5) | (227.8) | (234.7) | (225.8) |
| **Profit before Tax** | | | **253.0** | **156.7** | **215.2** | **318.9** | **148.2** |
| | (Tax charge) | | (46.2) | 17.7 | 15.2 | (77.3) | (32.7) |
| | Exceptional Tax Credit | | 67.7 | | | 230.2 | |
| **Profit after Tax** | | | **274.5** | **174.4** | **230.4** | **471.8** | **115.5** |
| | Extraordinaries, Discontinued Operations etc | | | | | (36.9) | 4.7 |
| **Profit / (Loss) for the Year** | | | **274.5** | **174.4** | **230.4** | **434.9** | **120.2** |
| | Attributable to Non-controlling Interests | | 1.9 | 2.6 | 2.9 | 1.1 | 1.1 |
| | **Attributable to Owners of Company** | | **272.6** | **171.8** | **227.5** | **433.8** | **119.1** |
| | (Preference Dividends) | | | | | | |
| | (Ordinary Dividends) | | (154.1) | (166.4) | (180.8) | (192.2) | (203.4) |
| **Retained Profit for Year** | | | **118.5** | **5.4** | **46.7** | **241.6** | **(84.3)** |
| | Statement of Gains and Losses | | 46.7 | (146.7) | (58.3) | (0.5) | (97.8) |
| Total Comprehensive Income | | | 321.2 | 27.7 | 172.1 | 434.4 | 22.4 |
| **EBITA (before Exceptionals & all Amortisation)** | | | **544.6** | **558.0** | **536.9** | **552.9** | **563.8** |
| **EBITDA (before Exceps. Deprn, & all Amortisation)** | | | **796.1** | **814.0** | **801.3** | **822.9** | **845.4** |
| **Cash Earnings (Before Goodwill, Exceps.& Extraords)** | | | **240.5** | **313.3** | **283.2** | **197.7** | **266.6** |
| **Cash Retained Profit (Before Goodwill, Exceps & Extraords)** | | | **86.4** | **146.9** | **102.4** | **5.5** | **63.2** |

**Equity Analysis Model**
***Waterwise plc***
**Balance Sheet**

| | Historical Data | | | | |
|---|---|---|---|---|---|
| *Accounts date* | **2011** | **2012** | **2013** | **2014** | **2015** |
| *Currency / units* | **GBP mill** | **GBP mill** | **GBP mill** | **GBP mill** | **GBP mill** |
| Goodwill | 68.3 | 44.9 | 41.7 | 14.8 | 14.3 |
| Other Intangible Fixed Assets | 134.9 | 116.0 | 99.3 | 80.2 | 66.7 |
| Property, Land & Buildings & Capital Work | 1,753.9 | 1,804.4 | 1,867.5 | 1,938.2 | 1,996.4 |
| Plant, Equipment & Vehicles - net | 4,673.1 | 4,773.4 | 4,892.5 | 5,085.3 | 5,243.4 |
| Financial Investments, Tax & Pension Assets & Deriv. | 193.2 | 137.5 | 135.2 | 77.7 | 18.2 |
| Medium-term Trade-related Assets | | | | | |
| **Total Fixed Assets** | **6,823.4** | **6,876.2** | **7,036.2** | **7,196.2** | **7,339.0** |
| Stocks, Inventories, Work in Progress | 27.1 | 34.4 | 32.1 | 27.2 | 16.7 |
| Trade and Other Receivables | 478.5 | 479.4 | 506.0 | 513.2 | 492.0 |
| Other financial assets & investments | | | | | |
| Cash and Short-term Investments | 315.2 | 295.1 | 403.6 | 123.2 | 176.7 |
| Tax Assets, Derivatives, Assets for Sale & Other | 4.3 | 30.0 | 41.5 | 29.4 | 132.6 |
| **Total Current Assets** | **825.1** | **838.9** | **983.2** | **693.0** | **818.0** |
| **Total Assets** | **7,648.5** | **7,715.1** | **8,019.4** | **7,889.2** | **8,157.0** |
| Short-term Debt | 23.9 | 89.3 | 170.3 | 206.1 | 463.0 |
| Trade and Other Payables | 391.2 | 397.6 | 399.0 | 412.7 | 494.0 |
| Corporation Tax Payable | 67.0 | 46.5 | | | |
| Provisions, Derivatives & Other Current Liabilities | 12.7 | 17.5 | 11.7 | 36.9 | 83.4 |
| **Total Current Liabilities** | **494.8** | **550.9** | **581.0** | **655.7** | **1,040.4** |
| Medium & Long-term Debt | 4,320.5 | 4,309.5 | 4,631.3 | 4,416.0 | 4,463.7 |
| Medium-term Trade Payables | 367.8 | 411.0 | 453.4 | 492.4 | 542.0 |
| Tax, Pension & Other Long-term Provisions | 1,359.3 | 1,462.3 | 1,509.7 | 1,235.0 | 1,287.6 |
| **Total Non-current Liabilities** | **6,047.6** | **6,182.8** | **6,594.4** | **6,143.4** | **6,293.3** |
| Issued Share Capital | 232.2 | 232.6 | 233.3 | 233.9 | 233.7 |
| Share Premium Account, Treasury Shares | 80.0 | 83.8 | 89.7 | 94.2 | 100.2 |
| Revaluation Reserve | | | | | |
| Other Reserves | 464.5 | 400.2 | 72.3 | 82.2 | 98.2 |
| Revenue Reserves | 323.1 | 256.9 | 437.9 | 667.3 | 377.8 |
| **Total Capital and Reserves** | **1,099.8** | **973.5** | **833.2** | **1,077.6** | **809.9** |
| Non-controlling Interests | 6.3 | 7.9 | 10.8 | 12.5 | 13.4 |
| **Total Shareholders' Funds** | **1,106.1** | **981.4** | **844.0** | **1,090.1** | **823.3** |
| *Balance Check* | **-** | **-** | **-** | **-** | **-** |

| | | | | | |
|---|---|---|---|---|---|
| Accumulated depreciation | 3,657.5 | 3,883.3 | 4,103.1 | 4,349.0 | 4,529.1 |
| Average Cost of Debt % | 5.34% | 5.43% | 4.95% | 4.98% | 4.73% |

## Equity Analysis Model

### *Waterwise plc*

### UK-Style Cash Flow Statement

| | Historical Data | | | | |
|---|---|---|---|---|---|
| *Accounts date* | **2011** | **2012** | **2013** | **2014** | **2015** |
| *Currency / units* | **GBP mill** | **GBP mill** | **GBP mill** | **GBP mill** | **GBP mill** |
| Number of months | **12** | **12** | **12** | **12** | **12** |
| **CASH FLOW FROM OPERATING ACTIVITIES** | | | | | |
| Operating Profit | 497.7 | 469.8 | 492.2 | 508.6 | 521.6 |
| Tangible Asset Depreciation | 251.5 | 256.0 | 264.4 | 270.0 | 281.6 |
| Dec(Inc) in Stock / Inventories | (0.5) | (7.4) | 1.9 | 4.4 | (5.7) |
| Dec(Inc) in Debtors / Receivables | (7.5) | 6.1 | (29.4) | (17.2) | (32.5) |
| Inc(Dec) in Creditors / Payables & Advance Payments | 22.3 | 5.0 | (2.4) | 4.0 | 20.0 |
| All other non-cash adjustments & Exceptionals | (10.5) | (3.6) | 4.5 | (39.6) | (24.9) |
| **Cash Generated from Operations** | **753.0** | **725.9** | **731.2** | **730.2** | **760.1** |
| Dividends Received from Associates | | | | | |
| (Tax Paid) | (32.4) | (72.0) | (72.5) | 27.2 | (28.6) |
| **Net Cash from Operating Activities** | **720.6** | **653.9** | **658.7** | **757.4** | **731.5** |
| **CASH FLOW FROM INVESTING ACTIVITIES** | | | | | |
| Income Received from Investments | 10.3 | 6.7 | 3.7 | 6.5 | 1.8 |
| Interest Received | | | | | |
| (Purchase of Tangible Fixed Assets) | (403.1) | (371.1) | (429.2) | (490.6) | (446.2) |
| Disposal of Tangible Fixed Assets | 24.5 | 31.9 | 43.4 | 40.6 | 47.8 |
| (Purchase of Subs, Intang., Financial & Forestry Assets) | (20.9) | (12.0) | (17.3) | (25.3) | (17.7) |
| Disposal of Subsidiaries, Intangibles & Financial Assets | | | 12.4 | | |
| **Net Cash from Investing Activities** | **(389.2)** | **(344.5)** | **(387.0)** | **(468.8)** | **(414.3)** |
| **CASH FLOW FROM FINANCING ACTIVITIES** | | | | | |
| (Interest Paid) | (190.6) | (217.1) | (192.8) | (211.1) | (220.0) |
| New Shares Issued | 4.7 | 4.2 | 6.6 | 5.1 | 6.7 |
| (Repurchase / Redemption of Shares) | (2.0) | (1.8) | (1.3) | (2.8) | (23.4) |
| (Costs of Issuing / Redeeming Equity) | | | | | |
| Total Increase in Debt | 171.2 | 250.0 | 668.3 | 0.7 | 685.0 |
| (Total Decrease in Debt) | (76.0) | (205.0) | (277.3) | (172.8) | (355.4) |
| (Dividends Paid on Ordinary Shares) | (169.4) | (159.0) | (322.0) | (185.3) | (196.9) |
| (Preference and Minority Dividends Paid) | (1.5) | (1.0) | (0.5) | (0.6) | (1.4) |
| Miscell. Financing Costs e.g. derivatives, bank fees | 20.5 | | (44.3) | | (139.2) |
| **Net Cash from Financing Activities** | **(243.1)** | **(329.7)** | **(163.3)** | **(566.8)** | **(244.6)** |
| **Net Cash Flow from Ops. Investing & Funding** | 88.3 | (20.3) | 108.4 | (278.2) | 72.6 |
| *Balance check* | - | (0.0) | - | - | - |
| | | | | | |
| Change in Cash | - | (20.1) | 108.5 | (280.4) | 53.5 |
| Change in Overdraft | 88.3 | (0.2) | (0.1) | 2.2 | 19.1 |

## Equity Analysis Model

***Waterwise plc***

### Cash Flow Analysis

| | | Historical Data | | | | |
|---|---|---|---|---|---|---|
| *Accounts date* | 2011 | 2012 | 2013 | 2014 | 2015 | Period |
| *Currency / units* | GBP mill | GBP mill | GBP mill | GBP mill | GBP mill | Total |
| **Cash Flow Summary** | audited | audited | audited | audited | audited | 2011-15 |
| Number of months | 12 | 12 | 12 | 12 | 12 | |
| **CASH FLOW FROM OPERATIONS** | | | | | | |
| Operating Profit | 498 | 470 | 492 | 509 | 522 | 2,490 |
| Other Non-cash & Exceptional Items | 10 | (4) | (40) | (40) | (164) | (237) |
| Investment Income | 10 | 7 | 4 | 7 | 2 | 29 |
| **"Cash Profit"** | **518** | **473** | **456** | **476** | **359** | **2,282** |
| (Increase) / Decrease in Net Working Assets | 14 | 4 | (30) | (9) | (18) | (39) |
| Tangible Asset Depreciation | 252 | 256 | 264 | 270 | 282 | 1,324 |
| Net Capital Expenditure | (379) | (339) | (386) | (450) | (398) | (1,952) |
| (Tax Paid | (32) | (72) | (73) | 27 | (29) | (178) |
| (Dividends Paid) | (171) | (160) | (323) | (186) | (198) | (1,038) |
| **Free Cash Flow before Interest** | **202** | **161** | **(90)** | **128** | **(3)** | **399** |
| (Net Interest Paid) | (191) | (217) | (193) | (211) | (220) | (1,032) |
| **Internal Cash Flow** | **11** | **(56)** | **(283)** | **(83)** | **(223)** | **(633)** |
| **ACQUISITION & FINANCING CASH FLOWS** | | | | | | |
| (Acquisitions),Disposals,(Investments) | (21) | (12) | (5) | (25) | (18) | (81) |
| Increase / (Decrease) in Share Capital | 3 | 2 | 5 | 2 | (17) | (4) |
| New Borrowing | 171 | 250 | 668 | 1 | 685 | 1,775 |
| (Loan Repayments plus O/D Changes)) | (164) | (205) | (277) | (175) | (375) | (1,196) |
| (Increase) / Decrease in Cash | | 20 | (109) | 280 | (54) | 139 |
| **Net Financing Cash Flow** | **(11)** | **56** | **283** | **83** | **223** | **633** |
| *Balance check* | (0) | (0) | 0 | 0 | 0 | 0 |

## Equity Analysis Model

***Waterwise plc***

### Sustainable Cash Profit

| | 2011 | 2012 | 2013 | 2014 | 2015 |
|---|---|---|---|---|---|
| | GBP mill | GBP mill | GBP mill | GBP mill | GBP mill |
| Operating Profit & Investment Income after Tax | 486 | 455 | 474 | 492 | 500 |
| Amortisation & Other Non-cash Adjustments | 10 | (4) | (40) | (40) | (164) |
| Depreciation | 252 | 256 | 264 | 270 | 282 |
| Replacement Capital Expenditure | (491) | (457) | (481) | (497) | (505) |
| Replacement Net Working Assets | 12 | 9 | 8 | 6 | |
| **Sustainable Entity Cash Flow after Tax** | **268** | **260** | **226** | **232** | **113** |

**Equity Analysis Model**

***Waterwise plc***

## Share Price Data

| | Historical Data | | | | |
|---|---|---|---|---|---|
| Accounts date | 2011 | 2012 | 2013 | 2014 | 2015 |
| Currency / units | GBP mill | GBP mill | GBP mill | GBP mill | GBP mill |
| | 12 | 12 | 12 | 12 | 12 |
| **Number of Shares & Eps** | | | | | |
| Basic Earnings per Share (pence) | 115.2 | 72.5 | 95.7 | 198.5 | 48.3 |
| **Adjusted Earnings per Share (pence or equiv.)** | **105.6** | **88.9** | **98.9** | **92.5** | **107.2** |
| Interim Dividend Per Share (pence) | 26.00 | 28.04 | 30.34 | 32.16 | 33.96 |
| Final Dividend Per Share (pence) | 39.05 | 42.06 | 45.51 | 48.24 | 50.94 |
| **Total Dividends Per Share (pence)** | **65.05** | **70.10** | **75.85** | **80.40** | **84.90** |
| Average number of common shares | 236.7 | 237.0 | 237.7 | 238.2 | 238.8 |
| Average number of preference shares | | | | | |
| **Share Prices** | | | | | |
| Common Share Price - Low (£) | 11.90 | 13.71 | 15.00 | 16.12 | 18.19 |
| Common Share Price - High (£) | 15.24 | 17.22 | 18.36 | 22.00 | 22.05 |
| Common Share Price - Average (£) | 13.57 | 15.47 | 16.68 | 19.06 | 20.12 |
| Preference Share Price - Low (£) | | | | | |
| Preference Share Price - High (£) | | | | | |
| Preference Share Price - Average | | | | | |
| **Risk rating** | | | | | |
| Variability % | 20 | 20 | 19 | 20 | 17 |
| Beta (actual or estimate) | 0.48 | 0.47 | 0.33 | 0.44 | 0.53 |
| **Assumed Market Risk premium** | **4.19** | **4.19** | **4.19** | **4.19** | **4.19** |
| **UK 5-year Gilt Yield** | **2.28** | **1.96** | **0.72** | **0.85** | **1.25** |
| **3-month LIBOR or equivalent** | 0.76 | **1.08** | **0.49** | **0.55** | **0.57** |
| **Market Capitalisation** | | | | | |
| Market Capitalisation - Common Stock | 3,212 | 3,666 | 3,965 | 4,541 | 4,805 |
| Market Capitalisation - Preference Stock | - | - | - | - | - |
| Market Capitalisation - Total | 3,212 | 3,666 | 3,965 | 4,541 | 4,805 |
| Minorities | 6 | 8 | 11 | 13 | 13 |
| Net Debt | 4,029 | 4,104 | 4,398 | 4,499 | 4,750 |
| Enterprise value [EV] | **7,247** | **7,777** | **8,374** | **9,052** | **9,568** |

## Equity Analysis

| | | | | | |
|---|---|---|---|---|---|
| **Equity Ratios** | | | | | |
| Underlying Eps Growth % | (14.0%) | (15.8%) | 11.2% | (6.5%) | 15.9% |
| P/E Ratio | 12.8 | 17.4 | 16.9 | 20.6 | 18.8 |
| Market / Book Ratio of Equity | 2.92 | 3.77 | 4.76 | 4.21 | 5.93 |
| Dividend Cover | 1.62 | 1.27 | 1.30 | 1.15 | 1.26 |
| Dividend Yield % | 4.8% | 4.5% | 4.5% | 4.2% | 4.2% |
| Total Return to Shareholders % | 27.7% | 19.2% | 12.8% | 19.1% | 10.0% |
| **EV Valuation Multiples** | | | | | |
| EV / Sales | 4.23 | 4.39 | 4.57 | 5.15 | 5.31 |
| EV / Book Capital Employed | 1.41 | 1.53 | 1.60 | 1.62 | 1.72 |
| EV / EBITA | 13.3 | 13.9 | 15.6 | 16.4 | 17.0 |
| EV / EBITDA | 9.10 | 9.55 | 10.45 | 11.00 | 11.32 |
| EV / Staff Costs | 22.9 | 26.5 | 24.6 | 27.6 | 26.0 |
| EV / Sustainable Free Cash Flow | 27.0 | 29.9 | 37.1 | 39.1 | 84.6 |
| **Yields and Implied Growth Rates** | | | | | |
| Sust. Free Cash Flow / EV = (WACC minus growth) | 3.7% | 3.3% | 2.7% | 2.6% | 1.2% |
| Real WACC | 0.0% | 1.6% | 0.9% | 2.1% | 4.0% |
| Implied Sustainable Growth Rate | (3.7%) | (1.7%) | (1.8%) | (0.4%) | 2.9% |

# Equity Analysis Model

***Waterwise plc***

## Financial Profile

| | Historical Data | | | | |
|---|---|---|---|---|---|
| *Accounts date* | **2011** | **2012** | **2013** | **2014** | **2015** |
| *Number of months* | ***12*** | ***12*** | ***12*** | ***12*** | ***12*** |
| **Annual % Growth Rates** | | | | | |
| Sales Growth | 0.4% | 3.5% | 3.4% | (4.1%) | 2.5% |
| EBITA Growth | (68.0%) | 2.5% | (3.8%) | 3.0% | 2.0% |
| Net Earnings Growth before Exceps & Extraords. | (85.9%) | 30.3% | (9.6%) | (30.2%) | 34.9% |
| **Margins and Cost Structure** | | | | | |
| (Cost of Materials, Other External Purchases) % Sales | (11.3%) | (11.3%) | (11.0%) | (8.5%) | (8.4%) |
| Personnel Costs % Sales | (18.5%) | (16.6%) | (18.6%) | (18.7%) | (20.4%) |
| Depreciation % Sales | (14.7%) | (14.5%) | (14.4%) | (15.4%) | (15.6%) |
| (Infrastructure Maintenance Expenditure) % Sales | (5.7%) | (7.3%) | (8.1%) | (8.0%) | (7.5%) |
| (Hired and Contracted Services) % Sales | (10.8%) | (12.6%) | (10.9%) | (12.9%) | (12.4%) |
| Total Exceptional Operating Items % Sales (+/-) | (1.3%) | (1.9%) | (0.3%) | (0.9%) | (1.0%) |
| Total Operating Costs & Revenues % Sales | (69.7%) | (71.5%) | (72.8%) | (70.2%) | (70.0%) |
| EBIT % Sales | 29.1% | 26.5% | 26.9% | 29.0% | 29.0% |
| EBITA% Sales | 31.8% | 31.5% | 29.3% | 31.5% | 31.3% |
| Non-Interest Financial Income & Expenditure (+/-) | (1.2%) | (4.7%) | (2.8%) | 2.3% | (8.3%) |
| **Profitability / Return on Capital Employed** | | | | | |
| EBITA % Capital Employed (pre-exceptionals) | 10.6% | 11.0% | 10.2% | 9.9% | 10.1% |
| Pre-tax Target Rate of Return 0n Book Value | 7.2% | 7.5% | 6.0% | 6.4% | 7.3% |
| EBITA % Market Enterprise Value | 7.5% | 7.2% | 6.4% | 6.1% | 5.9% |
| Pre-tax Target Rate of Return on Market Value | 5.1% | 4.9% | 3.8% | 3.9% | 4.2% |
| **Asset Utilisation / Capital Intensity** | | | | | |
| Sales / Total Assets | 0.22 | 0.23 | 0.23 | 0.22 | 0.22 |
| Stocks % Sales | 1.6% | 1.9% | 1.8% | 1.5% | 0.9% |
| Debtors % Sales | 28.0% | 27.1% | 27.6% | 29.2% | 27.3% |
| Creditors & Advance Payments % Sales | 44.4% | 45.7% | 46.5% | 51.5% | 57.5% |
| Net Working Assets % Sales | (14.8%) | (16.6%) | (17.2%) | (20.8%) | (29.3%) |
| Intangibles % Sales | 11.9% | 9.1% | 7.7% | 5.4% | 4.5% |
| Tangible Fixed Assets % Sales | 376% | 372% | 369% | 400% | 402% |
| Depreciable Assets % Sales | 273% | 270% | 267% | 289% | 291% |
| Net Capex % Annual Depreciation | 151% | 133% | 146% | 167% | 141% |
| Average Age of Depreciable Assets (years) | 14.5 | 15.2 | 15.5 | 16.1 | 16.1 |
| **Tax Ratios** | | | | | |
| Effective Interest Rate [P&L] % | 5.3% | 5.4% | 5.0% | 5.0% | 4.7% |
| Effective Tax Rate [P&L] % | (8.5%) | (11.3%) | (7.1%) | (47.9%) | 22.1% |
| Cash Tax Rate [Cash Flow] % | 12.8% | 45.9% | 33.7% | (8.5%) | 19.3% |

## Capital Structure & Credit Status

| | 2011 | 2012 | 2013 | 2014 | 2015 |
|---|---|---|---|---|---|
| **Balance Sheet Gearing & Leverage** | | | | | |
| Gearing; (Gross Debt % Tangible Net Worth) | 419% | 470% | 598% | 430% | 609% |
| **Gearing; (Net Debt % Tangible Net Worth)** | **388%** | **438%** | **548%** | **418%** | **587%** |
| Leverage: (Net Debt % Capital Employed) | 78% | 81% | 84% | 80% | 85% |
| Net Debt % Enterprise Value | 56% | 53% | 53% | 50% | 50% |
| **Interest Cover Ratios** | | | | | |
| Interest Cover: (EBITA / Net Interest Paid) | 2.42 | 2.42 | 2.38 | 2.40 | 2.51 |
| Interest Cover: (EBITDA / Net Interest Paid) | 3.54 | 3.53 | 3.56 | 3.58 | 3.77 |
| Cash Flow before Interest / Cash Net Interest | 1.06 | 0.74 | (0.47) | 0.61 | (0.01) |
| **Income Leverage (Debt Repayment Ability)** | | | | | |
| Gross Debt / Cash Retained Profit (years to repay) | 50.3 | 29.9 | 46.9 | 840.4 | 78.0 |
| Net Debt / Retnd. Profit + Goodwill Amort.(years to repay) | 46.6 | 27.9 | 42.9 | 818.0 | 75.2 |
| Net Debt / Sustainable Retained Profit | 15.0 | 15.8 | 19.5 | 19.4 | 42.0 |
| Net Debt / EBITDA | 5.06 | 5.04 | 5.49 | 5.47 | 5.62 |