



Investor Report and Compliance Certificate

For the SWS Financing Group

For the period ended 30 September 2012

Confidential

Important Notice

This report is being distributed in fulfilment of a finance document, the Common Terms Agreement. It is directed to, and intended for, existing investors in the company. No other persons should act or rely on it. The company makes no representation as to the accuracy of forecast information. This report should not be relied on as a guide to future performance and should not be relied on in deciding whether to undertake future investment in the company. It should be noted that the information in this report has not been reviewed by the company's auditors.

Investor Report

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General overview and business update

This Investor Report covers the six months ended 30 September 2012. The Investor Report is a requirement of the Common Terms Agreement (CTA), which governs the company's obligations to its lenders and investors.

Capitalised terms used in this Investors Report/Compliance Certificate shall have the same definitions as in the CTA.

General levels of service

Water resource is at average levels for this time of year. This six months period commenced with water restrictions across part of the region (following two successive dry winters), which was followed by an exceptionally wet summer.

From 2010/11, the Service Incentive Mechanism (SIM), a quantitative and qualitative customer service score, replaced the overall performance assessment, and scores from 2011/12 financial year will contribute towards the score that will determine comparative performance for regulatory price setting. The company SIM score for financial year 2011/12 was 65 (out of 100), a 20% improvement on the score in 2010/11 of 54.

Financial performance for the six months ended 30 September 2012

Turnover increased by 9.6% to £390.6m (September 2011: £356.3m) compared with an average tariff increase of 8.8%. The remaining increase in turnover relates to a reduction in void properties as a result of an improvement project, partly offset by a reduction in demand from the period of drought followed by the wet summer. Operating profit increased by 18.8% to £167.5m (September 2011 £141.0m). No final dividend was declared for 2011/12 or interim dividend declared for this period.

Net cash flow from operating activities increased by 2.7% to £246.9m (September 2011 £240.5m).

Financial ratios

As required by the CTA, financial ratios are reported up to the end of the current five year regulatory period. In all cases, the financial ratios are within the 'trigger levels' as defined in the CTA. The forecasts used to generate the financial ratios are derived from the SWS Business Financial Model and are in the format specified by the CTA.

Financial forecasts in this report fully reflect the projected shortfall in revenues against those assumed in the PR09 price determination (in the order of £150m over this AMP period), projected costs associated with the adoption of private sewers (£33m over the AMP period), plus other cost pressures such as the carbon reduction commitment levy on energy costs.

Short term forecast RPI's used for this Investor Report are calculated as the average of inflation forecasts published by a number of UK banks. The forecast RPI for March 2013 is 2.6%, and a long term forecast of 2.5% is used for remaining years. RPI at March 2012 was 3.6%

For investor reporting, interest paid is reported on an accruals basis in line with the requirements of the CTA.

Projected distributions comprise preference share dividends and group relief tax payments.

Operational performance

Leakage performance for 2011/12 was the best ever for the company at 82 MI/d (Ofwat target for 2011/12 was 93 MI/d, and 90 MI/d for 2012/13).

Drinking water compliance for the 2011 Calendar year was 99.88% (2010: 99.90%). This is a key measure of the quality of water received by customers. Maintaining compliance as close to 100% as practicable is a key target to ensure consistently high standards to customers.

Serviceability performance for each of Water non-infrastructure, Water infrastructure, Wastewater non-infrastructure and Wastewater infrastructure was assessed as 'Stable' for 2011/12.

Capital expenditure

Net capital expenditure for the six months ended 30 September 2012 was broadly in line with expectations at £160.6m.

Financing

On 7 July 2011, Moody's downgraded the rating on the Class A debt from A3 to Baa1 (negative outlook), the Class B debt from Baa3 to Ba1 (negative outlook) and the corporate family rating from Baa1 to Baa2 (negative outlook). On 15 July 2011, Fitch also downgraded the rating on the Class A debt from A (negative outlook) to A- (stable outlook) and the Class B debt from BBB+ (negative outlook) to BBB (stable outlook). On 7 May 2012 Standard and Poor's place the Class A debt rating of A- on negative outlook and the Class B debt rating of BBB on negative outlook.

Board membership

Robert Jennings was appointed as an independent non-executive Director in July 2012.

Ultimate parent company

The ultimate parent company is Greensands Holdings Ltd.

Consolidated cashflow

Ref.		31 Mar 2010 £m	31 Mar 2011 £m	31 Mar 2012 £m	31 Mar 2013 £m	31 Mar 2014 £m	31 Mar 2015 £m
	Revenue						
1	Appointed	669.0	684.0	711.0	763.9	796.2	806.6
2	Non Appointed	5.3	3.9	5.2	4.4	5.1	5.3
	Operating Costs						
3	Appointed	213.5	223.6	227.1	254.1	265.8	277.7
4	Non Appointed	2.7	1.9	2.0	1.6	1.7	1.7
	Exceptional operating cash outflow *	56.1	0.0	0.0	0.0	0.0	0.0
5	Net Capital Expenditure (inc Disposals of Assets)	212.5	375.9	453.4	402.1	395.3	257.9
	Annual Finance Charge	136.5	131.9	122.1	126.1	132.2	127.5
6	Taxation	0.0	0.0	0.1	0.1	0.2	3.6
	Payments on Subordinated Debt and Distributions	23.5	65.8	38.3	26.1	23.2	18.9
	Net cash reserves movement	29.5	-111.2	-126.8	-41.8	-17.1	124.6

* This relates to a one-off payment into the final benefit pension scheme

Annual Finance Charge

Ref.		31 Mar 2010 £m	31 Mar 2011 £m	31 Mar 2012 £m	31 Mar 2013 £m	31 Mar 2014 £m	31 Mar 2015 £m
	Class A debt interest	118.5	107.6	99.4	100.9	105.1	107.1
	Class B debt interest	21.6	21.8	22.9	24.7	26.5	20.6
	Interest income	4.9	2.2	2.4	1.7	1.6	2.4
	Class A Facilities commitment fees	1.3	4.7	2.2	2.2	2.2	2.2
7	Class A Debt Interest	114.9	110.1	99.2	101.4	105.7	106.9
8	Senior Debt Interest	136.5	131.9	122.1	126.1	132.2	127.5
	Annual Finance Charge	136.5	131.9	122.1	126.1	132.2	127.5
	Monthly Payment Amount *	12.0	11.2	10.4	10.6	11.1	10.8

* Monthly payment amount is stated gross and reduced by interest received in the DSPA

Cash accounts and reserves

Ref.	31 Mar 2010 £m	31 Mar 2011 £m	31 Mar 2012 £m	31 Mar 2013 £m	31 Mar 2014 £m	31 Mar 2015 £m
SWS O&M Reserve account						
Opening balance	44.4	46.3	46.3	46.3	46.3	46.3
Cash transferred	1.9	0.0	0.0	0.0	0.0	0.0
Closing balance	46.3	46.3	46.3	46.3	46.3	46.3
Capex Reserve account						
Opening balance	312.8	216.0	125.5	25.5	41.9	24.8
Cash transferred	-96.8	-90.5	-100.0	16.4	-17.1	124.6
Closing balance	216.0	125.5	25.5	41.9	24.8	149.4
Debt Service Payment account						
Opening balance	10.8	11.5	5.0	20.4	0.0	0.0
Cash transferred	0.7	-6.5	15.4	-20.4	0.0	0.0
Closing balance	11.5	5.0	20.4	0.0	0.0	0.0
SWS Operating accounts						
Opening balance	0.9	30.6	0.8	3.6	0.0	0.0
Cash transferred	29.7	-29.8	2.8	-3.6	0.0	0.0
Closing balance	30.6	0.8	3.6	0.0	0.0	0.0
Total Cash Balances						
Opening balance	368.9	304.4	177.6	95.8	88.2	71.1
Cash transferred	-64.5	-126.8	-81.8	-7.6	-17.1	124.6
Closing balance	304.4	177.6	95.8	88.2	71.1	195.7

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Bonds, Authorised Loan Facilities and Leases

Ref.	31 Mar 2010 £m	31 Mar 2011 £m	31 Mar 2012 £m	31 Mar 2013 £m	31 Mar 2014 £m	31 Mar 2015 £m
* Senior £350m A1 6.192% Fixed Rate Bonds due 2029	350.0	350.0	350.0	350.0	350.0	350.0
* £150m A2a 3.706% Index Linked Bonds due 2034	179.6	188.2	197.6	203.8	209.4	214.6
* £35m A2b 3.706% Limited Index Bonds due 2034	41.9	43.9	46.1	47.6	48.9	50.1
£350m A4 6.64% Fixed Rate Bonds due 2026	350.0	350.0	350.0	350.0	350.0	350.0
£150m A5 3.816% Index Linked Bonds due 2023	179.6	188.2	197.6	203.8	209.4	214.6
* £350m A7 5.0% Fixed Rate Bonds due 2021	350.0	350.0	350.0	350.0	350.0	350.0
* £150m A8 5.0% Fixed Rate Bonds due 2041	150.0	150.0	150.0	150.0	150.0	150.0
* £200m A9 4.5% Fixed Rate Bonds due 2052	200.0	200.0	200.0	200.0	200.0	200.0
* £300m A10 5.125% Fixed Rate Bonds due 2056	300.0	300.0	300.0	300.0	300.0	300.0
£300m A11 6.125% Fixed Rate Bonds due 2019	300.0	300.0	300.0	300.0	300.0	300.0
RPI accretion on Index-Linked swaps	70.4	97.4	169.9	214.5	250.8	291.1
£250m B1 step-up Fixed/Floating rate Bonds due 2038	250.0	250.0	250.0	250.0	250.0	0.0
New £250m B2 Bond/Loan	0.0	0.0	0.0	0.0	0.0	250.0
£50m Class B loan facility	50.0	50.0	100.0	150.0	150.0	150.0
* £165m Artesian 4.076% Index Linked Bonds due 2033	197.5	207.0	217.3	224.2	230.3	236.1
* £156m Artesian 3.635% Index Linked Bonds due 2032	182.7	191.5	201.2	207.4	213.1	218.4
** New cash required	0.0	0.0	0.0	0.0	0.0	0.0
Revolving Credit Facilities	0.0	0.0	0.0	0.0	0.0	0.0
DSR Liquidity Facility Drawings	0.0	0.0	0.0	0.0	0.0	0.0
Finance Leases	0.0	0.0	0.0	0.0	0.0	0.0
Class A Indebtedness	2851.7	2916.2	3029.7	3101.3	3161.9	3224.9
Senior Indebtedness	3151.7	3216.2	3379.7	3501.3	3561.9	3624.9
10 Class A Net Indebtedness	2547.3	2738.6	2933.9	3013.1	3090.8	3029.2
11 Senior Net Indebtedness	2847.3	3038.6	3283.9	3413.1	3490.8	3429.2
Nominal value of fixed rate debt swapped to Index Linked	877.0	877.0	1318.0	1318.0	1318.0	1318.0

* Wrapped by MBIA or FSA

** 'New cash required' is a notional class of debt included to forecast compliance ratios correctly. This is not an attempt to forecast the actual quantum, mix, cost and timing of future financing.

Interest Cover Ratios

	Trigger	Default	31 Mar 2010 £m	31 Mar 2011 £m	31 Mar 2012 £m	31 Mar 2013 £m	31 Mar 2014 £m	31 Mar 2015 £m		
A	Net Appointed Income (1+3+6)		455.5	460.4	483.8	509.7	530.2	525.3		
B	Net Total Income (1+2+3+4+6)		458.1	462.4	487.0	512.5	533.6	528.9		
C	Depreciation (CCD & IRC)		259.5	279.0	306.9	323.7	336.5	346.0		
D	Class A Debt interest (7)		114.9	110.1	99.2	101.4	105.7	106.9		
E	Senior Debt interest (8)		136.5	131.9	122.1	126.1	132.2	127.5		
F	Period end VAT debtor		4.4	7.0	8.9	7.8	7.7	5.4		
G	Capital Maintenance (MNI & IRE)		92.4	164.2	223.8	N/A	N/A	N/A		
Class A Adjusted ICR										
	Historic: (B-C+F)/D	Projected: (A-C+F)/D	1.3	N/A	1.8	1.7	1.9	1.9	1.7	
Class A Average ICR			1.4	N/A	1.8	1.9	1.9	1.8	1.7	
Senior Adjusted ICR										
	Historic: (B-C+F)/E	Projected: (A-C+F)/E	1.1	N/A	1.5	1.4	1.6	1.5	1.5	
Senior Average Adjusted ICR			1.2	N/A	1.5	1.5	1.5	1.5	1.5	
Class A ICR										
	Historic: B/D	Projected: A/D	N/A	1.6	4.0	4.3	5.0	5.1	5.1	5.0
Class A Post Maintenance ICR										
	Historic: (B-G+F)/D		N/A	1.0	3.2	2.8	2.7	N/A	N/A	N/A

Regulatory Asset Ratios

		Trigger	Default	31 Mar 2010 £m	31 Mar 2011 £m	31 Mar 2012 £m	31 Mar 2013 £m	31 Mar 2014 £m	31 Mar 2015 £m
G	Class A Net Indebtedness (10)			2547.3	2738.6	2933.9	3013.1	3090.8	3029.2
H	Senior Net Indebtedness (11)			2847.3	3038.6	3283.9	3413.1	3490.8	3429.2
I	RCV			3566.9	3745.1	4044.0	4250.2	4355.2	4440.9
Class A RAR									
	Projected: G/I	0.750	N/A	0.714	0.731	0.725	0.709	0.710	0.682
Senior RAR									
	Projected: H/I	0.900	0.950	0.798	0.811	0.812	0.803	0.802	0.772

The opening RCV on 1 April 2010 was reduced by £99m, the most significant part of which was a "log down" for uncommitted expenditure on the Brighton & Hove scheme, with delayed expenditure on that scheme forming part of the capital expenditure programme for AMP5.

Opening RCV for the next AMP6 period, may also be adjusted as a result of variance to projected capital expenditure and changes to the notified index. This is presently forecast to be a reduction of c£130m, resulting in an adjusted opening Senior RAR of 0.795, and Class A RAR of 0.703.

Declaration

We confirm that each of the above Ratios has been calculated in respect of each of the relevant periods for which it is required under the Common Terms Agreement and has not breached the Trigger Event Ratio Levels and has not caused Paragraph 20 (Ratios) of Part 2 (Event of Default (SWS and the Issuer)) of Schedule 7 of the Common Terms Agreement to be breached.

We confirm that the Annual Finance Charge is £126.1m for 2012/13 equating to a Monthly Payment Amount for this period of £10.6m.

We also confirm that no Default or Potential Trigger Event is outstanding and that SWS's insurances are being maintained in accordance with the Common Terms Agreement.



Matthew Wright
Director



Matthew Wright
Director



Mick Carmedy
Chief Financial Officer

for and on behalf of Southern Water Services Limited



Mick Carmedy
Chief Financial Officer

for and on behalf of Southern Water Services (Finance) Limited