



Tideway

Tideway HoldCo Group
Investor Report H1 2016/17
22 December 2016

Notice

IMPORTANT NOTICE

This Investor Report is being distributed by Bazalgette Tunnel Limited (as 'Holdco Group Agent') on behalf of the Holdco Group pursuant to the Common Terms Agreement.

This Investor Report contains forward looking statements that reflect the current judgment of the management of the Obligors regarding conditions that it expects to exist in the future. Forward looking statements involve risks and uncertainties because they relate to events and depend on circumstances that will occur in the future and, accordingly, are not guarantees of future performance. Management's assumptions rely on its operational analysis and expectations for the operating performance of each of the Obligor's assets based on their historical operating performance and management expectations as described herein. Factors beyond management's control could cause events to differ from such assumptions and actual results to vary materially from the expectations discussed herein. Investors are cautioned that the assumptions and forecast information included herein are not fact and should not be relied upon as being necessarily indicative of future results and are cautioned not to place undue reliance on such assumptions and forecast information. It should also be noted that the information in this Investor Report has not been reviewed by the Obligors' auditors.

BASIS OF PREPARATION

Investor Reports relate to the performance of the Holdco Group which includes Bazalgette Tunnel Limited. This Investor Report comments on the historical financial performance of the Holdco Group for the period to 30 September 2016.

Defined terms used in this document have the same meanings as set out in the Master Definitions Agreement unless otherwise stated.

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Overview

This Investor Report provides an update of Tideway's activities for the period to 30 September 2016. It covers business, regulatory and financing developments.

Over the period Tideway has made good progress towards its ambition to deliver safely the Thames Tideway Tunnel as early as possible:

- We continue to develop our transformational approach to health, safety and wellbeing, and are pleased to report that we have had no major injuries to date
- We have mobilised each of the three main tunnel drive sites between three and five months earlier than the original schedule
- With progress to date, we believe we are well placed to meet our target of handing over the Thames Tideway Tunnel to Thames Water to operate earlier than the baseline date, consistent with our licence, of 2024
- The programme's estimate-at-completion figure remains at £3.144bn (2014/15 prices), which is in line with our regulatory baseline
- Our financing plan has been significantly de-risked with £1.05bn of debt capital raised in the period, and additional £100m raised post period end. As of 30 September, our liquidity horizon was to 2022
- Post period end the new pier at Blackfriars was opened, and we started digging the shaft at Kirtling Street

Business update

Health, Safety and Wellbeing

We are pleased to report that there were no significant injuries during the six-month period. The accident frequency rate (the number of incidents resulting in greater than three days lost time per 100,000 hours worked) was 0.11 for the period, below the average for similar construction programmes.

Our transformational HSW strategy, 'RightWay', continues to be delivered across the project. From the start of the project to 30 September 2016, 4,760 people have attended EPIC - our industry-leading, interactive induction centre. The focus of RightWay in 2016 has been 'RightStart', the implementation of actions and standards designed to prevent those incidents that typically occur at the start of major projects – 'starting the RightWay'. RightStart will be undertaken at all construction sites and, during the period, evaluations were undertaken at the three main drive sites – Carnwath Road, Kirtling Street and Chambers Wharf.

Company and People

We launched a company-wide initiative to support leaders across the organisation, who are empowered and trusted to make decisions at the appropriate level.

We launched the Tideway Information Management project, with the aim of uniting information management in one effective, clear and usable solution. The project aims to improve information management by simplifying our approach, making information more accessible, and promoting better control.

Vision, Legacy and Reputation

We are helping deliver our vision of 'Reconnecting London, and Londoners, with the River Thames' through supporting community activities in the Boroughs where we work. These events have included the historic Doggett's Coat and Badge Race, the Totally Thames Festival, Source to Sea stand-up paddleboard relay as well as backing the Thames21 Citizen Science Initiative to monitor the health of the river. Tideway's staff community and STEM volunteering programme ramped up significantly in participation, with the project team (including the Main Works Contractors) volunteering 2,605 hours by half year. The Thames Skills Academy, which will train a new generation of river workers, was launched in the period.

Tideway has developed a 'more by river' strategy which will minimise the impact of road traffic movement on local communities and goes beyond the commitments of our Development Consent Order (DCO). The 'more by river' strategy has seen mobile office units for the Chambers Wharf and Carnwath Road sites transported to site by river.

Our community relations programme established working groups at several key sites, providing a forum for Tideway to engage with local residents and businesses through the life of the project. We have been working well with stakeholders and the consent granting authorities to secure the consents necessary to maintain the schedule, including early mobilisation to key sites.

Investment programme

Schedule, Cost and Quality

Progress on the construction schedule in the first six months of 2016/17 was ahead of the regulatory baseline, with the main tunnel drive sites in the West, Central and East sections of the tunnel mobilised three to five months early and, shortly after period end, two of the six tunnel boring machines ('TBMs') had been ordered.

In the West section, site preparation started at the Carnwath Road main drive site and Hammersmith Pumping Station. At Carnwath Road, work took place to progress the design and initial consents were secured post period end to strengthen the river wall in advance of our main shaft construction. The contractor has secured a letter of intent with the manufacturer for the procurement of the main tunnel TBM for the West section.

In the Central section, sheet piling for the shaft at the Kirtling Street main drive site has been completed. Shortly after period end the diaphragm wall construction commenced and both the TBMs were procured. Good progress was made during the period to relocate the Millennium Pier at Blackfriars and following the period end the new pier opened for riverboats to the east of Blackfriars Station together with a new lift and stairs.

In the East section, ground treatment, jetty demolition and temporary cofferdam piling have started at the Chambers Wharf main drive site. This will create the space we need to construct the main tunnel drive shaft. In line with our commitment to utilise the river more, the site offices were delivered by barge and these are now in use. Site investigation works have been completed at Greenwich Pumping Station that will inform the temporary and permanent works on the site.

The system integrator has, as planned, commenced the survey and inspection of the existing sewer network.

We continued to explore the potential for directly integrating Thames Water's proposed Counter's Creek sewer flooding alleviation scheme with our works at Cremorne Wharf. We submitted a Proposed Variation Notice (PVN) for Counter's Creek to the Liaison Committee, whose attendees include Defra, Ofwat, the Environment Agency and Thames Water. The PVN is the first stage in an on-going process with stakeholders to consider the integration of the scheme.

Total project costs for the six month period were £163.8m, taking the total costs to date to £325.0m. The tunnel's estimate-at-completion figure remains at £3.144bn (2014/15 prices), which is in line with our regulatory baseline.



New Blackfriars pier



Chambers Wharf sites offices delivered by river



Excavation of first shaft started at Kirtling Street

Financing activity

Over the period to 30 September we have significantly de-risked our financing plan, increasing our liquidity position and locking-in financing costs in the low rate environment:

- On 12 May we closed a £700m 35-year loan with the EIB. The structure of the loan enables Tideway to lock-in financing costs whilst matching its funding requirements and profiling debt service in line with the expected growth in our asset base
- On 2 June we priced four index-linked bonds totalling £100m. The bonds have deferred purchase dates of June 2020 and June 2021, and maturity dates of 2048 and 2054
- On 15 June we priced three index-linked bonds totalling £250m. The bonds have deferred purchase dates of June 2018, June 2019, and June 2020; and maturity dates of 2050, 2051 and 2052, respectively
- As at 30 September, Tideway entered into hedging transactions to lock-in the cost for the period to 2030 on a RPI basis of £240m notional value of the EIB loan
- Post period-end we issued a further index-linked £100m bond with deferred purchase date of December 2018, and maturity date of 2040; and hedged additional £240m notional value of the EIB loan

Tideway submitted a Revenue Statement for the year 2017/18. The IP Charge Estimate for the year 2017/18 is £28.6m, which takes into account the difference between forecast and actual investment in the previous years.

As at 30 September, the balance of equity was £266.0m and shareholder loans was £384.8m, which include the injection of £40.2m in equity and £60.3m draw on the shareholder loan as well as £11.8m of principal repayment on 30 September.

In line with our strategy to fund the early stages of our investment programme using our shareholders' funds, our £1bn revolving credit facility (RCF) remained undrawn during the period.

At 30 September, we had total liquidity in excess of £1.9bn, comprising £0.3bn of cash, £0.6bn of committed and undrawn capital from shareholders and the £1bn undrawn RCF.

Historical financial performance

During the six month period ended 30 September 2016, Tideway reported a loss of £30.3m. We do not consider the reported loss in the period is a reflection of the performance of the business. The loss reflects the movement in the fair value in the Holdco Group's financial instruments (see next page for more detail).

Tideway capitalises costs that meet the capitalisation criteria for assets under construction and revenue is reported as deferred income during the construction phase. At 30 September 2016, costs of £325.0m were capitalised within the asset under construction on the statement of financial position. This represents £163.8m of costs during the period and £161.2m for the prior period to 31 March 2016.

Main works costs

Main works costs are split between the three regional contracts West, Central and East for the design and construction of the Main Tunnel, the system integrator contract and the Volker Stevin marine contract. The three regional main works contracts are based on the New Engineering Contract (NEC3) Option C Target Price with Activity Schedule terms and conditions.

The costs incurred in the period include contractors' staff, design, consents and preliminary costs to support mobilisation, site preparation activities at key sites across the project and also to support the "Right Start" readiness programme.

Other direct costs

The other direct costs of £3.2m mainly consist of third party costs for the management, monitoring and mitigation of the impact of construction on third parties and safety training costs.

Indirect costs

The largest indirect costs are resource costs of £29.9m which includes the staff cost of those employed directly by the Holdco Group or through framework contracts and the resource costs of the programme delivery partner CH2M. Other indirect costs include non-resource costs such as information systems, premises and insurance.

Excluded costs

Excluded costs to 30 September 2016 are £17.1m which largely reflects financing costs such as interest on shareholder loans and costs related to the Holdco Group's debt financing activities such as bank fees, legal advice and rating agency fees.

Analysis of costs and cash outflows	Costs £m	Timing difference £m	Cash outflows £m
Direct costs	104.1	(3.6)	100.5
Indirect costs	42.6	1.2	43.8
Total allowable costs	146.7	(2.4)	144.3
Total excluded costs	17.1	14.7	31.8
Total	163.8	12.3	176.1
Cum as of 31/03/16	161.2		
Total	325.0		

Allowable costs	£m
Main works costs	100.9
Other direct costs	3.2
Direct costs	104.1
Resources	29.9
Other indirect costs	12.7
Indirect costs	42.6
Total	146.7

Historical financial performance (cont.)

Fair value measurements and valuation

During the six month period ending 30 September 2016, the Holdco Group entered into three long-term index linked swaps with commercial banks to hedge the interest rate of first three tranches of the EIB loan. The movement in fair value of these financial instruments is recognised in the Income Statement because under IAS 23 these do not represent current borrowing costs incurred for financing the project and so, unlike our other expenditure, cannot be capitalised.

As of 30 September, the fair value of those derivatives was £(30.3)m.

Tax

We have made a disregard election to HMRC effective 1 April 2016, which means that any gains or losses arising from movements in the fair value will be disregarded for current tax purposes.

A corporation tax charge of £nil was recognised in the period, which reflects the position that the Holdco Group did not have any taxable profits.

Cash flow

During the period, Tideway received equity and loans from its shareholders totalling £319.2m, and collected £16.9m in revenue, including £14.5m regulated revenue received from Thames Water and £2.4m of other inflows including interest and payments for other services provided to Thames Water.

In September 2016, £11.8m of principal was repaid.

Cash outflows of £176.1m includes £163.8m of investment on the construction of the tunnel and working capital outflows of £12.3m.

Post period end, Tideway received £120m of shareholder injections on 15 December in the form of £48.0m equity and £72.0m of shareholder loans.

Net cash	£m
Balance 31/03/16	130.4
(Net) Shareholder Loans	179.7
Equity	127.7
Revenue	14.5
Other	2.4
Cash Inflows	324.3
Construction of the asset	(163.8)
Working capital	(12.3)
Cash outflows	(176.1)
Balance 30/09/16	278.6

Ratios

We confirm that in respect of this Investor Report dated 30 September 2016, by reference to the most recent Financial Statements that we are obliged to deliver in accordance with paragraph 1 (Financial Statements) of Part A (Information Covenants) of Schedule 3 (Holdco Group Covenants) of the Common Terms Agreement (the Agreement):

- a) the Senior RAR⁽¹⁾ in respect of the relevant Test Period is equal to 0%; this is below the 5% threshold set out in the Agreement and therefore we are not required to report FFO ICR⁽²⁾ and Average FFO ICR

We confirm that the above Ratio has been calculated in respect of the Test Period(s) or as at the Test Dates for which it is required to be calculated under the Agreement.

Description of ratios

(1) Senior RAR measures at a test date, the ratio of Senior Net Indebtedness to RCV

(2) FFO ICR measures in respect of a test period, the ratio of Net Cash Flow to Senior Debt Interest

Other reportable matters

Significant management and board changes

In September 2016, the Board appointed one Non-Executive Director, Angela Roshier, to replace Moira Turnbull-Fox as the DIF Shareholder Director.

On 26 September Lucy Webster joined as Head of External Affairs, replacing Phil Stride who is now Strategic Projects Director.

Other than those outlined above, there have not been any other board or relevant management changes in the period.

Acquisitions and disposals

We confirm that we have not made any material acquisition or disposal.

Current Hedging Position

As at 30 September, Tideway entered into hedging transactions to lock-in the cost for the period to 2030 on a RPI basis of £240m notional value of the EIB loan.

Post-period end, Tideway entered into additional hedges to lock-in the cost for the period to 2031 on a RPI basis of additional £240m notional value of the EIB loan.

Confirmation

We confirm that:

- a) no Default or Trigger Event has occurred and is continuing;
- b) the Borrower is in compliance with the Hedging Policy;
- c) the statements set out in this Investor Report are accurate in all material respects; and
- d) the insurances are being maintained in accordance with paragraph 28 (Insurance) of Part C (General Covenants) of Schedule 3 (Holdco Group Covenants) to the Common Terms Agreement.

Mark Corben,

A handwritten signature in black ink, appearing to read 'Mark Corben', with a stylized, flowing script.

Chief Financial Officer

For and on behalf of Bazalgette Tunnel Limited as Holdco Group Agent

Appendix

The table below summarises the requirements of the Investor Report and references in this document

Requirement	Reference
General overview	Page 4, Overview
Regulatory and business update	Page 5, Business Update Page 6, Investment Programme
Capital Expenditure	Pages 8-9, Historical Financial Performance
Financing	Page 7, Financing Activity
Acquisitions or Disposals	Page 11, Other Reportable Matters
Current Hedging Position	Page 11, Other Reportable Matters
Ratios	Page 10, Ratios