



**Affinity Water Programme Finance Limited**

*(incorporated with limited liability under the laws of the Cayman Islands with registered number 274647)*

**£2,500,000,000**

**Multicurrency programme for the issuance of Guaranteed Bonds**

**financing**

**Affinity Water Limited**

*(incorporated with limited liability in England and Wales with registered number 02546950)*

This Supplement (the “**Supplement**”) to the prospectus dated 1 September 2015 (the “**Prospectus**”) which comprises a base prospectus for the purposes of Section 87G of the Financial Services and Markets Act 2000 (the “**FSMA**”) and is prepared in connection with the £2,500,000,000 multicurrency programme (the “**Programme**”) established by Affinity Water Programme Finance Limited (the “**Programme Issuer**”).

This Supplement is supplemental to, and should be read in conjunction with, the Prospectus and any other supplements to the Prospectus issued by the Programme Issuer. The purpose of this Supplement is to:

- (i) incorporate by reference the financial results of the Programme Issuer, Affinity Water Limited (“**AWL**”) Affinity Water Holdings Limited (“**AWHL**”) and Affinity Water Finance (2004) PLC (the “**Existing Issuer**”) for the year ended 31 March 2016. The Programme Issuer, AWL, AWHL and the Existing Issuer, being the persons responsible for the financial information included in the financial results, approve such financial information; and
- (ii) disclose information and update risk factors related to the paper issued by Ofwat dated May 2016 entitled “Water 2020: our regulatory approach for water and wastewater services in England and Wales” (the “**Water 2020 Paper**”).
- (iii) disclose information and risk factors related to the paper issued by Ofwat dated July 2016 entitled “The costs and benefits of introducing competition to residential customers in England”.

Unless otherwise defined in this Supplement, terms defined in the Prospectus have the same meaning when used in this Supplement. Unless stated otherwise, page numbers referred to in this Supplement refer to pages in the Prospectus.

The Programme Issuer and each of AWL, AWHL and the Existing Issuer (together with the Programme Issuer, being the “**Obligors**”) accepts responsibility for the information contained in this Supplement. To the best of the knowledge of each of the Programme Issuer and the other Obligors (as appropriate) (having taken all reasonable care to ensure that such is the case) the information contained in this Supplement is in accordance with the facts and does not omit anything likely to affect the import of such information.

**Financial results of the Obligors**

On 30 June 2016, the Programme Issuer, AWL, AWHL and the Existing Issuer published their financial results for the year ended 31 March 2016. A copy of those financial results has been filed with the United Kingdom Financial Conduct Authority (the “**FCA**”) and, by virtue of this Supplement, those financial results are incorporated in, and form part of, the Prospectus. Copies of all documents incorporated by reference in the Prospectus can be obtained from the website of AWL at <https://stakeholder.affinitywater.co.uk/investor-relations.aspx> and from the Affinity Water

headquarters at Tamblin Way, Hatfield, Hertfordshire, AL10 9EZ, United Kingdom and from the specified offices of the Paying Agents for the time being, as described in the Prospectus. Please note, however, that the content of the website is not being incorporated by reference into the Prospectus by way of this Supplement.

## **Water 2020**

### ***Changes in the specified inflation index***

In 2013, the UK Statistics Authority (the “**Authority**”) commissioned Paul Johnson (director of the Institute for Fiscal Studies) to review the UK consumer price statistics. Paul Johnson’s report, published on 8 January 2015, recommended that the Office for National Statistics (“**ONS**”) should move towards making “CPIH” (a measure of CPI inflation including housing costs) its main measure of inflation.

In its Water 2020 Paper, Ofwat stated that it intends to amend all water company licences, including AWL’s Instrument of Appointment so that wholesale revenues will be indexed by CPI (or CPIH) from 1 April 2020. In addition, 50 per cent. of RCV as at 1 April 2020 would be indexed by RPI and the remainder of the RCV as at that date, plus any new RCV added after that date would be indexed by CPI (or CPIH). Additionally, Ofwat has signalled that it intends to implement a full transition to indexation by CPI (or CPIH) as soon as practicable.

The Financing Group has liabilities linked to RPI, including in the form of Indexed Bonds and RPI Linked Hedging Agreements. The mismatch following the change to CPI (or CPIH) (and the full transition to that measure which is anticipated) could lead to AWL not having sufficient resources to make payments of interest and principal in particular on these instruments which are linked to RPI. In addition, and in general, the transition to CPI (or CPIH) could have financial risks for the company in terms of RCV and revenue growth.

### ***Targeted price control – Water resources***

In line with its work on upstream market reforms and introducing competition, Ofwat has stated in its Water 2020 Paper that it intends to amend licences to create a separate binding price control for water resources. The water resource price control would differentiate between revenue for pre- and post-2020 water resource capacity. The latter would be exposed to utilisation risk, the former would not. The total revenue control would constitute two elements: (a) a fixed element (e.g. £X million per annum); and (b) a mechanistic in-period adjustment factor that allows for bilateral market entry.

RCV would be allocated to this new price control. However, Ofwat have stated that this would be done on an unfocussed basis – meaning that, instead of a methodology required to value the relevant constituent parts of the business, it would be for each water company in making its PR19 application to develop and justify the allocation of RCV for its water resource price control, which could lead to risks around the elements of unbundled RCV where these parts of the business become open to wholesale competition in the future. Ofwat have stated that they would provide guidance for water companies on what they are expecting from water companies in late 2016 and expect to ask for allocations from companies in 2017 to be finalised as part of PR19. Ofwat may revise the allocation of the RCV between “network plus” (meaning the wholesale water price control) and the water resources price control at PR24 if this is needed to adequately protect pre-1 April 2020 RCV.

In addition to these changes, an additional licence change would be made to ensure that basic information for supply-demand deficits and water resource costs in a consistent format is available and to require water companies to allow reasonable commercial and non-commercial use of this public data.

### ***Direct procurement***

Ofwat would also incentivise incumbent water undertakers to use direct procurement for suitable discrete enhancement schemes with a whole-life totex guideline value of more than £100 million.

### ***Extending retail competition to households***

In November 2015, the UK government published “A better deal”, its plan to boost competition in different markets and lower bills for firms and families. This publication stated that “Ofwat will provide an assessment by summer 2016 of the costs and benefits of extending retail competition to household water customers [in England]. Following this, the government will work with water companies to begin the transition to household retail competition before the end of this Parliament.”

On 18 July 2016, Ofwat published their initial findings regarding household retail competition ahead of producing their final report to government in September 2016. Any decision to open the household retail market in England to competition is for the UK government and Ofwat will not be making any recommendation as part of its final report.

To the extent that household customers are enabled by future legislation to obtain their water supply from a different supplier, this could introduce a degree of uncertainty into AWL's business and adversely affect AWL's turnover, which could adversely affect AWL's business, operational performance, profitability or financial condition and thus the Programme Issuer's ability to make timely payments under the Bonds.

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To the extent that there is any inconsistency between (a) any statement in this Supplement or any statement incorporated by reference into the Prospectus by this Supplement and (b) any other statement in or incorporated by reference in the Prospectus, the statements in (a) above will prevail.

Save as disclosed in this Supplement, no other significant new factor, material mistake or inaccuracy relating to information included in the Prospectus has arisen or been noted, as the case may be, since the publication of the Prospectus.

An investor should be aware of its rights arising pursuant to Section 87Q(4) of the FSMA.

If documents which are incorporated by reference to this Supplement themselves incorporate any information or other documents therein, either expressly or implicitly, such information or other documents will not form part of this Supplement for the purposes of the Prospectus Directive except where such information or other documents are specifically incorporated by reference or where this Supplement is specifically defined as including such information.

This Supplement has been approved by the FCA, which is the United Kingdom competent authority for the purposes of Directive 2003/71/EC (the "**Prospectus Directive**") and relevant implementing measures in the United Kingdom, as a base prospectus supplement issued in compliance with the Prospectus Directive and relevant implementing measures in the United Kingdom.