NAVIGATING UNCHARTED WATERS

The Importance of Scenario Planning

Vikki Williams and Laura Frudd
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Future Challenges

Many of the key principles from PR14 may remain…

Customer Engagement

- CCGs to remain with clearer scopes
- Revealed preference and choice experiment type approaches to drive better customer-based decision making

Totex

- Use of totex maintain including modelled approach to cost assessment

Outcomes

- Continue to encourage longer-term thinking by water companies through the outcomes, PCs and ODI framework

Price Controls and RCV

- 5 year price controls but set within longer-term plans with in-period adjustments
- Extension of protection for historical investments included in RCV up to Mar 2020

But a package of reforms will see further changes in six key areas.

Making More Use of Markets

- Separate price controls for water resources and sludge treatment – resulting in 4 core wholesale price controls

Access Pricing

- Establishing 'gate' or 'access' prices to allow efficient market entry

Ensuring Resilience

- Delivering Ofwat's new duty to ensure long-term stability of asset systems, ecosystems and financing to deliver services to consumers

Innovative Financing and Operating Models

- Competitive procurement for discrete large-scale enhancement projects

Sustainable Investment

- Phased movement from RPI to CPI indexation for both prices and RCV with 50% of RCV to be indexed to CPI

Risk-Based Review +

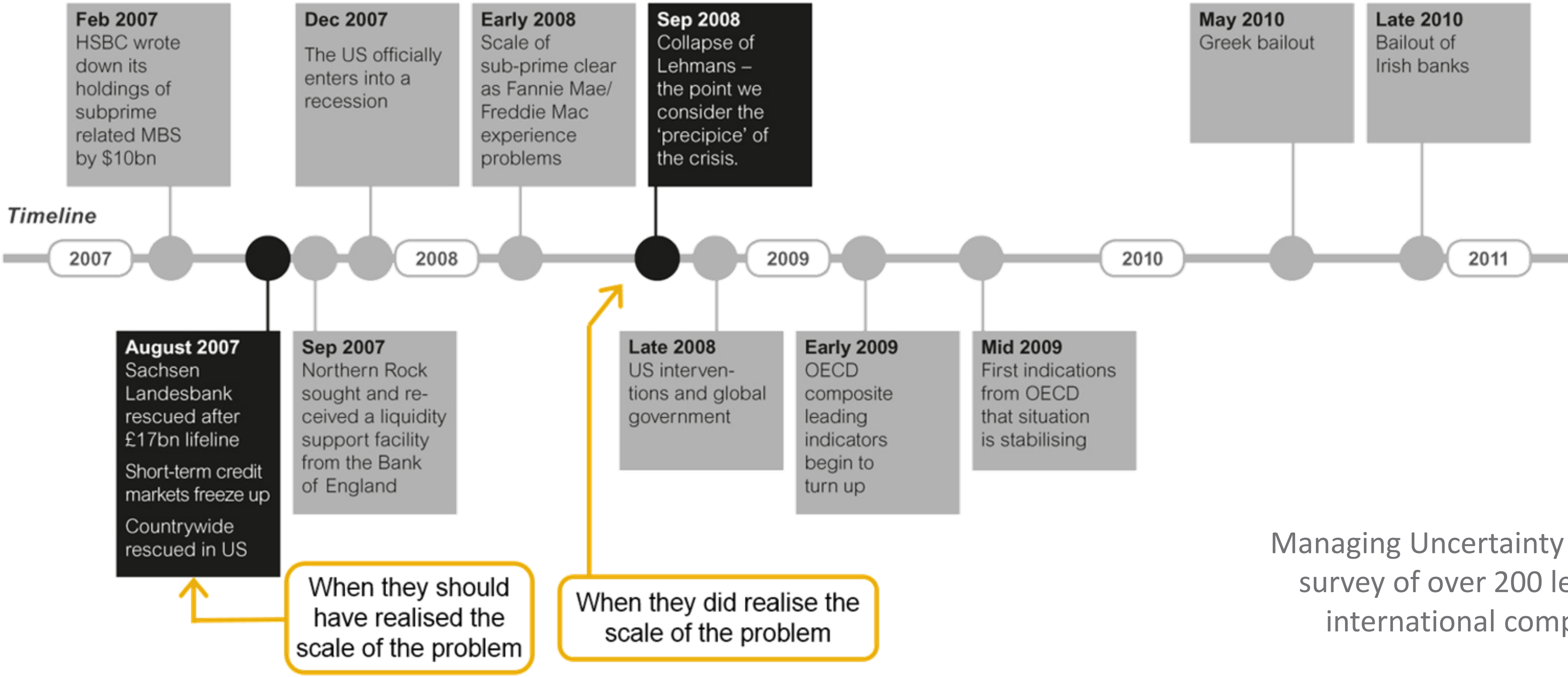
- The narrative /coherence around the 'story' needs to be better with greater collaboration and input from the supply chain

Let our advance worrying become advance thinking and planning

Winston Churchill

“What we know about the global financial crisis is that we don’t know very much”

Paul A Samuelson, Nobel laureate and eminent US economist

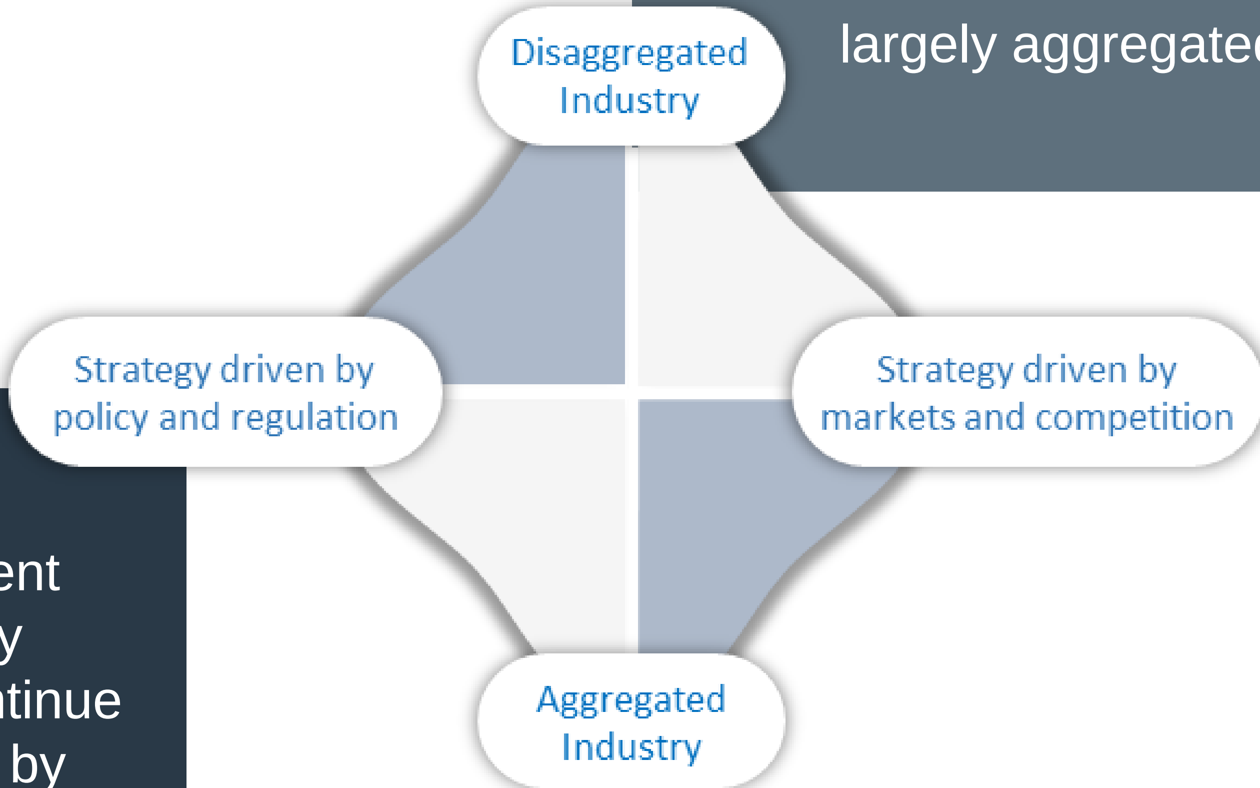


Managing Uncertainty – PA’s survey of over 200 leading international companies

Companies which adopted the strategic mindset experienced 10% higher shareholder return than those which adopted the tactical mindset.

Developing Future Scenarios for 2022

Will the water industry remain a largely aggregated monopoly industry?



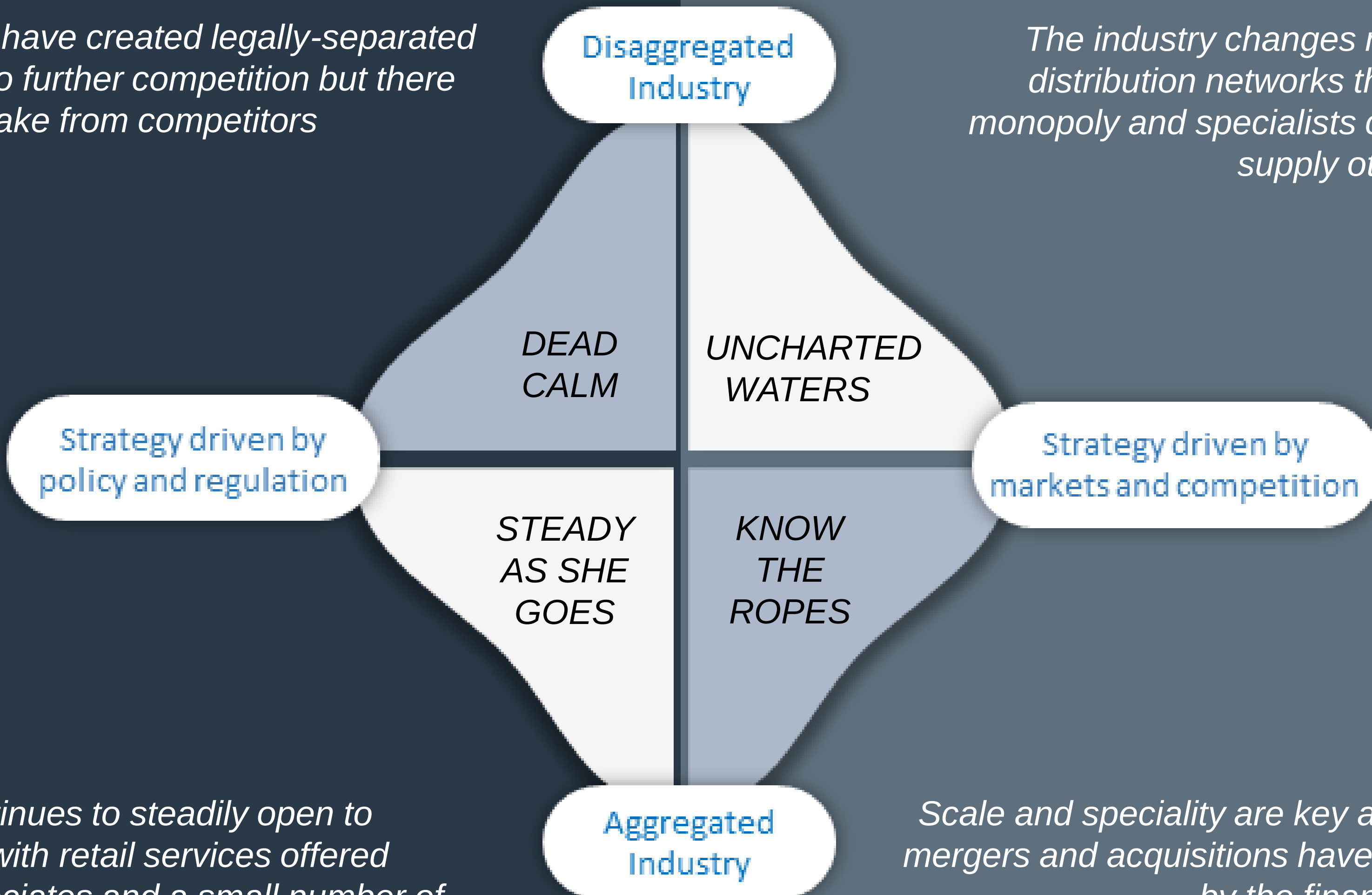
To what extent will company strategy continue to be driven by policy and regulation?

PA's 'Future Worlds' planning tool promotes innovative thinking by creating alternative scenarios to drive business and contingency planning

FUTURE WORLDS WATER SCENARIOS

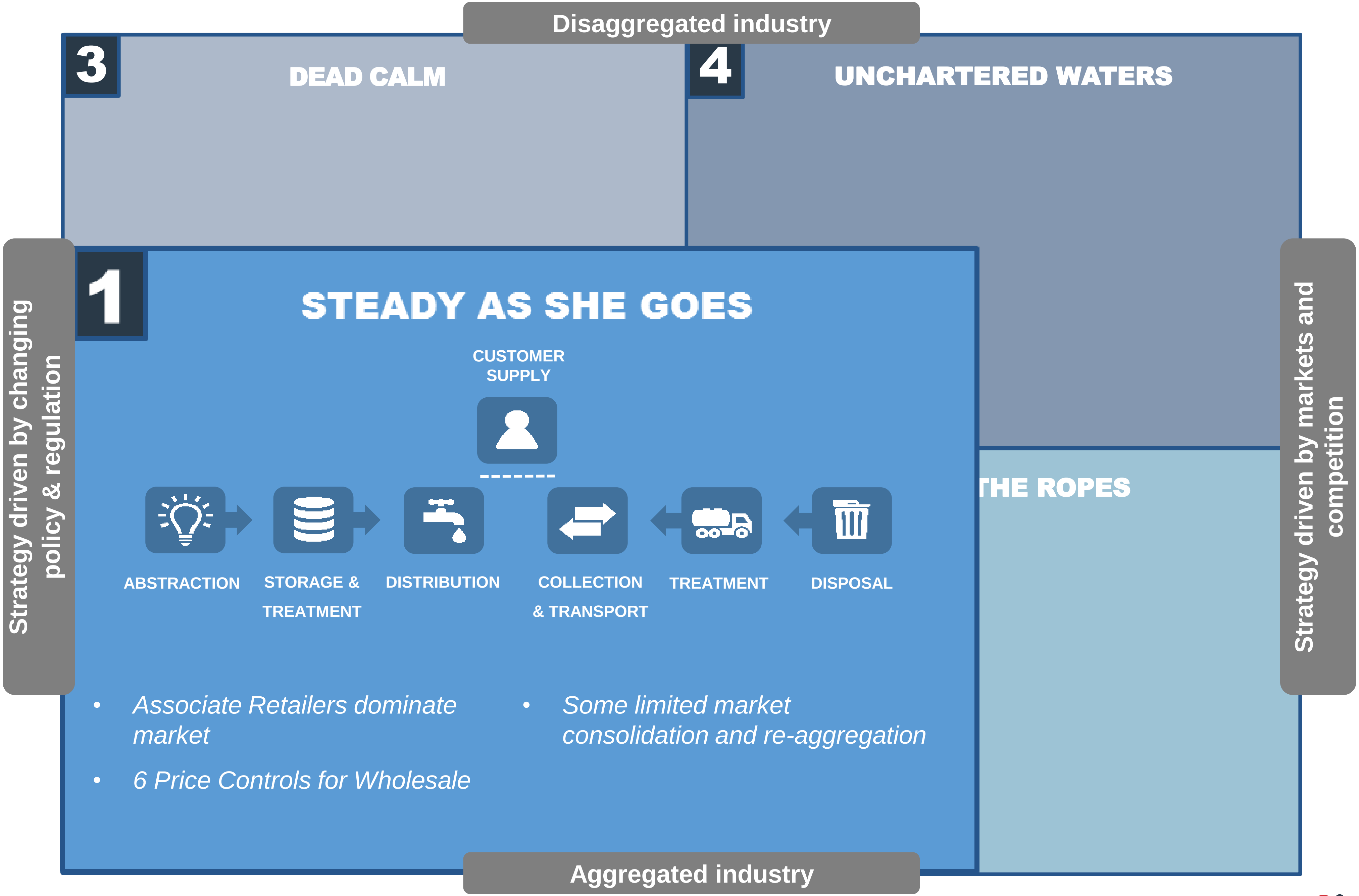
Wholesalers have created legally-separated businesses to further competition but there is limited uptake from competitors

The industry changes radically with distribution networks the remaining monopoly and specialists competing to supply other services

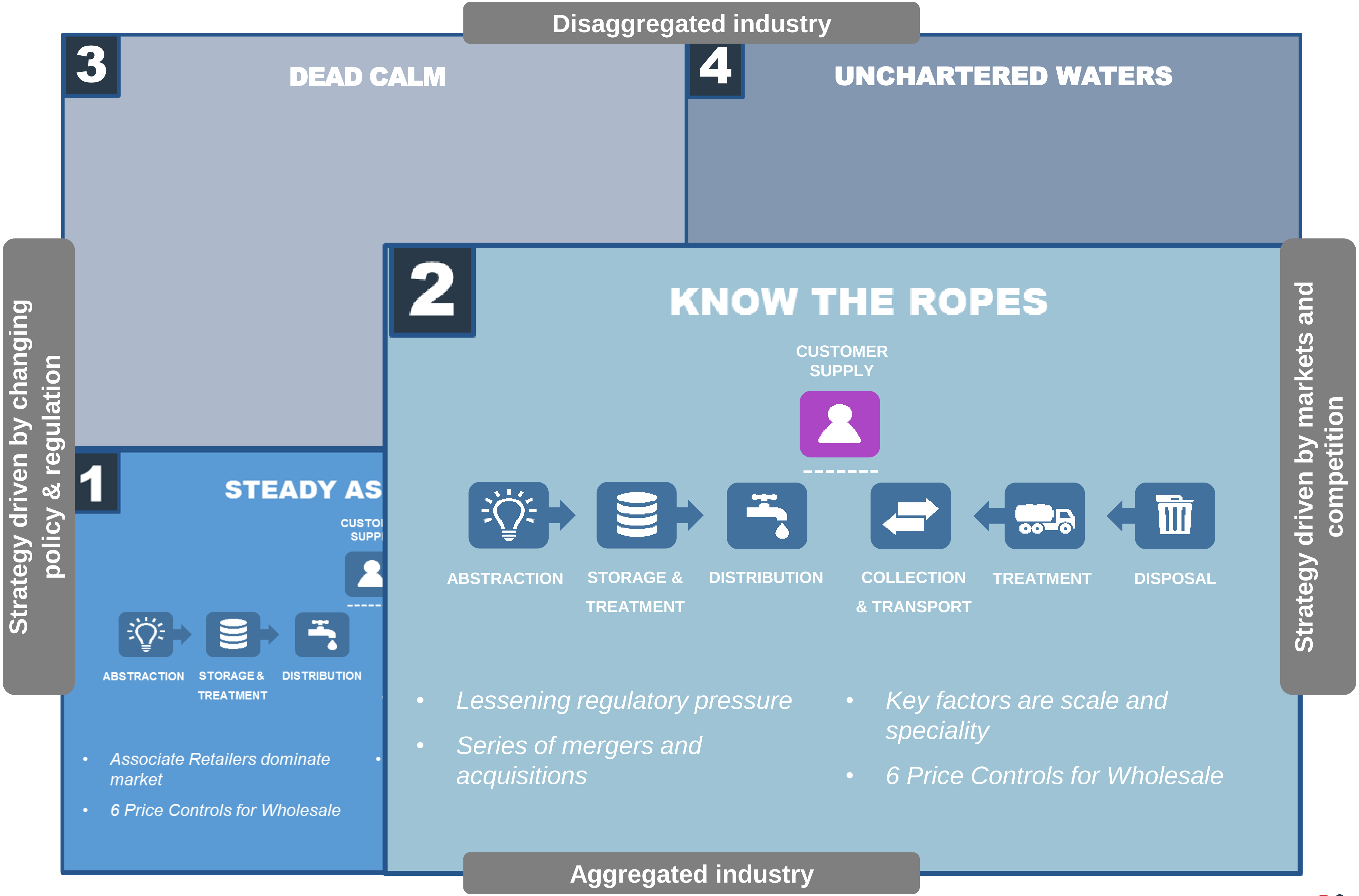


Industry continues to steadily open to competition with retail services offered through associates and a small number of new entrants

Scale and speciality are key as a series of mergers and acquisitions have been driven by the financial markets



- *Associate Retailers dominate market*
- *6 Price Controls for Wholesale*
- *Some limited market consolidation and re-aggregation*


Disaggregated industry
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DEAD CALM
4
UNCHARTERED WATERS
Strategy driven by changing policy & regulation
Strategy driven by markets and competition
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Aggregated industry

Disaggregated industry

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CUSTOMER SUPPLY

ABSTRACTION | STORAGE & TREATMENT | DISTRIBUTION | COLLECTION & TRANSPORT | TREATMENT | DISPOSAL

- *Water trading and sludge treatment and disposal legally-separated*
- *Continued strong policy and regulation*
- *Lack of incentive for competition*
- *Retail market stabilises around most efficient providers*

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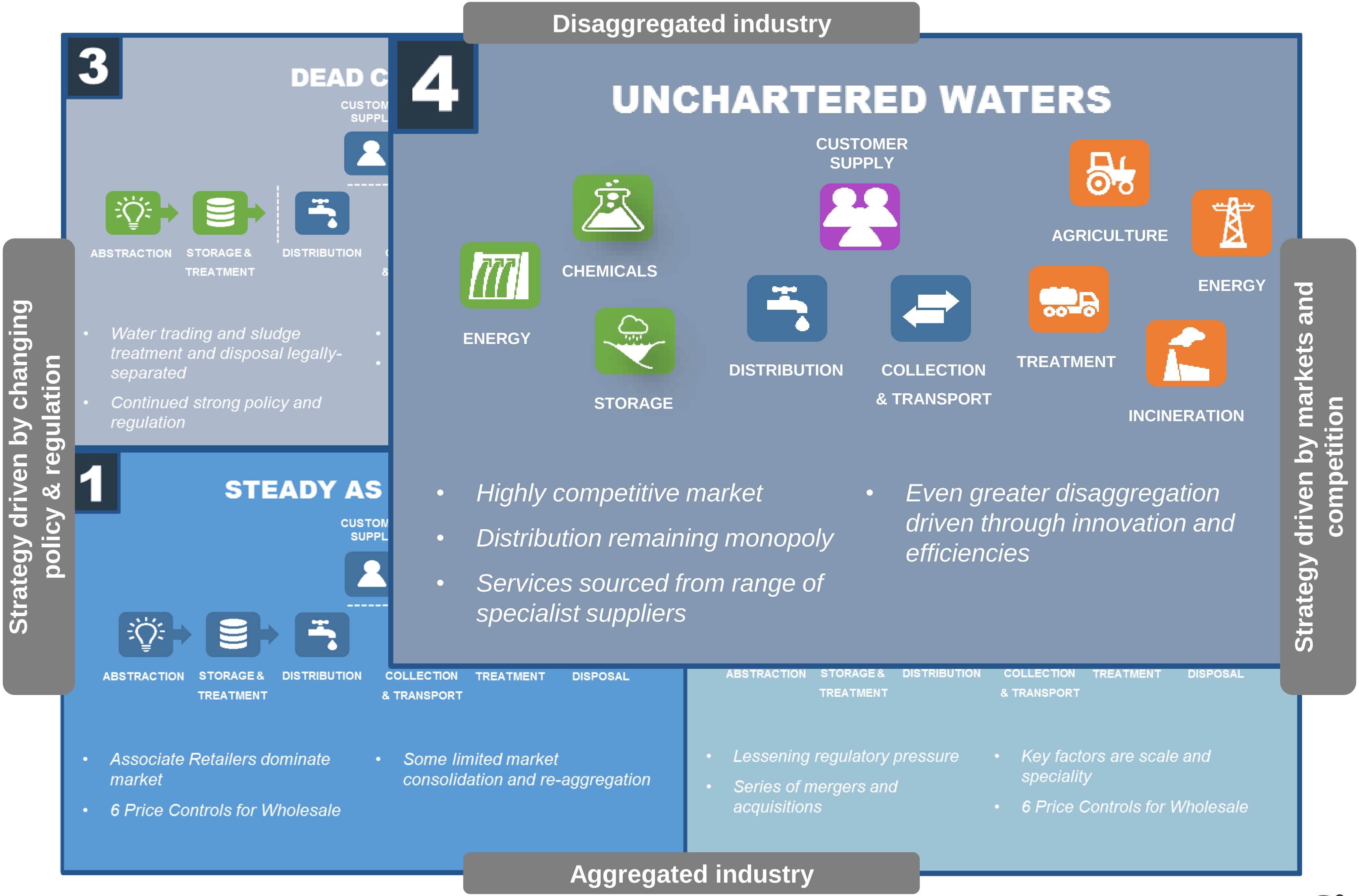
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Distribution remaining monopoly
Services sourced from range of specialist suppliers
Even greater disaggregation driven through innovation and efficiencies
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1. Identifying the questions or uncertainties they want to test (levers);
2. Considering the scenarios resulting from addressing those levers;
3. Determining the investment implications of each scenario;
4. Creating an action plan with immediate and contingent actions;
5. Implementing the immediate actions and setting up monitoring of key indicators to determine when to trigger contingent actions.

> In preparing for battle I have always found plans are useless, but planning is indispensable
>
> Dwight D Eisenhower, US President 1953-1961

END

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