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# PR14 Update From Severn Trent Revised Business Plan Submission

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1<sup>st</sup> July 2014

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# Context

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- Responded to Ofwat's guidance on risk and reward and the risk based review
- Constructive engagement with Ofwat and other stakeholders
- Discussion focused on 3 areas:
  - Birmingham resilience
  - Legacy adjustments
  - ODIs
- Main changes in revised plan:
  - Wholesale water totex (Birmingham)
  - WACC
  - Legacy adjustments
  - ODIs
- Plan is fair, balanced and financeable

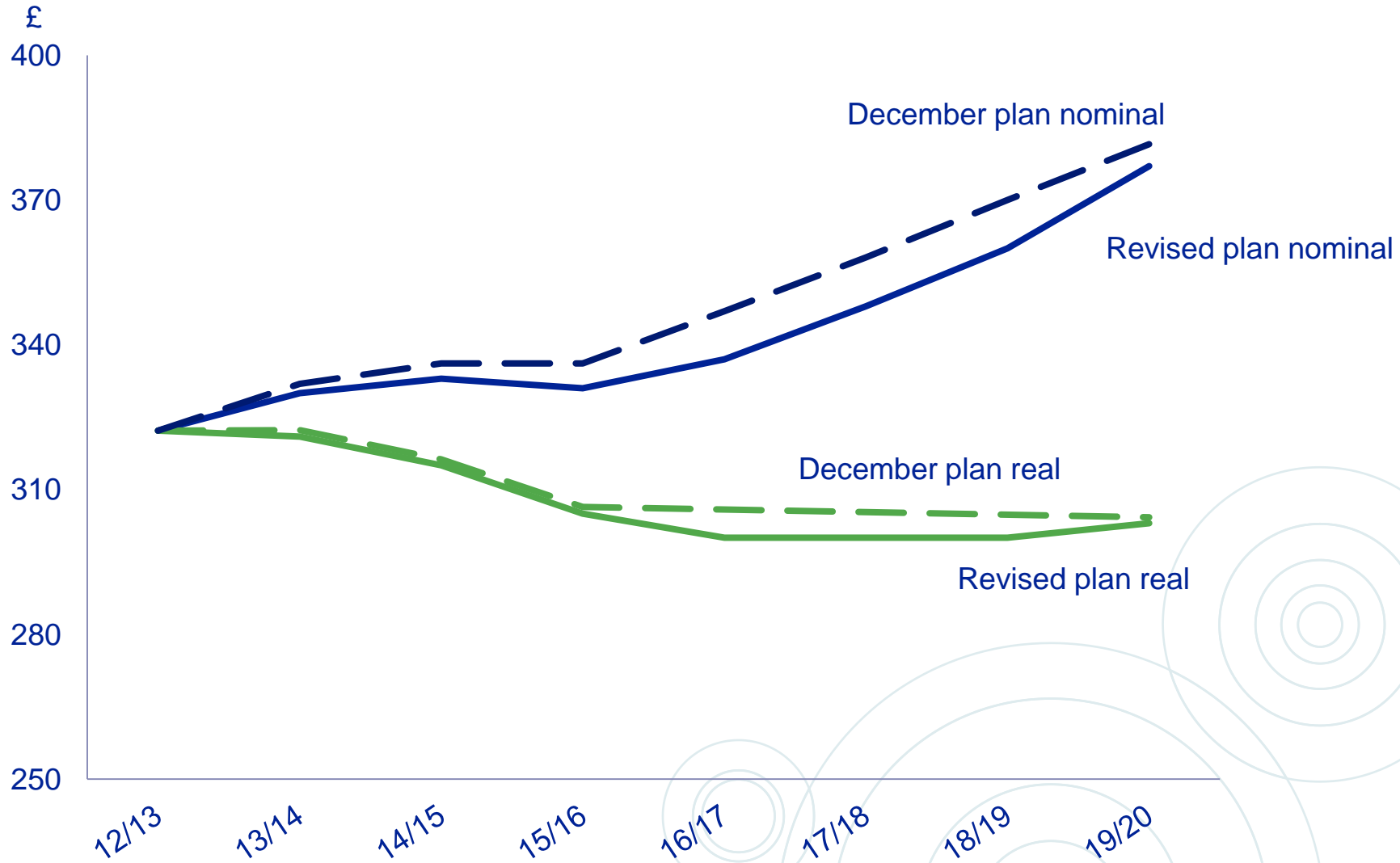
# Overview of our revised plan

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- Bills
- Totex (opex + capex)
- Outcome Delivery Incentives (ODIs)
- Financing and WACC\*

\*Weighted average cost of capital

# Customer Bills



# Totex – 5 year period

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2012/13 prices	AMP5 (£m)	AMP6 (£m)	Change £m	Change %
Capital investment	2,535	3,299	764	30%
Operational expenditure	2,996	2,894	-102	-3%
<b>Total expenditure (totex)</b>	<b>5,530</b>	<b>6,192</b>	<b>662</b>	<b>12%</b>

- Birmingham resilience scheme amendments
- We expect to be within the efficient cost corridor
- PAYG rate c.57% vs. c.55% in December plan

# Outcome Delivery Incentives

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- 27 ODI's
  - 21 with penalties and rewards (7 in December plan)
  - 4 penalty only (4 in December plan)
  - 1 reward only
  - 1 related to Birmingham
- Examples:
  - Speed of responses in repairing leaks (% fixed within 24 hours)
  - Number of pollution incidents
  - Environmental compliance
- Customers supportive of framework
- In line with Ofwat guidance
- Impact on Bills / RCV

# Financing

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- £2.8 billion funding requirement
  - £2.6 billion in December plan
- £1.3 billion of existing debt matures during AMP6
  - 30% of current debt portfolio
- Investment grade credit rating





# WACC comparison

	Severn Trent Plan (Dec '13)	Ofwat guidance (Jan '14)	Severn Trent Revised Plan (Jun '14)
Assumed Gearing	60%	62.5%	62.5%
Cost of debt	2.54%	2.75%	2.75%
Cost of equity	6.7%	5.65%	5.65%
<b>Appointee Vanilla WACC</b>		<b>3.85%</b>	<b>3.85%</b>
Retail		-0.15%	-0.15%
Wholesale WACC	4.2%	3.7%	3.7%
Household retail	0.06%	0.08%	0.08%
Non household retail	0.09%	0.07%	0.07%
<b>Effective Return on RCV</b>	<b>4.35%</b>	<b>3.85%<sup>1</sup></b>	<b>3.85%<sup>1</sup></b>

1. Excludes additional 0.6% for non household retail

# RoRE<sup>1</sup> ranges



Source: Ofwat -

[www.ofwat.gov.uk/pricereview/pr14/pr14publications/prs\\_pre201406pr14investor.pdf](http://www.ofwat.gov.uk/pricereview/pr14/pr14publications/prs_pre201406pr14investor.pdf)

# What The Water Forum said

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“...the company has amended its plan in a way that responds appropriately to a number of challenges from Ofwat but still reflects customers’ priorities and willingness to pay. The Forum has spent a considerable amount of time checking this to ensure that there continues to be a clear line of sight between customers’ expectations and the proposals, and a continuing audit trail.”

# Next steps

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- 29 August
  - Draft determination
  - Representations for 5 weeks until 3 October
- October / November
  - Totex Menu Choices
- 12 December
  - Final Determination
- Post 12 December
  - Decision on dividend



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**Q & A**



# Contact details



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[www.severntrentservices.com](http://www.severntrentservices.com)

## Useful Links

Ofwat

[www.ofwat.gov.uk](http://www.ofwat.gov.uk)

Defra – Department for Environment, Food and

Rural Affairs

[www.defra.gov.uk](http://www.defra.gov.uk)

Environment Agency

[www.environment-agency.gov.uk](http://www.environment-agency.gov.uk)

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# Appendix



# Key Publications



**Changing Course – Delivering a sustainable future for the water industry in England and Wales**  
Publisher: Severn Trent  
[Web Hyperlink](#)



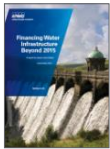
**Changing Course – Through water trading**  
Publisher: Severn Trent  
[Web Hyperlink](#)



**Changing Course – Through sustainable financing**  
Publisher: Severn Trent  
[Web Hyperlink](#)



**Changing Course – Through the sustainable implementation of the Water Framework Directive**  
Publisher: Severn Trent  
[Web Hyperlink](#)



**Financing water infrastructure beyond 2015**  
Publisher: Severn Trent  
[Web Hyperlink](#)



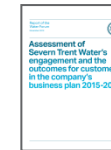
**Investor Pack – June 2014**  
Publisher: Ofwat  
[Web Hyperlink](#)



**PR14 Publications**  
Publisher: Ofwat  
[Web Hyperlink](#)



**Severn Trent Water Business Plan 2015 – 20**  
Publisher: Severn Trent  
[Web Hyperlink](#)



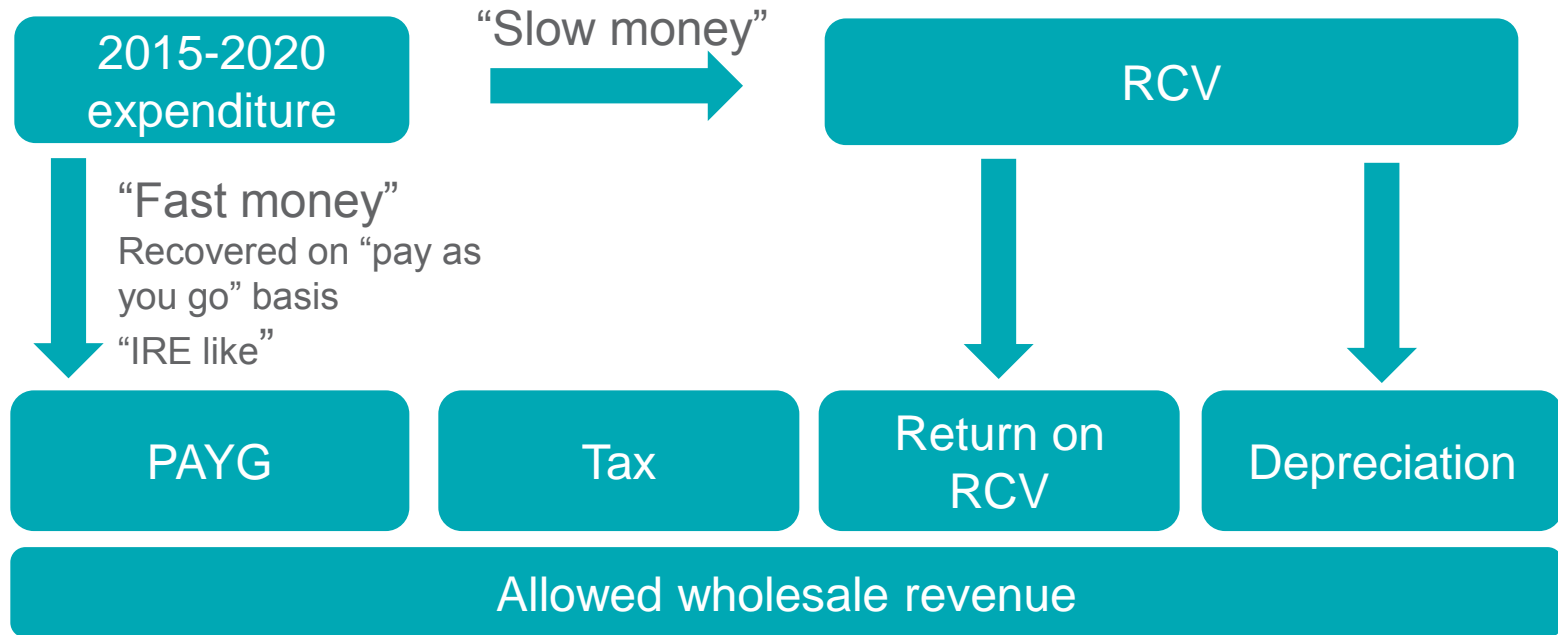
**The Water Forum Report**  
Publisher: The Severn Trent Water Forum  
[Web Hyperlink](#)



**The Water Act 2014**  
Publisher: UK Government  
[Web Hyperlink](#)



# Totex PAYG rate



+ retail allowed costs and margin

- $\text{PAYG} = \text{IRE} + \text{opex}$
- PAYG rate c. 57%

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