

December 2017

Trust in water

Investor survey 2017: a summary of the results

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The role of investors and why perceptions matter

Customers and society depend on the essential public services that water companies provide. The water sector has come a long way since privatisation in 1989 with high levels of customer satisfaction, a significant improvement in environmental quality and major service improvements (including lower leakage, fewer interruptions, less sewer flooding and far fewer problems with low water pressure). Average bills are about the same as they were 20 years ago and are now falling in real terms. All of the service and environmental improvements required significant investment and private investment has played a key role in the improvements in service that have been achieved. Further investment will also be important for ensuring the sector continues to deliver against expectations in the face of significant challenges, especially the need to tackle climate change and invest in infrastructure for the future.

Investors also play an important role in directly challenging management and holding them to account. But they can only do this effectively if they understand our policies and, like ourselves, can trust the information that companies publish (i.e. assurance). We use our investor survey to assess investor understanding of Ofwat's regulatory framework and how it is changing.

Given that our PR19 methodology will be more demanding on companies, the role of investors in challenging and supporting their management teams to do things differently becomes even more crucial. Our methodology consultation document proposed that PR19 would bring: more stretching outcome performance commitments; more powerful outcome delivery incentives; a strengthened efficiency challenge on costs; and a further rebalancing of returns away from financing to operating the business. This would mean that companies who innovate can prosper, while those who don't would find life challenging. And outside of the price review process we have also been focusing on effective corporate governance to facilitate the responsiveness of companies to the balance of returns.

Another way we use this survey is to monitor our perceived regulatory independence in the eyes of investors as this affects the perceived regulatory and political risks in the water sector which directly influence companies' financing costs and, ultimately, customers' bills.

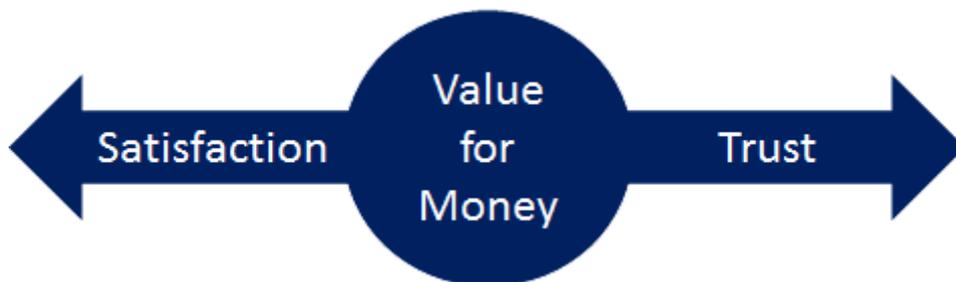
Sector legitimacy: what shapes it and how do investors and management play a part?

To be truly effective, a regulatory system needs to be seen to be legitimate. The current public debate on the achievements of the current regulatory regime is wide ranging but includes a challenge to the investor community and the way companies are managed. What is clear is that earning customers' trust will require greater openness and transparency. Given the close link between legitimacy and investability, we expect investors to play a lead role in challenging companies to deliver a high level of transparency and engagement with their customers to earn and maintain their customers' trust and confidence.

Customer satisfaction with the service provided by companies, whether customers feel they are getting value for money and the trust customers have in their companies, all play a key role in the regime's legitimacy. Customer satisfactionⁱ is very high (91%) and has remained fairly stable over the last five years.ⁱⁱ Whether customers feel they are getting value for money has remained fairly stable over the same period, but at 75% is lower than for customer satisfaction.ⁱⁱⁱ The trust customers have in their companies is lower than the other two metrics at 60%, with 5% of customers saying they did not trust their company.^{iv}

The role of trust within legitimacy is important and can manifest itself independently of the quality or price of any service provided. These figures suggest that companies still have some way to go before they can feel comfortable that they have convinced the public of their legitimacy. Investors will play an important role in this process.

Diagram 1: If trust is low(er), it can pull perceptions on value for money away from satisfaction with services provided.



Our 2017 survey

2017 Ofwat Investor Survey

Thank you for taking part in our 2017 investors survey. Completing the survey shouldn't take you more than 10 minutes.

* 1. Please state how much you agree with the following statements.

	Strongly agree	Agree	Neither agree nor disagree	Disagree	Strongly disagree
Ofwat's regulatory framework aligns the interests of regulated companies and their investors with those of customers over the long term.	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Ofwat regulates in a proportionate, consistent, transparent and targeted way, choosing the most appropriate tools from within a wide range of regulatory responses.	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Ofwat is independent of government(s).	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Ofwat's policies are well-considered and consistent.	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Ofwat is listening to investors.	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Ofwat engages with the investor and credit-rating communities in an open and transparent way.	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Ofwat engages consistently and sufficiently with all types of investment stakeholder (debt, equity and analysts).	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>

The picture shows the investor survey that was sent out in mid-October 2017. The survey included a mix of set and free-text questions.

This report summarises the survey results and suggests a number of follow-up actions we see as being in the best interest of customers.

2. In terms of our engagement, what is the best thing we have done over the last year?

3. Which one thing could we do to improve our relationships with the investor community?

4. Are there any other comments you would like to make about our relationships with you?

5. To help us understand the range of views in this survey, please choose from the following list.

- Advisor
- Consultant
- Credit analyst
- Equity analyst
- Fixed income
- Listed equity
- Private equity
- Rating agency
- Other (please specify)

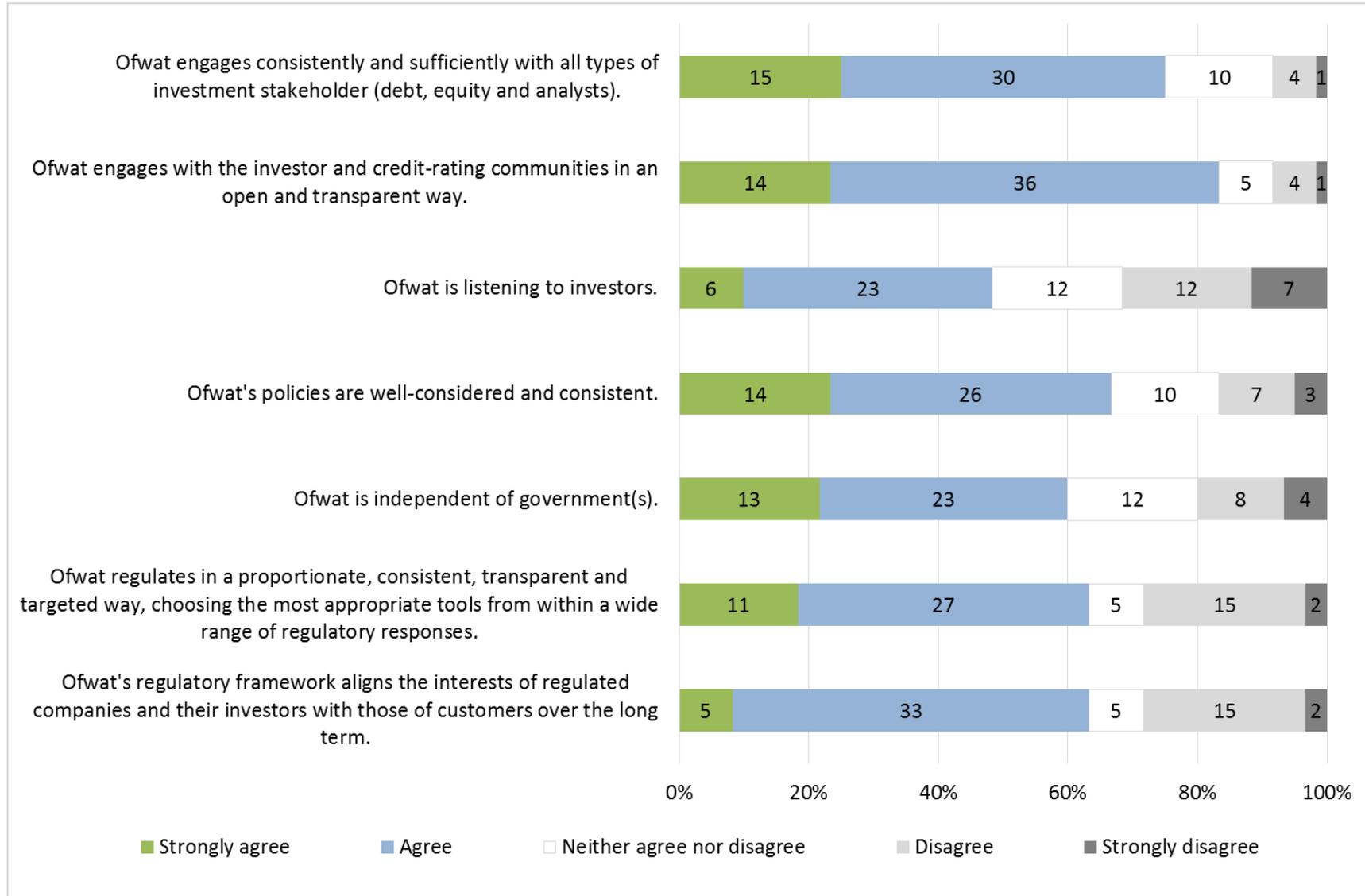
6. Email address (optional)

Survey sample

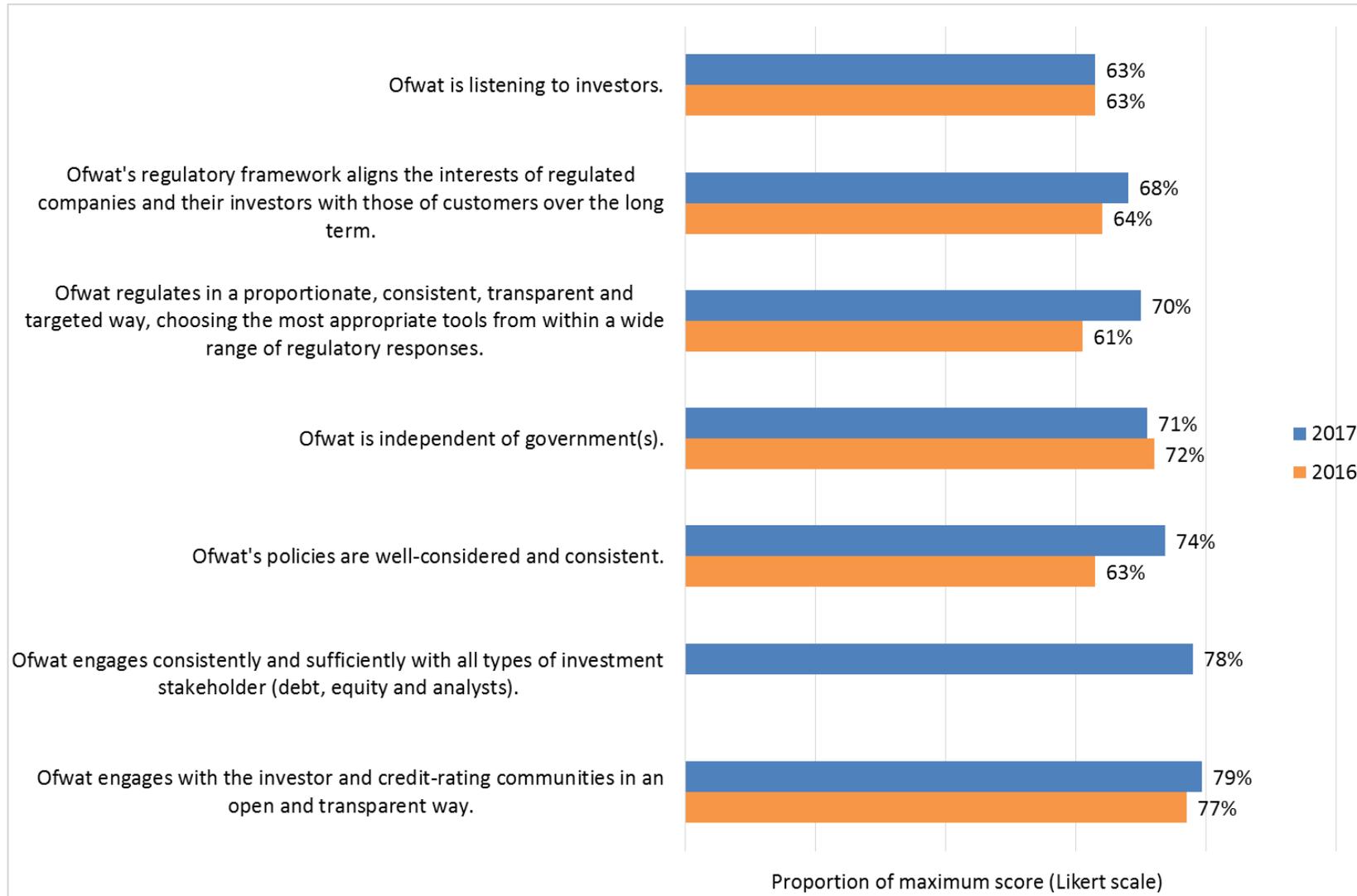
The survey was sent out to a sample of 528 people and we received 60 responses (i.e. an 11% response rate). This was up from 20 responses to our first investor survey last year (the 2016 survey was only sent to around 140 people). There were 60 responses for section one, 42 responses to section two (70% of total respondents), 38 responses to section three (63%) and 21 responses to section four (35%). We explain the categories we used to group respondents at the end of this report.

A breakdown of this year's survey sample and the respondents is shown below.



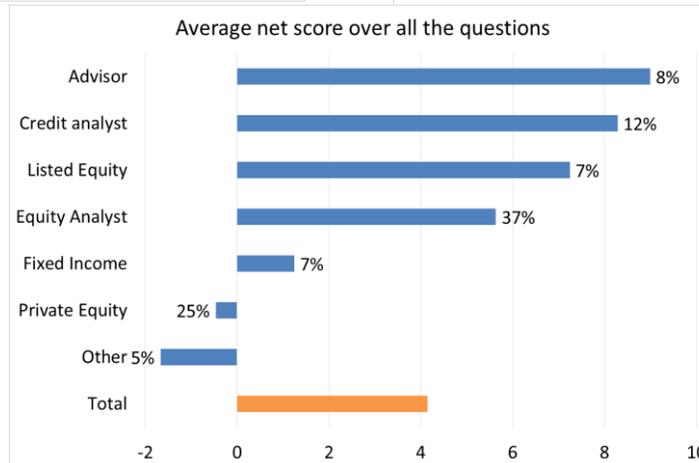
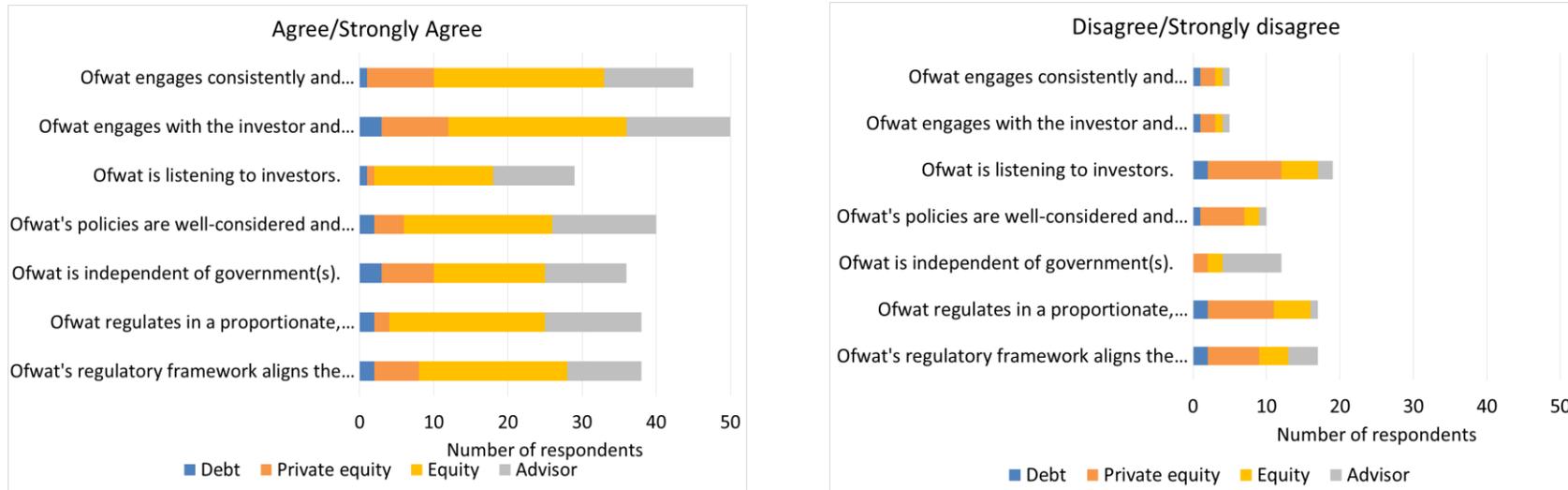


The bars in the chart represent the proportion for each answer and the data labels show the number of responses.



In this chart the proportion of maximum score allocates five points for strongly agree down to one point for strongly disagree. This means the lowest achievable score is 20%, while the score would be 60% if each of the five options (from strongly agree to strongly disagree) received the same proportion of votes.

The two charts below show the composition of agree and disagree votes by investor type. Equity makes up a high proportion of strongly agree and agree votes while strongly disagree and disagree votes are more evenly weighted between debt and equity. Respondents categorising themselves as private equity or other, who as a group accounted for 30% of respondents (18 out of 60 in total) were the most negative across all of our seven questions (as shown in the average net score chart below).



The net score is calculated by rating the response “strongly disagree” minus 2 to “strongly agree” positive 2 with “neither agree nor disagree” equal to 0. The percentage values next to the bars are the number of respondents for each category as a proportion of the total number of respondents.

What investors said we did well on in terms of our engagement with them over the last year

Investors meetings

- More frequent meetings
- Smaller group meetings instead of conferences
- City Briefings
- Quality and structure of the meetings

Early timing of PR19

- Early engagement with stakeholders
- Early publication of the PR19 methodology consultation
- Level of detail of the PR19 methodology consultation
- Collaborative and transparent consultation

Governance

- Continued focus on governance
- Monitoring financial resilience report

What investors suggested we could improve on in terms of our engagement with them over the next year

Listening to investors

- Ofwat encourages investors to give feedback. However, it is unclear how this feedback is taken into consideration.
- Engage consistently with all types of investors.

Investor meetings

- More regular and substantive interaction
- More one-to-one meetings
- More frequent City Briefings

Legitimacy

- Take advantage of PR19 to deliver value for money to contribute to sector legitimacy
- Continue to monitor perceptions of Ofwat's regulatory independence
- Distinguish the performance of efficient players from a few bad actors

Our responses to your feedback

Listening to investors (and other stakeholders)

The December methodology document will have an appendix in which we will reply to responses to our consultation making it clear where we have changed our methodology and, where we have not, we will explain clearly why this is the case.

Investor meetings

We have added a form on the Investors page of our website so investors can easily request a one-on-one. We have set aside another day per quarter for one-to-one and small group meetings. We will look to add to our roundtable schedules to cover equity analysts and fixed income/rating agencies. Investors are just one of our key stakeholder groups and we aim to ensure that the balance of our interactions with investors is appropriate by reference to our engagement with other stakeholders, customer representatives in particular.

Legitimacy

Investors should not confuse our emphasis on a long-term approach with no requirement for change. We do not believe that a continuation of the status quo is going to improve the sector's legitimacy. We would urge investors not to underestimate the strength of the current legitimacy challenge. The sector cannot expect the regulator to meet this challenge on its behalf. Companies and investors are fundamentally accountable.

Categories used to group respondents to our investor survey

To help us understand the range of views expressed in our survey, we asked respondents to choose from a set list of categories to describe themselves. An explanation of these categories is provided below.

Advisor: This category includes investment banking, consultancy and lending organisations.

Equity analyst: Equity analysts can work on the buy-side (investor) or the sell-side (provider of research and execution services). Buy-side analysts work for fund managers. On the sell side, equity analysts work for investment banks and independent stockbrokers and publish research reports on companies listed on the stock exchange for their buy-side clients.

Listed equity: This category covers investors who own shares in companies which are listed on the public stock exchange. There are three water companies in England which are listed on the stock exchange: Pennon (which owns South West Water), Severn Trent and United Utilities.

Private equity: Private equity is composed of funds and investors that directly invest in private companies, or that engage in buyouts of public companies, resulting in the de-listing of public equity.

Credit analyst: A credit analyst can also work on the buy-side (investor), the sell-side (provider of research and execution services) or at a credit rating agency. Credit analysts evaluate the financial position of companies including assessing the likelihood of financial distress.

Fixed income: This category represents investors in fixed-income securities such as bonds.

Other: All remaining respondents who do not fit in any of the categories above. This can include a listed company that owns a stake in a private water company.

ⁱ Customers were asked, “taking all those aspects of your water supply services into account, overall how satisfied or dissatisfied are you with your water supply? They were asked a similar question on their sewerage service.

ⁱⁱ [Water Matters, Household customers’ views on their water and sewerage services 2016, Consumer Council for Water, June 2017.](#)

ⁱⁱⁱ [Water Matters, Household customers’ views on their water and sewerage services 2016, Consumer Council for Water, June 2017.](#)

^{iv} [Water Matters, Household customers’ views on their water and sewerage services 2016, Consumer Council for Water, June 2017.](#) In the Consumer Council for Water’s “Water Matters” 2017 report, the trust data is represented as a mean score out of 10, where 1 is “do not trust at all” and 10 is “completely trust”. To present this in the same percentage form to be consistent with the satisfaction and value for money results, the Consumer Council for Water derived the 60% figure based on the total net responses of 8, 9 and 10 for customers who trust their companies and the 5% figure based on total net responses of 1, 2, 3 and 4 for customers who do not trust their companies.