
Speech from Rachel Fletcher - A greener water sector: How can our water companies leave a positive legacy for future generations?

Institute of Water Environment Conference, 7 November 2018

Thank you very much for the opportunity to come and speak today on such a vitally important topic and one which is so very close to our hearts at Ofwat.

Ofwat is frequently called the “economic regulator” - clearly to distinguish us from other regulators in this sector and perhaps particularly the Environment Agency. So you might be wondering why I am speaking on this platform and you may also be assuming that Ofwat is concerned solely with price and service. I am very keen to dispel that particular myth here today and to show you just how much the environment flows through everything we do.

Setting the scene – water and the environment

I'm sure I don't need to convince any of you of the challenges that climate change poses for our planet. Changing weather patterns, melting ice-caps, rising sea levels, greater GHG emissions – we're all aware of the stark projections. But let's for a moment just look at the picture for water.

In the years ahead, our scarce water resources are set to come under greater pressure than at any point in recent memory. Wetter winters and drier summers are likely to become more common. Our population is projected to grow by upwards of 10 million people over the next 20 to 30 years.

Much of the housebuilding is projected to happen in already water scarce areas such as the Oxford Cambridge corridor, with 3 new towns expected to emerge in this area alone. The risk is that we abstract even more from our already stressed and environmentally sensitive rivers. And that sewer flooding and surface run off creates more pollution in the rivers and seas.

I joined Ofwat at the beginning of this year. I am brand new to the water sector having spent the last 25 years in energy – so I have a lot to learn. One of the most

fascinating aspects of my new role has involved visiting the rivers that the sector depends on for water and as a repository for treated effluent.

This has opened my eyes. I now know abstraction is slowing down the flow from some of our beautiful and ecologically special chalk streams, causing them to silt up and in some cases dry up altogether. I know that there is evidence of pollution damaging the fragile ecological balance and killing off plant and fish life in some rivers. And I know there is a risk that climate change, population growth and ageing infrastructure threatens to make this situation worse.

It is vital we avoid this risk, turn the situation around and get focused on improving the environment. I'd go as far as to say that the strain on the environment is creating a burning platform for the water sector which deserves all of our urgent attention.

It is perfectly appropriate that I use my position as the CEO of Ofwat to make this statement. Our role in its broadest sense is to protect consumer interests. And consumers need sustainable water resources to provide them with reliable drinking water supply for the long term. But it goes beyond this.

The more polluted our water supplies, the more expensive it will be to treat them to drinking quality levels. The lower the flow in water, the harder it will be to dispose of treated waste water safely back to the environment.

But also – each water consumer is a citizen – perhaps a parent that enjoys taking their kids to the local stream to catch tadpoles. Or a walker who treasures the time out a stroll by a river can provide. Customer interests span beyond the service they get or the price they pay for water. They care about the so called amenity value water can bring and about preserving and enhancing this for future generations.

So in Ofwat we are passionate about doing our part to make sure that water companies are responsible stewards of the environment. This is not an add-on, but is integral to our duties to protect customers' interests in their widest sense.

Before I move on to talk about what needs to be done to ensure water companies leave a positive environmental legacy, let me say a little bit more about out how I see the challenge for the water sector.

We (by which I mean the companies and the regulators) face what I think of as the water sector "trilemma". This is the challenge to provide resilient, safe and reliable water supplies for future generations, in a way that keeps water affordable and which leaves our environment in a better condition than we found it.

This is a daunting task, but I don't think we can say that the water sector has left a positive legacy if it doesn't achieve all 3 limbs of this challenge.

The good news – which I will talk about now – is that there is a range of things we can do to protect the environment while keeping bills affordable and improving the resilience of our long term water supplies. The other good news is that we have already started using these “win, win, win” approaches. But we need to do more and do it faster.

Let's now turn to talk about the four things that can allow us to address the trilemma:

- Regulations
- Innovation
- Relationships with customers
- Long term view

Standards, incentives and penalties

The first plank is to ensure that water companies are held to account through standards, penalties and rewards for improving the environment. And this is an area where Ofwat, as well as the EA, has an important role to play.

Over recent years we've given serious thought to how we can use our tools – and our leadership position - to drive environmental improvements. The regulatory settlement currently includes incentives relating to leakage, pollution incidents, and treatment work compliance and makes customers' money available to clean up bathing water and rivers and meet European environmental standards (in an efficient way, of course).

With PR19, the suite of environmental incentives and performance commitments will be even greater, and include commitments on per capita consumption for example and tighter standards overall.

Much publicity has been given to our challenge to companies to reduce leakage by 15% over the period to 2025 – which could save around 170 billion litres of water a year – meeting the yearly needs of around 3.1 million people.

I'm pleased to say all companies have agreed to this challenge, with the industry now also jointly committed to at least halving leakage by 2050.

But what might be less well known is that the PR19 business plans contain over 350 catchment management schemes – a 66% increase from current levels. And the

expectation that 8000km of rivers will be improved over the 5 year period. And a commitment to reduce serious pollutions by 90%.

We've also seen commitments to reduce per capita consumption, with some companies setting targets of as low as 119 and 120 litres per person per day compared to the current average of 141 litres per day.

There is a price tag here – companies propose to spend more than £5bn to make the improvements needed to meet European standards alone. But we have the tools in Ofwat to challenge the companies on efficiency – including efficient financing costs. Even before we have carried out our own benchmarking, we expect on average the cost of water to fall in real terms over the PR19 period. A great example of more for less for customers and the environment.

So our direct regulation of the industry is important. But it will not be enough if all the water companies do is respond to regulations. As I know you've discussed as an institute already – the companies need to go beyond regulation and own the environment challenges.

Innovation is key to a greener water sector – and is a key part of the “win win win” strategy we need to address the environmental challenges in an affordable way.

Business as usual simply won't cut it anymore; water companies must embrace the opportunities presented by new technology, new ways of operating, big data and AI and innovative commercial arrangements. At present, these are still largely untapped.

We all recognise for example, that there is no way the leakage ambition will be achieved without a change in approach to maintaining and managing the networks. There are huge opportunities to use remote monitoring and diagnostics to “manage out” the pressures on the system that cause leaks or sewer flooding. But these types of approaches are still the exception rather than the rule.

More progress is being made, as I mentioned, in using innovative catchment management – or nature based approaches. I've found it fascinating to see water companies work with farmers to reduce methaldehyde and nitrate run off into the water source. Reed beds are being used to reduce the risk of effluent damage in sensitive rivers. Sustainable drainage systems are being used to reduce the environmental damage associated with heavy rainfall. These provide wins for the environment, are often lower cost and provide enhanced amenities for local

communities. We need to continue to see this “system wide” thinking applied as a matter of course.

Ofwat can and does play an important role in encouraging innovation. We’ve introduced a totex approach and a set of outcome incentives which allow plenty of room for innovation. We offer rewards to companies that bring genuine innovation into their business plans. And we want to think further about our tools in this regard as we move beyond PR19.

We have also introduced a range of markets that should bring forward environmentally friendly innovation. Take the example of bioresources - what once may have been regarded as waste. This can be transformed by anaerobic digestion into useful products like biogas and fertiliser.

In April 2017, we opened up the business retail market in England enabling business customers to “shop around” for new deals, including support in using water more efficiently. We’ve already seen some retailers help business customers better manage their water usage, as well as reduced water bills.

This new market, combined with the NAV market, has the potential to drive new approaches such as the use of “grey water” or recycled water for commercial purposes.

So Ofwat can encourage innovation. But effective markets require the regional water companies to come to the party – to work with new players and participate in trading. It requires them to see these markets as an opportunity to make a positive difference for customers and the environment, not an irritation or a commercial threat.

Relationships with customers are the 3rd of the 4 planks to protect the environment

We often forget that customers sit at the centre of the water system and are an active part of it.

We know, for example that Britain has one of the highest per capita consumptions in Europe - we use 141 litres per day compared to 121 litres in Germany.

Unlike other countries in the world we make very little use of water recycling for tasks like watering gardens and washing cars. There is significant potential to be tapped here and the technology is available to do so. Again, there is a win win opportunity to

cut bills by reducing use of treated water and in turn to reduce the pressure abstraction puts on our environment.

How we use water is part of the answer to the environmental challenge. And while there is a role for personal responsibility, and for policy improvements – for example on building standards and white goods labelling - water companies have an important role to play.

If this summer taught us anything, it was that it is hard to get people to use water wisely if they are not confident that water companies are doing their bit, in this case on leakage.

Equally, if people do not believe that their water company has their interests at heart – for example if they think all they care about is profit – then it will be so much harder to engage customers as willing partners in the quest to protect the environment. So building that relationship and building further trust is important – not just for the reputation of the sector, but if we are to engage customers in being part of the solution to our environmental challenges.

I do think there are positive signs here – in developing their business plans, companies engaged with over 1.5 million customers, representing a step change in contact and a platform which companies can use to build an ongoing relationship. But there is still a way to go.

Finally, to leave a legacy for the environment, water companies and the regulators need to be better at planning for the long term

The National Infrastructure Commission's report – Preparing for a Drier Future – flagged the economic cost to the country if we have sustained periods of drought. It estimated this at £40bn a year by 2030 unless we make further investment in water resources and reduce demand. This finding caught the headlines. But just as important was the NIC's recommendation that the whole approach to water resource planning needs to change.

At present planning to meet customers' water demands is done by each company separately, with only 4% of water needs met by inter-company trades. By working together the industry has a huge opportunity to develop lower cost options for meeting our long term water resource needs.

Importantly, this also affords an opportunity to take a long hard look at the level of abstraction which different water sources can sustain and to use this joined up long term planning exercise to reduce the stress we put on the environment in serving our water needs.

I'm pleased to say that groupings of water companies have begun to consider regional plans. Ofwat, EA, Defra and the companies are collaborating on a new framework to give these regional plans coherence and rigor. Overall this should enable the industry another win, win, win opportunity to meet our long term need for water in a way that is both affordable and allows us to leave a positive environmental legacy.

Conclusion

So to sum up – leaving the environment in a better shape than we find it is not an optional extra for the water sector. This challenge has to be addressed alongside and as part of the “trilemma” that also involves securing our future water needs and keeping water affordable.

Having been up and down the country visiting water companies, I see many in the sector are galvanised by these challenges. It is also positive that there are “win win win” strategies to deploy, such as those I've talked about today. And we are beginning to make progress in using them.

But my note of caution is that we should not underestimate the extent of change that is likely to be needed in the companies – and in how we regulate. I've talked about the need for new skills, cultures, technologies and partnerships.

In Ofwat we are working now to shape a vision for the sector. I want this to be a vision that is jointly owned by all stakeholders and which resonates with customers. This is why we are reaching out through social media to find out peoples' Water Stories and I hope that those in this room might participate in this.

In parallel with PR19 we are building a new regulatory strategy. We don't assume the approaches we are using now will be enough to drive the significant change needed to address the water trilemma. And we want to play the fullest role possible.

But my closing remark to the industry is don't wait for Ofwat or others to come up with the answers. Work with us, but most of all grab these challenges with both hands and own them. That way you can leave a positive environmental legacy for the future.