

July 2019

Trust in water

PR19 draft determinations

**Anglian Water – Securing long-term resilience
actions and interventions**

0 f w a t

www.ofwat.gov.uk

PR19 Draft Determinations: Anglian Water – Securing long-term resilience actions and interventions

Following our initial assessment of plans, we categorised two types of actions for slow-track and significant scrutiny companies:

- required actions for companies which in general were required for draft determinations (or final determinations for some aspects of past delivery); and
- advised actions for companies to do by a specific date but that are not required for our draft determinations.

Table 1 below sets out the required and advised actions, a summary of the company's response to the action, our assessment of the company's response, and any further interventions we are making as part of the draft determination.

Each action has a unique reference. The prefix 'ANH' denotes the company Anglian Water. The central acronym references the test area where the action has been identified, please see the 'PR19 draft determinations: Glossary' for a key to these acronyms. Actions whose numbers are preceded with an 'A' denote required actions and actions whose numbers are preceded with a 'B' denote advised actions.

Table 2 below sets out any further interventions that are not resulting from an action which we are making as part of the draft determination.

Each further intervention that is not resulting from an action has a unique reference. The prefix 'ANH' denotes the company Anglian Water. The central acronym references the test area where the action has been identified, please see the 'PR19 draft determinations: Glossary' for a key to these acronyms. Intervention numbers are preceded with a 'C'.

For all other documents related to the Anglian Water draft determination, please see the [draft determinations webpage](#).

Table 1 – Anglian Water's response to required actions and interventions for draft determinations

Test area	Action reference	Action type	Action	Date required	Summary of company response to action	Our assessment and rationale	Required interventions
Securing long-term resilience	ANH.LR.A1	Required	The company should ensure that its common and bespoke performance commitments associated with operational resilience are clearly defined, sufficiently demanding for the 2020 to 2025 period and the long term, and supported by the right incentives. We expect the company to satisfy the relevant actions set out in relation in the outcomes areas ensuring a line of sight between risks to resilience and package of outcomes.	1 April 2019	Anglian Water has not implemented all relevant outcome actions associated with operational resilience, in particular those related to asset health and to its bespoke resilience performance commitments.	Intervention required. The company should address any outstanding actions associated with operational resilience from the 'Anglian Water - Delivering outcomes for customers actions and interventions' tables, in particular those related to total mains repairs, sewer collapses, unplanned outage, treatment works compliance and to its bespoke resilience performance commitment	Refer to interventions described in the 'Anglian Water - Delivering outcomes for customers actions and interventions' tables regarding total mains repairs, sewer collapses, unplanned outage, treatment works compliance and its bespoke resilience performance commitment

Test area	Action reference	Action type	Action	Date required	Summary of company response to action	Our assessment and rationale	Required interventions
						('Percentage population with single supply').	('Percentage population with single supply').
	ANH.LR.A2	Required	The company should provide a commitment that it will, by 22 August 2019, prepare and provide to us an action plan to develop and implement a systems based approach to resilience in the round and ensure that the company can demonstrate in the future an integrated resilience framework that underpins the company's operations and future plans showing a line of sight between risks to resilience, planned mitigations, package of outcomes and corporate governance framework.	1 April 2019	Anglian Water has confirmed its commitment to complete the action by 22 August 2019.	No intervention required. The company has complied with the required action.	N/A
	ANH.LR.A3	Required	The company should also provide a commitment to work with the sector to develop robust forward looking asset health metrics and provide greater transparency of how its asset health indicators influence its operational decision making.	1 April 2019	Anglian Water has confirmed this commitment.	No intervention required. The company has complied with the required action.	N/A
	ANH.LR.A4	Required	The company's assessment of financial stress scenarios extends only to 2025. The company should commit to demonstrating that its assessment of financial resilience extends beyond 2025 in its next Long-Term Viability Statement.	1 April 2019	Anglian Water has committed to demonstrate financial resilience beyond 2025 in its long term viability statements.	No intervention required. Anglian Water has responded satisfactorily to the requirement.	N/A
	ANH.LR.A5	Required	Please explain how the company has taken account of the risks associated with: <ul style="list-style-type: none"> • long term financial resilience associated with possible downgrade to its credit rating given the negative outlook; • requirements to refinance subordinated debt; • any application of the gearing outperformance mechanism for PR19; and • outline associated risk management/mitigation approaches identified by the company to provide assurance on long term financial resilience. 	1 April 2019	<p>Anglian Water says that it is addressing the risk of a credit rating downgrade through dialogue with rating agencies, reduced dividend levels to achieve de-gearing, and a simplified capital structure. It considers the main risk associated with a downgrade to be increased debt costs, but has stress tested a 2% increase in new debt costs and considers it would retain an investment grade rating.</p> <p>Anglian Water says it has a relatively small amount of class B debt to refinance in 2020 to 2025 and has reduced the proportion of subordinated debt for financing its investment plan. It also says it has sufficient liquidity facilities (of just under £1bn) to cover the risk of restricted credit markets.</p> <p>Anglian Water says that it plans to reduce its gearing from a relatively</p>	Intervention required. The company has provided a Board assurance statement that its business plan achieves the credit metrics for a Baa1 credit rating under the actual capital structure based on our early view cost of capital. However the company expects to be highly geared (around 78% through 2020-25).	The company is responsible for maintaining its long term financial resilience. The company should provide further detail and Board assurance about its plans to maintain its long term financial resilience taking account also of action ANH.LR.C1. In its future reporting, we expect Anglian Water to apply suitably robust stress tests in its long term viability

Test area	Action reference	Action type	Action	Date required	Summary of company response to action	Our assessment and rationale	Required interventions
					<p>high present level of around 78% to a 'mid 70s' percentage during 2020 to 2025. It estimates that the cost to it of the PR19 gearing outperformance mechanism will be £40m. However, it notes that the adjustment would be applied as part of the PR24 price review and does not consider the mechanism will have an impact on its credit rating.</p> <p>Anglian Water has outlined the following risk management approaches with respect to its long term financial resilience:</p> <ul style="list-style-type: none"> • Further dividend reductions • Equity injections • Reviewing financing arrangements and costs • Reducing the cost base of the business 		statements in 2020-25.
	ANH.LR.B1	Advised	No advised actions	N/A	N/A	N/A	N/A

Table 2 – Further interventions for draft determinations

Intervention reference	Our assessment and rationale	Interventions
ANH.LR.C1	The Board assurance on actual and notional financeability and financial resilience in the revised business plan was provided on the basis of the assumptions made in the business plan, prior to any interventions we have made in the draft determination and our updated view of the cost of capital. There is evidence of further downward pressure on the cost of capital in very recent market data which will be considered for our final determination.	We expect companies to provide further Board assurance, in their responses to the draft determination, that they will remain financeable on a notional and actual basis, and that they can maintain the financial resilience of their actual structure, taking account of the reasonably foreseeable range of plausible outcomes of their final determination, including evidence of further downward pressure on the cost of capital in very recent market data as we discuss in the 'Cost of capital technical appendix'.

Ofwat (The Water Services Regulation Authority) is a non-ministerial government department. We regulate the water sector in England and Wales. Our vision is to be a trusted and respected regulator, working at the leading edge, challenging ourselves and others to build trust and confidence in water.

Ofwat
Centre City Tower
7 Hill Street
Birmingham B5 4UA

Phone: 0121 644 7500
Fax: 0121 644 7533
Website: www.ofwat.gov.uk
Email: mailbox@ofwat.gov.uk

July 2019

© Crown copyright 2019

This publication is licensed under the terms of the Open Government Licence v3.0 except where otherwise stated. To view this licence, visit nationalarchives.gov.uk/doc/open-government-licence/version/3.

Where we have identified any third party copyright information, you will need to obtain permission from the copyright holders concerned.

This document is also available from our website at www.ofwat.gov.uk.

Any enquiries regarding this publication should be sent to us at mailbox@ofwat.gov.uk.

