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Dear Sir or Madam,

Financial resilience in the water sector: a discussion paper

Thank you for the opportunity to contribute to the discussion on financial resilience in the water sector.

We agree that it is essential that water companies can demonstrate financial resilience and maintain a sufficient strong investment grade credit rating to efficiently finance their activities. We believe companies should demonstrate sufficient financial headroom to meet their current and future commitments and we agree that companies should take action to maintain and improve their credit ratings.

Financial resilience needs to be considered holistically and we support the proposal not to define limits on capital or financing structures. The sector is going to face increasing investment requirements in the future. We believe a one size fits all approach would constrain companies' abilities to seek efficient funding (particularly considering the current low cost of debt). We also believe that consideration of specific company circumstances needs to be taken into account and the framework needs to allow for flexibility to adapt to uncertain futures.

We support the proposed requirement for companies to develop resilience plans when a rating falls below a certain level (backed up with additional board assurance). We believe this reflects good practice and companies should be doing this anyway and we support increased transparency on companies' activities to manage financial resilience.

However, we do not support the proposal to raise the threshold on lock up provisions and argue this is unnecessary. We believe this could have a greater impact on smaller companies' abilities to attract investment. This is a key consideration for Portsmouth Water through the period of high growth while we construct the Havant Thicket reservoir. We highlight that companies can continue to operate and raise finance while maintaining an investment grade rating.

We challenge whether it is proportionate and efficient for a smaller company to hold two credit ratings (others in the sector have one or none). While we see the benefit for larger companies it does not necessarily provide the same value to smaller companies and their customers. Following a decision made around 2 years ago based on performance and cost of one of our 2 ratings agencies, we currently hold one credit rating. If there are concerns that there is a risk of companies 'shopping for ratings' we believe an alternative approach could be a requirement for companies to notify Ofwat of the intention to switch rating agencies. We support the principle that companies should formally notify Ofwat of changes in ratings.

We would challenge whether the license needs changing to align with the dividend guidance at this stage given the guidance provided in the final determination. We fully support the approach Ofwat have taken through the recent feedback on dividends and believe it is appropriate to allow companies to respond if there is a significant issue to address in this area.

We would advise against regulating dividend policies or creating compliance issues by formally linking dividends to service. Investors across the sector value dividend stability and this supports acceptance of a lower equity return. Introducing explicit links to in year service could create a challenge to investor confidence where dividend volatility is driven by performance impacted by one off events e.g., by a severe winter.

We are supportive of greater transparency around swaps and pensions liabilities. We recognise the current concerns around the use of swaps but we would flag that swap have an important role to play in financial risk management. We also believe they can present an efficient solution to the complex challenges facing companies with legacy debt. It is important that companies work closely with Ofwat and rating agencies to identify how to provide comfort through better disclosures to avoid creating barriers to access to important markets.

We are also supportive in principle of a level of transparency around holding company liabilities and we have disclosed group funds raised at holding company level to support our investment in Havant Thicket in our recent APR. However, we believe that any disclosures should only relate to ring fenced company activities associated with Ofwat's powers of appointment.

We strongly support that companies should provide a Board assessed statement on financial resilience but would emphasise that this can only be fully informed if there is sufficient guidance from Ofwat on key issues such as risk and reward. We would also stress that considerations around financial resilience cannot be disconnected from risk and reward and that consideration of company specific circumstances needs to be considered when assessing financability, not just the notional company.

Your sincerely,

[redacted]

Chief Financial Officer