



Speech

Given by John Russell, Senior Director Strategy, Finance and Infrastructure
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Balancing investment leading up to AMP8, and beyond

Good morning all,

It's a real pleasure to be invited to open today's conference by talking about how more collaboration, more progress, and more efficient investment will build a better sector.

Don't get me wrong, this is not a small or easy topic – and considering what there is to be achieved – it was never going to be. But that doesn't mean it is impossible and that the sector doesn't have the talent and capabilities to deliver what is needed.

At the moment, there is a strong public focus on the actions and progress of the water sector and particularly its role in protecting and enhancing the environment through its management and investment in wastewater networks. Our watercourses have been described as "chemical cocktails" with only 16% of rivers in England and 44% of rivers in Wales meeting good ecological status a troubling picture for everyone concerned. The post-privatisation gains in reductions in phosphates and ammonia seem a long time ago. We've also seen increased concerns about those with sewage in their homes.

There is no more hiding from the fact that improvements need to happen now. Households are already being put under pressure by cost-of-living increases and the impacts of climate change are bringing new challenges to our environment and resilience of networks. Our sector has a duty to cope effectively with these challenges and provide resilient water and wastewater services that support to the day-to-day functions of our society.

Today, and this will come as no shock, I will say that substantial investment will be needed now and all the way through the next few AMPs. There is no way around this as what the sector are looking to achieve, and at the pace we need, will need 2 to 3 times more investment. And whilst opportunities for investment and funding are available, I think the bigger question is around how all investment moving forward can be efficiently allocated and delivered for the better.

Can companies step up to the challenge?

Just before the winter break, we published our annual water company performance reports and although there were improvements across the industry in areas such as leakage and

unplanned outages, there are still many companies failing to meet the basic levels of service that are expected.

Additionally, for the 2021-22 period, the number of serious pollution incidents increased, which led to companies having to return almost £17 million to customers. Customer satisfaction has dropped, and most companies have missed targets to reduce the levels of household water consumption.

And what is more disappointing is that we're already seeing evidence of underspend. Our report found that between the first two years of AMP7, certain companies are falling behind on their investment plans.

Now, I'm not ignoring that we have had a difficult few year – not just as a sector, but as a country. Covid, economic woes and a very dry summer have all been real challenges, but we must question why we are seeing a rise in performance failures and unspent budgets when customers are paying to see improvements and stable progression. Now is not the time to fall two steps behind when we need to be several steps forward.

Last year, the Government announced that it will now require companies to deliver their largest ever environmental infrastructure investment. We can expect £56 billion of capital investment over the next 25 years to tackle storm overflow discharges by 2050.

This is because, now more than ever, customers need to be convinced that companies are on the right side of the challenges that are to come. That they're taking substantive action, horizon scanning to prepare for unplanned challenges, but also working to improve the service they currently provide which, in many cases, is lacking.

Opportunities for AMP 8

So, as we continue towards the PR24 price review, the sector must ask itself what opportunities it can look to right now, that will better prepare us for the next AMP and beyond.

For this, I will highlight three areas that we believe companies should be looking toward:

Firstly, there is more to be done on how companies can increase their focus on the long term. Stronger adaptive planning is needed to deliver the right investment to meet the immediate and long-term challenges we are all set to face. A large part of this will require companies to develop long term strategies, and to set their five-year business plans within the context of the bigger picture. Whilst companies are partially doing this already through frameworks such as water resource management plans and drainage water management plans, there is now a need to expand the remit of how we plan for the future.

This includes aspects such as greater clarity to how the five-year plan will deliver against companies' long-term ambitions, as well as greater clarity on the outcomes that companies have achieved with the commitments they've already received funding for. This will give customers greater confidence that the challenges over the new few decades will be met.

Whilst it can be difficult to predict what is to come, adaptive pathways will allow companies' long term delivery strategies to adjust more efficiently to reflect new information, options, and experiences. We will expect this to be a core principle throughout every company's business plan for PR24.

There is also a role here for us as the regulator to be clearer about which improvements we expect companies to make over time from on-going base expenditure, clarity on the impact of enhancement expenditure on future performance levels, as well as re-evaluating the measures we take if performance improvements are not sustained.

It will also be vital for companies to think about how they effectively collaborate and coordinate with each other and the supply chain to deliver the improvements needed at a scale that hasn't been seen since privatisation. Is it credible to think that each company operating on its own will be able to deliver this or is a stronger coordinated national and regional effort needed to plan and programme this investment? This is something we all need to consider seriously as we look towards the next AMP and beyond.

The second aspect I wanted to mention involves the sector's capacity to improve its long-term resilience.

It's vital that the sector focuses on asset management and delivering sustainable operation resilience and health. In 2022, we collaborated with the sector to co-create the asset management maturity assessment which increased the sector's understanding of how companies monitor and manage the operational resilience of their assets. It's been a great example of the sector (companies and regulator) working together.

And whilst it was positive to see companies demonstrating clear processes, thorough evaluation, and contingency planning, we identified a need for companies to:

- Create a more comprehensive suite of leading and lagging asset health measures
- Have clearer insights into how their investments are delivering intended improvements in performance
- Enable their Boards to take greater interest in asset health in the decisions they take.

Building resilience will also require the adoption new approaches such as direct procurement for customers. As a process for water companies to competitively tender for a third party to design, build, finance, operate and maintain infrastructure, this will ensure that much needed large infrastructure projects are efficiently procured and implemented. This also opens a new long-term pathway for potential investors over the next 25 years.

Although we are in the early stage of implementing the DPC process, we are continuing to develop how we can better support delivery and incentivise companies to engage moving forwards.

Lastly, I believe you should always be asking yourselves, and your organisations, whether you are thinking as creatively and as innovatively as possible. As I mentioned in the first few minutes of this keynote, there must be a real change in how companies work and the investment choices they make. This is to ensure they can meet the sector's targets and enhance the scale of improvement in an affordable way.

This will require companies to fully embrace blue and green solutions, increase their engagement with customers on issues such as reducing blockages and per capita consumption, and leverage greater partnerships with third parties to deliver more for customers and the environment.

On the latter, our innovation competitions are just one avenue that has enabled the sector to be as innovative as possible. Our Breakthrough Challenge competitions have enabled water companies, in partnership with third parties and other water companies, to put forward potentially transformational innovations and get 90% of costs covered by the innovation fund.

So far, we've awarded over £60m on 40 projects across two competition rounds. This includes brilliant projects to transform the wastewater sector such as:

- The AI and Sewer Defect Analysis Project which aims to give a better understanding of sewer deterioration and reduce the cost of inspections
- The Industrial Symbiosis project which will look new ways waste or by-product materials from one company can be used as the raw materials for another.

By May, we'll have spent another £35-40m. You'll be excited to hear that our next competition, which has launched today, will take things one step further...

Our Water Discovery Challenge is a new competition targeting earlier-stage ideas and open to anyone with a potentially game changing idea. Water companies will play a critical role in supporting the assessment of entries and in mentoring those that are successful.

Entries could receive up to £500,000 and a host of non-financial support to test and develop their ideas and progress them towards adoption and roll out. We hope the Water Discovery Challenge will attract a huge range of solutions from outside the sector to further catalyse innovation thinking in the sector.

How Ofwat is stepping up

Alongside companies – we as regulators need to step up our ability to push companies further. The innovation competitions are a great example of a regulatory intervention designed to drive certain behaviours and push companies to go further, but there are other things we can also do.

A good example of this is strengthening our role in company performance monitoring. Our view is that there is the potential to do more to provide a better ongoing picture of the state of the sector. Our latest Water company performance report identified those companies lagging behind expectations who are now required to explain what has led to their poor performance and present a clear action plan to turn this around. Ofwat expects to see companies delivering on their commitments to customers.

We intend to further develop our approach to monitoring company performance to generate deeper insight into where there are sector-wide or company specific major issues and better target regulatory action to address them. Effective collaboration with our partner regulators

will also be vital as well as ensuring progress open data to drive greater transparency, innovation, efficiency and accountability across the sector.

We also know that there is a lot of power in collaboration and Ofwat is keen to ensure that collaboration and innovation sit within the heart of the principals we champion in the sector. That also means ensuring that the sector's regulators are collaborating to eliminate barriers, create opportunities, and hold the sector accountable on what it promises to deliver. A great example of this is our combined service with the EA and DWI, Streamline, which is available to help and support early-stage innovations and address any regulatory barriers and opportunities that may apply.

In terms of boosting the long-term resilience in the sector, we've been working with our partners in RAPID to progress the development of new strategic water resource options. With the demand for water increasing, we expect the companies and regulators to work together to deliver new resources.

Conclusion

So, to finish, I think it is key to note that there are opportunities to make a once in a generation change to improve water quality, performance, and our relationships with customers.

Last year at this conference, I delivered a speech on how regulation will shape the future of wastewater and I still believe in the version of what "Great" would look like. Great is having networks with advanced real time monitoring, great is seeing more green/blue infrastructure that support our precious environment, great is a resilient and pollution free network that companies manage and customers are educated on.

Following my speech today, I think it's important to highlight that great will include companies delivering resilient and adaptable investment plans that customers can be proud of.

In the immediate term, companies should be looking at how they can make this a reality and the bottom line is that we do not have the luxury of time. With our climate changing and our population growing rapidly, we need tangible solutions that we can rely on for the many generations to come.

And I know that this is something that can be achieved if we get the balance right and all of us, companies, regulators and wider society play our part.