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For the attention of Jonson Cox, Chairman

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29 August 2019

Dear Jonson

BOARD RESPONSE TO THE DRAFT DETERMINATION

I am writing on behalf of the Board of Dŵr Cymru Cyf. in response to the Draft Determination issued by Ofwat on 18 July 2019. Throughout the PR19 process, our Board has been deeply involved in leading the development of our future plans for our customers, for the next five years and beyond. Indeed, the quality of our planning and Board assurance process was highly commended by Ofwat in its Initial Assessment of Business Plans (IAP). Throughout, we have pushed ourselves hard to come up with an ambitious plan, which will strike the optimal balance between the particular needs and priorities of our customers, both now and for future generations. Our Business Plan, submitted in September 2018, was very well received by our customers (with an acceptability level of 92%) and by our stakeholders. Our Board remains of the view that this Plan, if delivered, would represent a very good outcome for our customers.

We welcome some significant items of progress since the IAP in January 2019 but there remains an unsustainably large gap between our Business Plan and the Draft Determination (DD), which raises serious concerns for our Board. The Board is not able to give an assurance that the DD is financeable, not least because it does not allow funding for certain specific statutory obligations. The Board also has serious concerns that it may be asked to 'sign up' to particular performance commitments set by Ofwat, even where it does not consider them to be deliverable.

However, we are encouraged by the areas of movement in the Draft Determination, which have occurred after constructive engagement between our two organisations, such as the funding allowed for our required reservoir safety programme, for the NEP and for the WRMP. We also welcome the dialogue that has taken place on other aspects of our expenditure plan, such as resilience schemes. In order to concentrate attention on the most serious outstanding issues, we have provisionally moved our position on several material items of dispute, including the efficiency challenge of some programmes (such as the NEP), the scope of our proposed resilience programme, and aspects of the proposed performance commitments and ODIs.

However, time is now very short to resolve the remaining substantial areas of disagreement between us, if we are to reach a Final Determination (FD) that is acceptable to all parties and a good deal for our customers. In this letter, I therefore summarise the most important issues of disagreement that we have with the DD, with the aim of focussing consideration and discussion on the points that will matter most in hopefully achieving such an outcome. We have also submitted a revised business plan, reflecting the funding issues outlined below, for which the Board can provide assurance that it is financeable. Further detail is provided in a range of supporting documents and in our revised Business Plan tables.

1. Financeability and the Allowed Rate of Return

In the DD, Ofwat found that the Dŵr Cymru notional company was not financeable without making an adjustment to the PAYG ratio. We concur with that view. However, after detailed consideration, our Board is not able to give the required assurance that the DD is financeable, because:

- the DD does not fund certain specific statutory obligations (see below), which cannot be absorbed within the overall, very challenging financial settlement;
- our DD package of financial ratios (notably FFO/net debt and RCF/net debt) for the notional company is much weaker than that for all the other water and sewerage companies, and does not meet the tests for financeability;
- the ratings agencies will in practice use their own definition for AICR, which is materially less favourable than Ofwat's definition, resulting in a level which is also not financeable;
- there is a clear downside risk to the central case projections, as demonstrated in the RoRE range reported in the DD; and
- we do not accept some important elements of Ofwat's calculation of the allowed rate of return (WACC) at the DD, which seems to be clearly too low in practice, in that it results in financeability adjustments for nearly half the companies in the sector (8 out of 17).

We have submitted a revised business plan, for which the Board can provide assurance that it is financeable. To arrive at that financeable business plan, use is made of the financeability "levers" (PAYG ratio and RCV run-off rate) made available in the DD, to deliver notional company financial ratios which are more consistent with those for other companies in the sector.

PAYG rate

In the DD, the level of the PAYG ratio set by Ofwat was calculated on a basis which did not reflect the high proportion of enhancement expenditure which had been "disallowed". We have recalculated the required level of the PAYG ratio in our revised business plan, at 51.2%, reflecting the revised proportions of operating costs and IRE. However, as in the DD, a further increase in the PAYG rate is required to deliver a plan which is financeable for the notional company, for the AICR ratio. The revised average PAYG rate at 52.9% remains well within the pack for the sector as a whole.

RCV run-off rate

The DD in our case results in levels for other key financial metrics for the notional company which are well below the norms established by DDs across the sector. In particular, the FFO/net debt and Retained cash flow (RCF)/net debt are much the lowest for the water and sewerage companies (WaSCs), being significantly below the levels set for other companies where Ofwat either intervened or accepted a company's intervention on grounds of financeability. In large part, this reflects the fact that the RCV run-off rate for Dŵr Cymru, at 3.5%, is the lowest for the WaSCs.

Table – Key cashflow ratios in WaSC Draft Determinations (notional companies)

Company	FFO/net debt	RCF/net debt	RCV run-off rate
Anglian	9.3%	7.2%	4.7%
Northumbrian	10.0%	7.9%	4.8%
Severn Trent	10.0%*	7.6%	5.0%
Southern	10.9%	8.9%	5.2%
South West	11.9%	9.5%	4.9%
Thames	8.8%*	6.8%	4.4%
United Utilities	9.8%*	6.7%	4.6%
Wessex	9.2%	7.3%	4.3%
Yorkshire	9.4%	7.4%	3.8%
Implied DD Threshold	c. 9%	c. 7%	-
Welsh Water	7.6%	5.5%	3.5%

Note: *denotes companies where Ofwat intervened at the draft determination stage to restore an acceptable level of FFO/net debt.

In our revised business plan, we have modestly increased the RCV run-off rate to 3.75%, so as to achieve levels for FFO/net debt and RCF/net debt which are more in line with the norms for financeability established in the DDs across the sector, thus allowing the Board to give assurance that the notional company is financeable on that basis. At 3.75%, our RCV run-off rate remains the (equal) lowest for the water and sewerage companies at the DD stage.

Revised business plan

Notwithstanding these changes, the revised business plan results in a level of the average customer bill at the end of the period which is below that in our original business plan, which already had a strong level of customer support – a view endorsed by our CCG. (We have not proposed a greater use of the financeability levers in our revised plan, which could arguably be justified, so as to ensure that the average bill for customers remains below that in our original plan.)

Our revised business plan also reflects the preferred overall balance of our customers as revealed in a large body of customer engagement over a number of years. Most notably, when presented with a choice exercise, customers preferred, by a ratio of 2:1, the option with higher investment in service and resilience to the option which maximised the reduction in the average customer bill.

Long term financial resilience

In addition to assurance on financeability during AMP7, the DD requests Boards' confirmation of the long-term financial resilience of their actual business, in light of downside risks on issues such as cost reductions or ODI penalties and, in particular, a possible further reduction in the allowed rate of return (WACC) at the FD in December 2019. In practice, it is not possible for any Board to give long term assurance of financial sustainability resulting from a FD which has not yet been determined. Our financial modelling at this stage shows that a further reduction in WACC at the FD would not be financeable.

In our case, there would be scope for further upward adjustments to the RCV run-off rate, to restore the key cashflow ratios (FFO/net debt and RCF/ net debt) to acceptable levels. However, AICR is already a binding constraint. Further adjustments to the PAYG to levels above the "natural rate"

would be ignored by Moody's and Fitch in calculating their AICR, which would lead to negative credit rating implications for the company. (Increases in the RCV run-off rate do not impact on AICR).

Whilst the "actual" company could withdraw all its 'customer distributions', this would have a limited impact on its financial ratios and would have serious negative consequences for the funding of social tariffs for disadvantaged customers (see below).

At the sector level, many companies already have a significantly higher levels of PAYG and RCV run-off rates than we do, which suggests that there would be limited scope to make further use of these financeability "levers" for these companies without impacting on the sustainability of their Regulatory Capital Values (RCVs), leading to negative credit rating action across the sector.

As such, we strongly question whether there is any scope to make further reductions in the allowed rate of return (WACC) at the FD without causing significant negative credit rating consequences for our company and for the sector, which would not be consistent with long-term financial resilience or the efficient funding of future capital investment for customers. We would strongly caution Ofwat against placing reliance on current market estimates of WACC to justify setting an even lower allowed rate of return at the FD, given the very unusual and volatile market conditions that we are experiencing and the potentially very damaging consequences for customers of wholesale credit rating downgrades across the sector.

2. Allowed Wholesale Expenditure

The DD reflects a gap of some £400 million between the wholesale Totex allowed in the DD and our Business Plan, of which £360 million relates to enhancement expenditure. We have dropped or amended several expenditure items in our Business Plan, which reduces the gap in enhancement expenditure to around £250 million. The remaining disputed Totex cost items are summarised briefly below; all of which we need to be funded in full in the FD, to have a financeable plan which allows us to meet our statutory obligations and our commitments to our customers.

Funding for Statutory Obligations (£100 million)

- DWI water network improvement notices for 17 water distribution zones, which are only funded to 50% of their forecast cost in the DD. These are specific statutory obligations on the company, which need to be funded in full if we are to achieve a financeable Business Plan. (£59m)
- Water Treatment Works (WTW) maintenance - as part of the proposed DPC scheme for the new Merthyr WTW, the DD assumes that maintenance can be significantly reduced at the 3 existing WTWs in the area, whilst the new WTW is under construction. Delivering drinking water to the required standards is a clear statutory obligation on the company and it will not be possible to deliver that without maintaining the existing WTWs throughout the AMP7 period, given that the new WTW is not scheduled to come into production until well into the AMP8 period. (£17m)
- Drainage and Wastewater Management Plans (DWMPs) - the Welsh Government is expected to make DWMPs a statutory obligation on companies in Wales. In part, this reflects advice from Natural Resources Wales (NRW) that these DWMPs are a crucial input to achieve the wider benefits of the Sustainable Management of Natural Resources (SMNR) at a "place based" level, as required under the Environment (Wales) Act 2016. As such, the DWMPs also have an important element of "public value", as they enable NRW and other environmental stakeholders to unlock further benefits for ecosystems and biodiversity at the catchment level. (£14m)

- Cyber security - the DD only funds 50% of the costs of meeting the new Cyber security requirements on water companies, as set out in the Security of Network and Information Systems (NIS) Regulations. Again, these are a statutory obligation on the company which need to be funded in full. (£10m)

Funding for Resilience Schemes (£34 million)

- South Wales water grid - the creation of a new water grid, by building an inter-connection between the Cardiff and the Swansea supply systems, would significantly enhance the water supply resilience in south Wales, mitigating key single points of failure that are beyond management control. We have responded to Ofwat's requests for further detailed information on the risks addressed and the proposed mitigation option. (£20m)
- The Hereford supply system - being completely dependent on a single river abstraction for the supply of 117,000 people represents a clear example of a low probability, very high impact risk resulting from a single point of failure that is outside management control. Again, we have responded to Ofwat's requests for further detailed information. (£14m)

Funding for Public Value Initiatives (£26 million)

We are very supportive of Ofwat's proposed new vision for the water sector, which has three main elements – stewardship for the future, delivering everyday excellence and delivering public value. In the past, Dŵr Cymru has been able to fund significant delivery of public value from its 'customer distributions'. In light of the very challenging nature of the financial settlement proposed in the DD beyond 2020, with a much reduced allowed rate of return, it will be very difficult for us to fund such public value delivery in future. In these circumstances, Ofwat has suggested that we might consider whether there is scope to "make explicit" such public value initiatives in our AMP7 Business Plan.

- Project Cartref (Home) - has been recognised in the DD as a highly innovative programme to reduce water loss and wastage inside customers' properties. This programme could lead the way to reduce the water consumption of customers across England and Wales, as well as delivering substantial public value benefits to the customers concerned, in terms of giving them greater control over their water bills, saving disadvantaged customers money and helping to reduce their carbon footprint. To date, only 50% of the cost of Project Cartref is allowed for in the DD, which does not make it viable to proceed with the project as planned. (£14m)
- Visitor Centres- our proposed bespoke Performance Commitment for Visitors to Recreational Facilities (Ft11) is based on the proposed expansion of our visitor centres and a new centre at the Lisvane and Llanishen reservoirs in north Cardiff. These centres will deliver significant public value benefits in terms of recreation, education, healthy lifestyles and biodiversity. We had hoped to be able to fund these new centres through our 'customer distributions' but the very challenging nature of the DD does not make it possible for us to do this. Therefore, we now propose to bring these schemes into our AMP7 investment plan. (£12m)

We believe that the concept of delivering public value also has relevance for certain aspects of our retail cost base and for our approach to funding social tariff support for customers post 2020, both of which are referred to further below.

Funding for Service Improvements (£106 million)

The DD methodology is that “performance levels are achievable under base cost allowance and that companies should be aiming to continuously improve service within base cost allowances”. Whilst we accept that companies should always be striving to improve performance levels, we do not believe that the proposed “step change” in performance levels for some measures can be achieved without some specific funding allowance for enabling investments. In the past, such investment by companies has been allowed for as enhancement expenditure and so was not recorded within Botex outturns and is not, therefore, reflected in Ofwat’s modelled level of efficient Botex expenditure, using historical data. In addition, diminishing returns in service improvement investment mean that it will cost more in future to achieve incremental improvements than in the past.

In our case, the biggest areas of service enhancement expenditure not allowed for in the DD are:

- leakage reduction (£38m)
- supply interruptions (£22m)
- sewer flooding mitigation (£42m)
- pollution incident reduction (£4m)

Botex cost modelling (£29 million + frontier shift)

Whilst cost modelling in the water sector is necessarily imperfect, we believe that the Botex cost models that Ofwat has used as the basis for the DD generally function as intended and produce meaningful results. In most cases, we welcome the adjustments that have been made to the models in response to feedback received from companies at the IAP stage.

Our principal objection to the Botex allowances in the DD relates to Ofwat’s assumption of a frontier shift in cost efficiency which outperforms CPIH by 1.5% a year. Whilst welcoming the recognition of a real price effect for labour costs, we continue to believe strongly that the methodology underlying this assumption is unsound and that the data it draws upon is significantly out of line with market expectations for productivity growth in the UK economy over the next 5 years. In addition, the cost frontier shift taken together with the very significant improvements in service performance assumed in the DD effectively results in a “double counting” of the scope for quality adjusted productivity growth, resulting for example in a 13% required productivity shift over 5 years for our water network activities.

There also remain a small number of specific points related to the DD allowance for Botex.

- Wastewater business rates - the increase post 2020 is determined by changes to rateable values that have already occurred or which are predictable. In these circumstances, which are more certain in Wales than in England, it is wrong not to allow for these known cost increases. (£16m)
- The enhancement opex adjustment - was introduced at the DD stage. We believe this is based on a misinterpretation of “enhancement opex” insofar as it effectively removes from our botex allowance an amount which is based on an extrapolation of other companies’ data and which was never part of our cost plan in the first place. (£13m)

3. Performance Commitments and ODIs

Ofwat's approach of setting "upper quartile" cost efficiency targets and "forecast upper quartile" performance targets in isolation from each other risks setting a combined cost-service frontier which is not actually achievable. Following receipt of the DD, we have looked closely at the proposed targets and incentives proposed, with a view to accepting those where the differences to our Business Plan are not material, or where we accept that Ofwat's proposal is based on sound evidence. However, there remain a number of key differences, which are summarised briefly below.

Common performance targets

The performance targets set out in our Business Plan were challenged in detail by the Board and found to be stretching but achievable, given the particular circumstances in which we operate. Our Board has serious concerns that it may be asked to 'sign up' to particular performance commitments set by Ofwat, even where it does not consider them to be deliverable, or which would only be achievable on the basis of enabling investments which are not currently funded in the DD. To do so would undermine the credibility of target-setting for the business as a whole and could weaken our customers' confidence in the business.

Whilst we support Ofwat's desire to promote service improvement, we continue to believe that service targets need to reflect i) the differing starting positions of companies, ii) the differing operating environments within which they operate and iii) the differing priorities of companies' customers. In particular, having set targets which the Board considers to be stretching for the following measures, we do not believe that the target levels set by Ofwat in the DD are achievable:

- *Interruptions to water supply* – where our network topography leads both to more bursts per customer and also to longer lead times to effect repairs, with limited network inter-connectivity in rural areas;
- *Pollution incidents* – where more detailed analysis shows that our proposed target in fact outperforms the industry upper quartile (see below);
- *Sewer flooding (internal)*; and
- *Sewer flooding (external)* – in both cases, we have submitted new data from the Met Office which demonstrates a significantly greater than average impact in our case from the change in definition to include the impact of severe storms.

In the case of pollution incidents, we have proposed an alternative approach to model the upper quartile level of performance, taking account of all the various wastewater assets that can give rise to pollution incidents, not just the length of sewers. On the basis of this more sophisticated approach, which we understand is supported by NRW, our business plan target exceeds the forecast upper quartile performance for the sector. We would urge Ofwat to develop similar econometric models for each performance commitment to set service targets that reflect differences in operating environments, in the same way that it uses econometric models to determine cost efficiency targets.

ODI rates

We have gone to considerable effort to explore the views of our customers in terms of penalty and reward rates for ODIs, including further willingness to pay research carried out in conjunction with our Customer Challenge Group (CCG) in April 2019, after the submission of our April 2019 Business Plan. The overall quality of our customer engagement for PR19 was also well received in the IAP. On that basis, we cannot accept the approach in the DD for some ODIs, where the rates that reflect the views of our customers have been challenged on the basis of sector averages or the particular

rate proposed by a different company. In some cases, this does not lead to a material divergence but in the following cases we believe that the DD ODI rates should be reset at levels which reflect, in large part, the views of our customers.

- Interruptions to water supply
- Sewer flooding (internal)
- Sewer flooding (external)
- Per Capita Consumption (PCC)

To not do so risks invalidating the customer engagement work we have carried out for PR19, including the work of our CCG.

Ofwat's interventions on ODI targets and rates have resulted in a skewed range of potential penalties and rewards (-1.5% to +0.42% as a RoRE range). This does not result from a lack of ambition by the company but is the inevitable outcome of incentives on individual measures in the DD which are now heavily biased to the downside. For example, the maximum penalty for water supply interruptions to the average customer is for 28 minutes (£21 million in 2024-25) as compared to a maximum theoretical reward capped at 17 seconds (£175,000).

Rejected ODIs

We also think that it is wrong for Ofwat to reject certain bespoke reward and penalty measures proposed in our Business Plan, which had support from our customers. These included asset resilience measures, community education and visitors to recreational facilities.

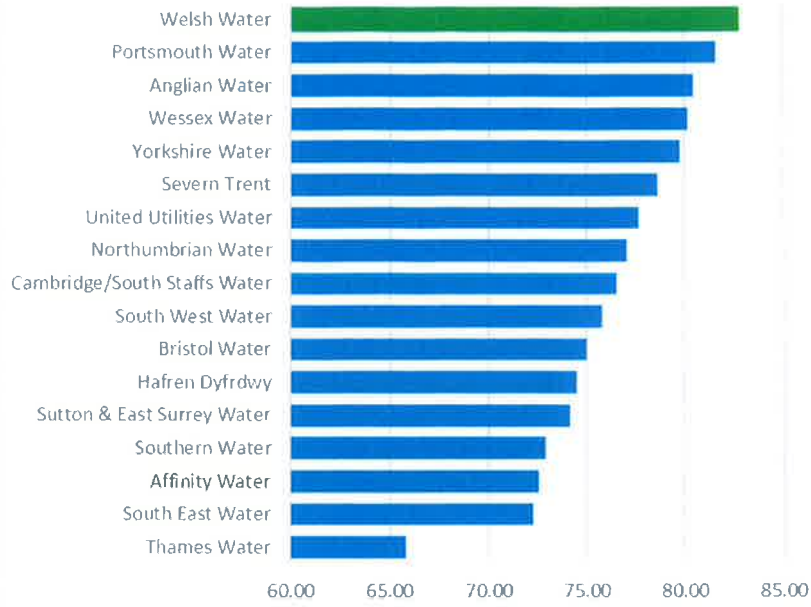
Customer Trust and C-MeX

Ofwat has also expressed concerns about our proposed ODI for Customer Trust, which it considers overlaps with the C-MeX measure. Whilst we accept that point to some extent, we remain concerned that C-MeX alone does not provide sufficient incentivisation for companies that are ambitious to push forward the frontier for customer trust and service.

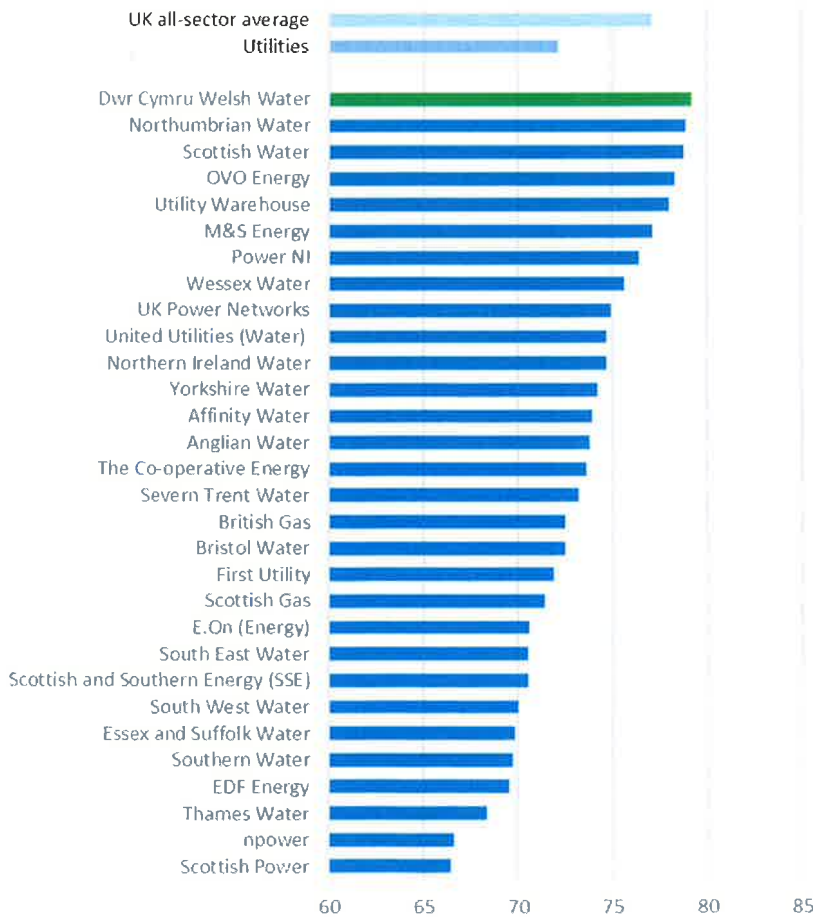
In particular, Ofwat propose to cap C-MeX rewards at a relatively modest level, unless a leading water company is also upper quartile across all sectors in the Customer Satisfaction Index (CSI) produced by the UK Institute of Customer Services. However, we do not believe that Ofwat's proposal is an appropriate use of the CSI, as that index is derived from interviews with a small, self-selected group of customers for each business, giving results that are statistically much less reliable than C-MeX itself. In addition, the CSI survey method consistently results in much better scores for sectors with positive, discretionary interactions with customers in person (such as retail, tourism and leisure) than for universal service sectors with often remote contact channels (such as utilities, transport and public services).

This point is clearly illustrated by our current performance where we are ranked top of the water sector on the C-MeX measure (year to date) and are also the top ranked company in the CSI for the utility sector (outperforming market leading, "disruptor" energy companies such as Ovo Energy, M&S Energy and Utility Warehouse) but we would nonetheless fall well short of the overall CSI upper quartile value:

C-MeX Quarter 1 Results



Organisation Ranking by UKCSI Score (July 2019, ICS Utilities Report)



4. Household Retail Price Control (£23 million)

The cost modelling for household retail services is inherently more problematic than for wholesale costs, in part because of inconsistent accounting policies between companies in areas such as void properties, revenue recognition, cost allocation between services and providing for bad debts. In addition, companies operate in geographically separate markets with very different characteristics, in particular in terms of the levels of disadvantaged customers served. In these circumstances, it is perhaps not surprising that the DD household retail cost models have relatively weak explanatory power, with our business plan level of cost being significantly above the modelled level.

In our response, we have set out some amendments to Ofwat's cost modelling approach, which would better reflect the circumstances within which we operate, materially reducing the size of that gap. These include taking account of quality of service and addressing an inconsistency between the way that Ofwat has reflected income deprivation for English and Welsh companies. In addition, we have had a further detailed external review by PwC which concluded that we are operating in line with "leading practices and performance in debt management".

We also believe that a proportion of our retail cost base reflects the service preferences and requirements of our customers – reflecting aspects of public value delivery. These factors include the cost of administering social tariff support to a far larger proportion of our household customer base (at around 10%) than any other water company. In addition, the cost of bi-lingual service provision are material and are a statutory requirement on us under the new Welsh Language Act. These two aspects add over £10m to our retail cost base over the period.

5. Social Tariffs

Our business plan included an aspiration to grow our level of support for disadvantaged customers over the course of AMP7, funded in part by an increasing 'customer distribution', as we have achieved in AMP6. However, given the extremely challenging nature of the DD, we are not currently able to commit to any level of support. The resulting uncertainty that this situation creates could have serious consequences for our ability to sustain the existing level of social tariff support for the current 110,000 households who benefit from it (around 10% of households).

Ofwat has suggested that it would be preferable for Dŵr Cymru to make a firm commitment to a certain level of social tariff funding. Our revised business plan includes an assumed level of 'customer distributions' to support social tariffs at around the current level of £11 million a year, funded by advancing value from subsequent periods through an additional RCV run-off rate adjustment. (This is roughly equivalent to twice the proportional level of company support envisaged in the DD for United Utilities, for example.) We have adjusted our performance commitment for vulnerable customers on social tariffs (BI2) accordingly. We also retain our commitment to share all net outperformance rewards with customers, including through additional funding for financial support for disadvantaged customers.

However, it is conceptually very difficult for our Board to "commit" to any level of funding given the large "gap" between our revised plan and the DD. We would therefore propose to have further dialogue with Ofwat whilst the FD is being finalised to explore the potential implications for the

funding of social tariffs, not least because decisions on the tariffs for April 2020 will need to be finalised very soon after the FD is received and would not be avoided by an appeal to the CMA.

We understand that Welsh Government may reconsider its formal guidance on social tariffs during the second half of 2019, which could impact the level of cross subsidy available for social tariff support in the longer term. To reflect this possibility, rather than the entire reduction in the average bill happening at the start of the period with bills held flat in real terms thereafter, we have adapted our proposed bill profile, so that it allows a decline in real terms throughout the AMP7 period, finishing at around £413 a year (as compared to £439 this year – at a 2017-18 price base). Such a profile would make it possible to gradually increase the level of cross subsidy to fund social tariffs during the course of AMP7, if that were to be allowed by Welsh Government's revised Guidance, without resulting in above inflation increases in bills for non-social tariff customers. We have not had the opportunity to test this revised bill profile with customers directly in the time available but we will be discussing the proposed change with our CCG.

6. Other issues

Merthyr Tydfil Water Treatment Works (WTW)

The DD is welcomed in that it supports the need for the new Merthyr Tydfil WTW. However, it proposes that the scheme should be taken forward by Dŵr Cymru as a direct procurement for customers (DPC) scheme. We believe that it is imperative that the new WTW is provided as quickly and reliably as possible, as it is required to meet existing DWI statutory obligations and is essential in addressing key single points of failure in the south Wales water supply system.

The proposed use of the DPC route does raise uncertainties for us – in terms of a risk of delay to the delivery of the scheme, whether in practice it would deliver cheaper funding for our customers and how to ensure the safe operation of such a highly integrated network asset by a third party working under contract. We would, therefore, welcome further multi-party dialogue with Ofwat and the DWI on the best way to apply DPC in this case, to achieve the timely and efficient delivery of this strategically important scheme.

Loughor Rainscape expenditure

We have written separately to Ofwat on the unique circumstances surrounding this investment scheme, which has resulted in the highly innovative retro-fitting of sustainable urban drainage systems (SUDS) into industrial era communities, achieving a huge cost saving for our customers and major enhancements to biodiversity and the local quality of life. As such, Rainscape is an excellent example of the delivery of public value through the exercise of our functions, albeit one that required us to phase the work over a longer time period for transition expenditure than generally allowed. Had we left the work to be commenced within the transition window, the work could not have been completed by the December 2020 legal deadline, likely resulting in Infracore fines levied on the Welsh Government by the EU Commission. We remain of the view that the Rainscape expenditure should therefore be allowed for in full in the PR14 reconciliation model.

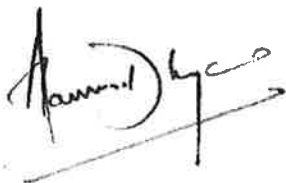
7. Conclusion

The Dŵr Cymru Board believes that our September 2018 business plan and our revised business plan of April 2019 were ambitious and sought to strike the optimal balance for our customers between the future level of average bills, investment in improving service standards, the long-term resilience of the system and the delivery of public value. Our plans have received strong support from our customers (with 92% finding our September 2018 plan to be acceptable and 95% rating it as affordable) and also from a wide range of stakeholders in Wales. Our plans reflect the particular, local circumstances within which we operate and are closely aligned with Welsh Government's Strategic Priorities Statement and with the objectives and ways of working set out in the Well-being of Future Generations (Wales) Act 2015.

Whilst we welcome aspects of the Draft Determination received on 18 July, we have concluded that it does not reflect the priorities of our customers as evidenced in numerous research and engagement activities over a number of years, most notably their preference for increased investment rather than the maximum average bill reductions. It is also not financeable in its current form.

However, with the changes suggested in this response and as reflected in our revised business plan, we believe that a Final Determination could still be reached that would be ambitious, challenging, financeable, affordable and which strikes the optimal long-term balance for customers. We welcome the engagement with Ofwat that we have had to date and we stand ready to work further with Ofwat and other stakeholders over the coming weeks to achieve that common objective.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Alastair Lyons', with a horizontal line drawn underneath it.

Alastair Lyons
Chair of the Board