

AN OPEN LETTER
FROM THE CHAIRMAN
OF GLAS CYMRU,
ALASTAIR LYONS

2020–2025



Dŵr Cymru
Welsh Water

CONTENTS

THE BOARD'S APPROACH TO PR19 AND WELSH WATER 2050	8
LISTENING TO OUR CUSTOMERS	10
THE BOARD'S STRATEGIC PARAMETERS FOR PR19	12
AFFORDABILITY	14
IMPROVED SERVICE AND VALUE FOR MONEY	16
WELSH WATER 2050 – RESILIENCE IN THE ROUND.....	20
DELIVERING FOR CUSTOMERS – INNOVATION, EFFICIENCY AND COLLABORATIVE WORKING.....	22
KEEPING OUR CUSTOMERS INFORMED AND INVOLVED	26

This business plan is the culmination of over two years' work by the Board of Dŵr Cymru Welsh Water and we would like to thank all those thousands of customers and other stakeholders, including the Customer Challenge Group (CCG) and our independent Members, who have contributed their views during this process to help make this the most customer-driven business plan Welsh Water has ever produced.

Because we have no shareholders, our company culture is always to strive to do a better job for our customers, both now and long into the future.

Our customers' priorities reflect the unique social, topographical and climatic features of the areas we serve, especially in terms of the long-term challenges we face:

- the impact of climate change, such as the increased risks from more extreme and frequent rainfall events for urban flooding and reservoir safety
- population growth and increased urbanisation, especially around Cardiff, Swansea, Chester and Hereford
- increased stress on the environment from the potential intensification of land-use and greater risks of floods and droughts
- tighter quality standards for drinking water and environmental protection
- preserving the resilience of essential public services with an ageing infrastructure, and
- rising customer service expectations (from households, businesses and developers)

In this document, we set out our plans for bills, service standards, investment and value for money for customers over the five years to 2025 and beyond.

We also explain how we intend to report each year on delivery against the overall plan and the measures of success contained within it, so our customers and other stakeholders can judge for themselves how we are progressing.

The Board of Welsh Water has provided in-depth leadership throughout the development of this business plan, supported and challenged at every stage by the CCG.

The resulting business plan meets the strategic parameters set by the Board last year and the Board has ensured the targets for cost efficiency, service performance, future resilience and support for vulnerable customers are ambitious, but also deliverable and affordable.

At the end of the process, the Board commissioned independent research into the overall acceptability of the plan for customers, which found 92% of our customers found the plan acceptable and 95% found it affordable (including those who considered it would be affordable at "a stretch"), with consistently-high support across all customer groups.

Through review of the key risks to the delivery of the business plan, the Board is assured the business will remain financially resilient to severe, combined-downside scenarios, given the maintenance of a gearing level of around 60% in our central case.

The Board has also overseen a comprehensive programme of internal and external assurance of the plan itself.

As a result of this exhaustive process, we are confident our ambitious business plan to 2025, set in the context of our long-term resilience vision set out in Welsh Water 2050 and based on our ongoing engagement with our customers, will enable us to continue to meet our obligations as the supplier of an essential public service and to "earn the trust of our customers", not just for the next five years but for future generations to come.



ALASTAIR LYONS
Chairman

THE BOARD'S APPROACH TO PR19 AND WELSH WATER 2050

The Board set out its approach to PR19 at the outset of the process in September 2016.

The Board decided its business plan to 2025 and beyond should:

- be driven by the views of customers, elicited through an unprecedented programme of customer research and engagement
- should be developed in the context of a long-term plan that looked forward a generation – Welsh Water 2050 – similarly reflecting the views of customers

- set ambitious targets to improve costs, service and resilience for the benefit of customers, harnessing innovation and new ways of working
- have a particular focus on the needs of customers in vulnerable circumstances, including those struggling to pay their water bill

- incentivise through objective and stretching performance measures the business and management to deliver improved value for money and resilience for customers, and enhance the financial, corporate and operational resilience of the business.

During 2017, the Board developed its long-term vision for Welsh Water in 2050, "to become a truly world class, resilient and sustainable water service for the benefit of future generations".

The Board decided to adopt a new long-term strategic planning approach, informed by a review of international best practice in resilience planning (notably the Rockefeller Foundation 100 Resilient Cities initiative).

This approach is based on the Welsh Water Resilience Wheel, which captures all aspects of what it means to be a resilient public service provider – including assets, systems, people, finances and governance.

Using this approach, we consulted and worked extensively with our customers the CCG and numerous stakeholders to develop 18 strategic responses, which we will need to deliver over the next six five-yearly regulatory periods, in order to meet the challenges and opportunities of the future.

This business plan for 2025 and beyond has been developed from the outset as an ambitious, but affordable step towards the achievement of the Welsh Water 2050 vision. Customer engagement

work has demonstrated very strong support from across our customer base for taking this long-term planning approach, recognising the importance of future investment and innovation to preserve the resilience of the essential public services we provide, which is so important to customers and the environment.



GLAS CYMRU BOARD OF DIRECTORS

LISTENING TO OUR CUSTOMERS

Welsh Water is the only private, non-shareholder-owned water company in the UK. Our vision is “to earn the trust of our customers, every day”.

As such, it is natural for us to want our business plans to be informed by the greatest degree of customer insight and customer involvement we can achieve, so we can really be sure that we are delivering against customers' priorities and that we strike the right balance between customer bills, service standards and investment in long-term resilience.

For this reason, we have a comprehensive, ongoing programme of gathering customer insight, guiding the decisions we make each year. We have built on this comprehensive knowledge base through an unprecedented programme of customer engagement, firstly in the formulation of Welsh Water 2050 and then in the development of our plans

for the period 2020 to 2025 and beyond.

This programme of customer involvement over recent years has seen around 40,000 customers sharing their views with us through our “Have Your Say” and PR19 campaigns, at a wide range of shows and events across our region, as well as directly via our online engagement site.

We have introduced successful innovations in this process to increase the numbers and spread of customers getting involved – using tools such as our

chatbot questionnaire on social media, our new Online Customer Community and our Youth Board. We have supported all this engagement with a comprehensive programme of independent market research, using a wide range of qualitative and quantitative techniques to ensure a truly representative view of customer opinion is obtained.

We have been greatly helped in this by the work of our CCG and the Consumer Council for Water (CCWater), who have challenged us throughout the process on the methods used,

the coverage achieved, the interpretation of the results and their integration into our planning process.

We have gathered a wide range of customer opinion through this programme, reflected in many aspects of the detail of our plan. Overall, certain key themes have emerged which have been repeated through the many exercises and engagement channels:

- affordability is a key concern for customers – but there is no overriding desire to reduce bills at the expense of other considerations

- customers would not countenance any deterioration in service levels, even if this were reflected in lower bills

- given the overarching consideration of keeping bills affordable, customers in general are prepared to pay to finance investment that ensures the long-term resilience of the essential services they receive

- the greater the level of information customers have about our company's unique ownership structure and our plans for the long-term, the greater the overall level of trust

in the company and support for our plans

- customers expect us to harness innovation and efficiency to keep down the cost to customers, while communicating effectively the benefits of investments for customers and the environment

- there is majority (but not universal) support for special help for those customers who are genuinely struggling to pay their water bills, and

- customers expect us to protect the environment and contribute more broadly to the well-being of the communities we serve

In some cases, our customers' views may be somewhat different to those of the customers of other water companies, probably reflecting our unique ownership model, a particular sense of community in Wales, and also the impact of the overarching long-term policy framework set out in the Well-being of Future Generations (Wales) Act 2015.

THE BOARD'S STRATEGIC PARAMETERS FOR PR19

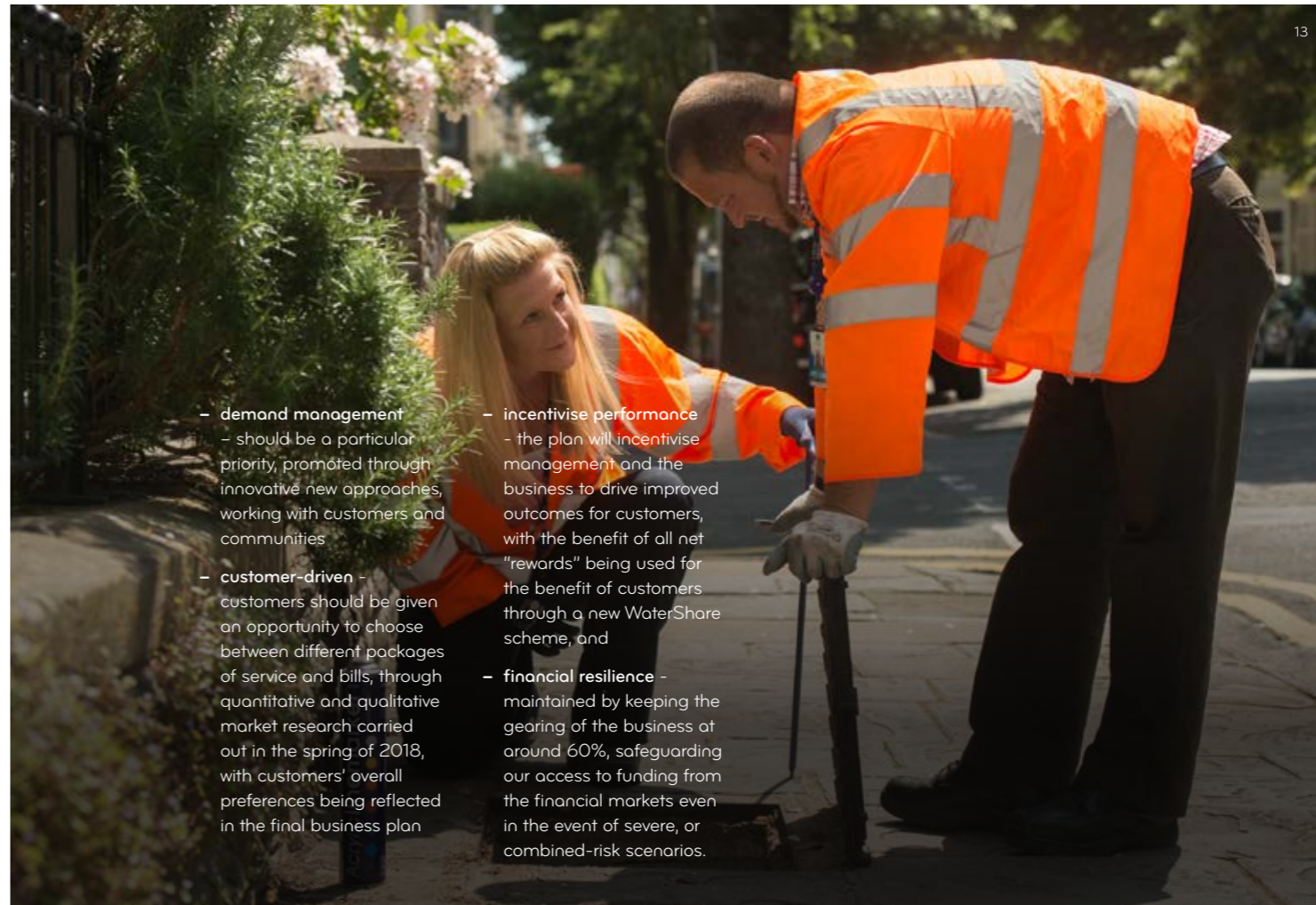
Having carefully considered all this customer sentiment, at the end of 2017 the Board set 10 key Strategic Parameters for our business plan to 2025:

- **affordability** – customers as a whole should see a reduction in the average bill in real terms, reflecting the reduction in the allowed level of profitability post-2020 (the “return on capital”)
- **social tariffs** – Welsh Water would aim to expand its funding for social tariffs through its unique “customer dividend”, to help more of those struggling to pay, while keeping the cost of the support from other customers at around current levels (in real terms)
- **long-term resilience** – should be enhanced, through a significant investment programme targeted at the most urgent strategic responses

identified in Welsh Water 2050, covering drinking water, environmental protection and future service resilience

- **stretching performance targets** – must be set, in particular for service areas where our performance falls short of our customers' expectations, while ensuring all existing standards of drinking water quality, customer service and environmental protection are at least maintained
- **ambitious new service offerings** – should be developed, offering improved value for money across all customer segments – households, businesses and developers
- **innovation, efficiency and collaborative working** – should be maximised in the plan, while taking advantage of new market opportunities wherever appropriate, so we can deliver ambitious plans at an affordable cost

- **demand management** – should be a particular priority, promoted through innovative new approaches, working with customers and communities
- **customer-driven** – customers should be given an opportunity to choose between different packages of service and bills, through quantitative and qualitative market research carried out in the spring of 2018, with customers' overall preferences being reflected in the final business plan
- **incentivise performance** – the plan will incentivise management and the business to drive improved outcomes for customers, with the benefit of all net “rewards” being used for the benefit of customers through a new WaterShare scheme, and
- **financial resilience** – maintained by keeping the gearing of the business at around 60%, safeguarding our access to funding from the financial markets even in the event of severe, or combined-risk scenarios.



AFFORDABILITY

Welsh Water has kept the increase in the average household customer bill to below the rate of the Retail Prices Index (RPI) rate of inflation in each year over the 10 years to 2020 – an unprecedented record.

We intend to build on this by reducing average bills by around £20 or 5% over the next five years, before the impact of CPIH inflation. This bill reduction can be achieved through the reduction in the allowed rate of profitability expected for the sector ("the return on capital" or WACC) and by innovating to materially-improve efficiency

within our business. In this way, we plan to deliver a substantial bill reduction, while simultaneously increasing levels of investment to improve service performance and long-term resilience.

In addition, we will target more help to those customers who are most struggling to pay their bills, for example

by promoting metering where appropriate. We plan to increase the number of customers benefitting from social tariffs from around 100,000 today (by far the highest rate of support in the sector) to around 150,000 by 2025 – this will cost Welsh Water itself around £85 million over the period ('customer dividend' money that in other companies would have been paid out in shareholder dividends).



IMPROVED SERVICE AND VALUE FOR MONEY

Businesses, developers and households will see improved value for money, in that they will both see lower bills (from the reduced return on capital), experience improved service levels, receive bold new customer service offerings, and benefit from increased investment to improve the long-term resilience of our public services and the environment.

We have set stretching performance targets for the next five years and beyond, following a process of detailed challenge by the Welsh Water Board and the CCG. While maintaining the current very high levels of drinking water quality and environmental performance, we will target by 2025:

- a 15% reduction in leakage levels (which have already been roughly halved in the last 20 years or so)
- a reduction in the numbers of customers experiencing temporary discolouration or

taste and odour issues with their water supply, from 2.8 to 2.0 (contacts per 1,000 customers)

- a reduction in supply interruptions, which are particularly important for businesses as well as households, from 12 to eight minutes a year per customer
- a 10% reduction in incidents of sewer flooding of customer premises each year, which would otherwise be on an upward trend due to climate change, from 300 to 273 a year

- a 20% reduction in pollution incidents (which are predominantly minor 'category 3' incidents), from 112 to 90 a year, and
- the number of customers receiving a service below our defined minimum-threshold levels will be reduced by 18%, from 1,500 to 1,230, meaning fewer "worst-served" customers suffering from repeated water supply outages, sewer flooding or low water pressure

Our plan includes incentivisation arrangements for the business (Outcome Delivery Incentives – ODIs) which could result in penalties (equivalent to 1.5% of our return on equity – RoRE) or rewards (equivalent to 1.2%).

These ODIs have been selected and scaled to reflect customers' views, as ascertained through a wide range of customer research sources, and are pitched towards the lower half of the Ofwat-prescribed range, reflecting a general questioning by our customers of the appropriateness

of such incentives, given our unique status as a non-shareholder company. In response to these views, we are proposing a new WaterShare mechanism, through which half of any net reward would be immediately returned to customers through lower bills, with the remaining half being used for the benefit of customers after consultation with customers, regulators and the CCG.

We are also planning to introduce a range of innovative new customer service offerings, including:

- a new strategy for a more personalised service for customers in vulnerable circumstances, increasing the number of customers registered to receive priority services from around 26,000 now to 100,000 by 2025
- making our service free to the "worst-served" customers, until we can address or mitigate the root cause of their repeated service failure

- a free leak repair service on customers' supply pipes (no longer limited to one free repair in every three years)
- a free lead pipe replacement scheme, targeting 7,000 customers by 2025
- a new Guaranteed Standards Scheme for housing developers, meaning that they will receive automatic compensation if we fail to hit specified performance timescales
- a unique surface water removal incentive scheme for developers
- for business and non-household customers, an extended range of co-created "value-added" services, such as water efficiency and advanced metering technology, and
- as a major step in demand management, a new service for households to fix leakage on customers' pipes and appliances, identified through the widespread use of

innovative measurement technology (Project Cartref – 'Home'), to reduce leakage on customers' plumbing, improve water efficiency and help customers save money.



WELSH WATER 2050 – RESILIENCE IN THE ROUND

In the next regulatory period we plan an increased investment of around £2.3 billion across our business (compared to around £2 billion in this period), financed by exacting cost efficiency targets rather than increases in customers' bills.

This investment programme will enable us to make a significant step towards the long-term objectives set out in Welsh Water 2050, in particular in the quality and supply of drinking water, enhanced resilience and improving the environment.

Priority investments for the period to 2025 (AMP7) include:

- catchment management plans – working with other land users as our first line of defence for drinking water quality – including the Brecon Beacons Mega Catchment

- comprehensive “zonal studies” investment to refurbish and redesign those priority drinking water networks that give most problems for customers, particularly in terms of acceptability and interruptions – covering 17 zones networks and some 920,000 customers (costing around £130 million as part of a plan covering AMP6, AMP7 and AMP8)

- a substantial extension of our RainScape programme for sustainable urban drainage solutions, covering

10 priority catchments, and reducing sewer flooding

- a major investment programme to enhance the safety of our reservoirs, meeting new requirements to make them resilient to future severe storm risks resulting from a changing climate (costing around £115 million as part of a plan covering AMP6, AMP7 and AMP8)

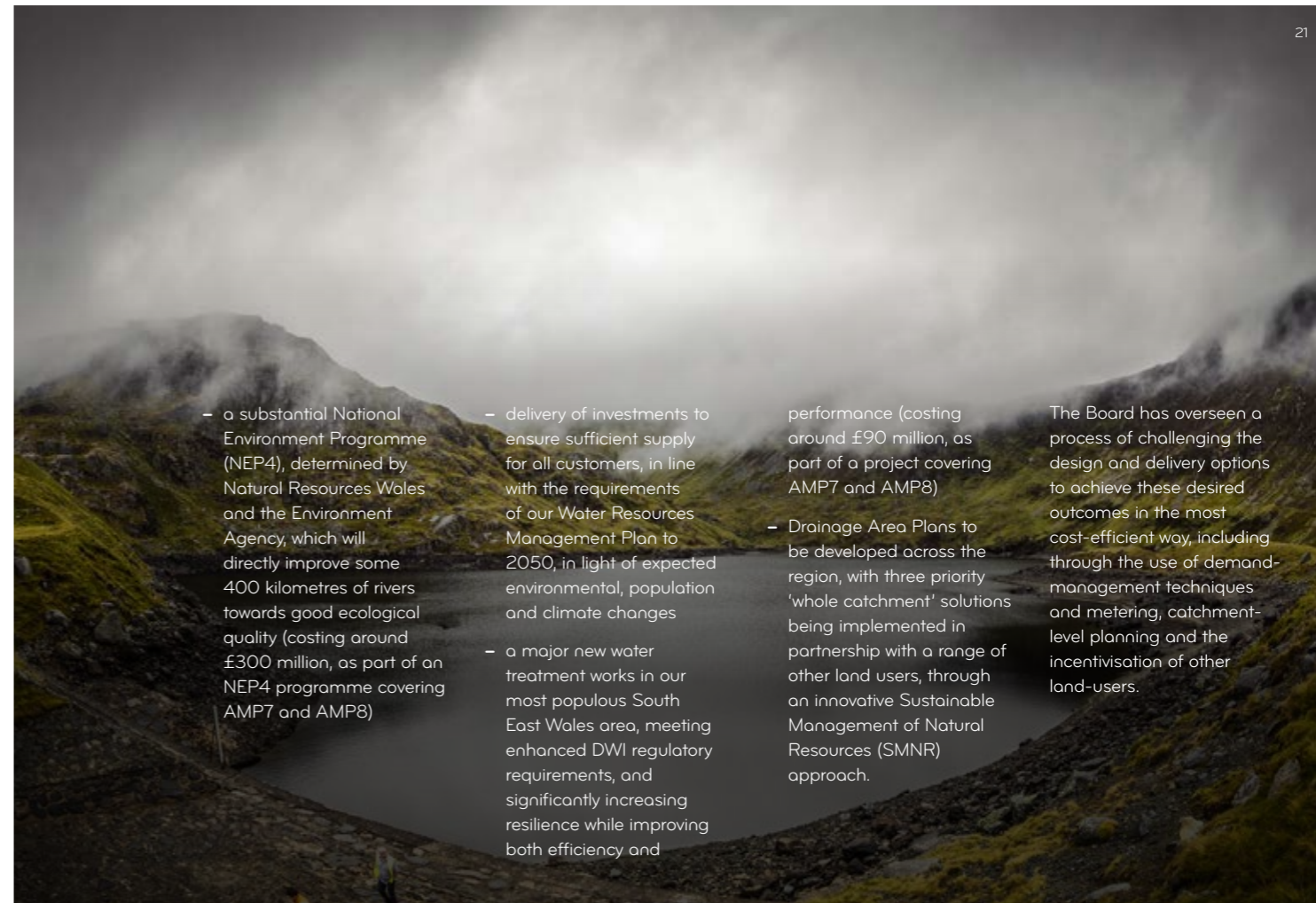
- a substantial National Environment Programme (NEP4), determined by Natural Resources Wales and the Environment Agency, which will directly improve some 400 kilometres of rivers towards good ecological quality (costing around £300 million, as part of an NEP4 programme covering AMP7 and AMP8)

- delivery of investments to ensure sufficient supply for all customers, in line with the requirements of our Water Resources Management Plan to 2050, in light of expected environmental, population and climate changes
- a major new water treatment works in our most populous South East Wales area, meeting enhanced DWI regulatory requirements, and significantly increasing resilience while improving both efficiency and

performance (costing around £90 million, as part of a project covering AMP7 and AMP8)

- Drainage Area Plans to be developed across the region, with three priority ‘whole catchment’ solutions being implemented in partnership with a range of other land users, through an innovative Sustainable Management of Natural Resources (SMNR) approach.

The Board has overseen a process of challenging the design and delivery options to achieve these desired outcomes in the most cost-efficient way, including through the use of demand-management techniques and metering, catchment-level planning and the incentivisation of other land-users.



DELIVERING FOR CUSTOMERS – INNOVATION, EFFICIENCY AND COLLABORATIVE WORKING

To deliver our ambitious plans for customer service and increased investment in resilience, without needing to increase customers' bills, we need to harness the power of innovation, efficiency and collaborative working right across our business.

Innovation: our business plan includes a record budget of £68 million for research, development, science and innovation, with examples across all aspects of the plan. Innovation ranges from scientific research and the adoption of new technology, through to making better

use of the large quantities of data we have in our business and learning from leading organisations in other sectors and other countries. Some representative examples of innovation that we are planning in the next five years include:

- introducing peak flow wastewater treatment technology to supplement the world renowned Sustainable Urban Drainage schemes that we have pioneered – delivering a sustainable solution for urban drainage problems in Llanelli and Swansea for around £130 million, as compared to an estimated £650 million cost for a conventional engineering solution
- partnership with the Natural Environment Research Council (the only one in the water sector) and with the G4W group of water research centres at UK universities, to develop new solutions and methods of working
- a leading participant in the international Smart Water Networks Forum group of utilities, pioneering SMART network management techniques, based on real time data analysis and
- successful "best practice" partnerships with leading international water service providers, Oasen Drinkwater in the Netherlands and Hofor in Denmark

We will also embrace the opportunities from developing market mechanisms to seek better-value outcomes both for our customers and those of other water providers and we are already actively pursuing specific prospects for increased cross-border trading, notably in the areas of bioresources and water resources.

Efficiency: since we became a non-shareholder company, Welsh Water has the best record for reducing operating costs of all of the water and wastewater companies

in England and Wales (according to Ofwat data). Our business plan includes an ambitious target to further reduce our annual operating costs ("Botex" – including asset maintenance costs) by around 10% over the next five-year period, through a wide range of cost saving initiatives, better methods of working and using data to better prioritise our activities.

This in turn contributes to a saving in total costs ("totex" – including capital investment) of around £300 million or 12% in the next five-year

period, as compared to our current level of costs. In part, we can make these savings through working closely with our Capital Alliance of leading international engineering and design companies.

They are working to a rolling, five-year capital programme, with greater incentivisation and opportunity to identify worldwide innovation in design and delivery, while maximising efficiency through maintaining a stable supply chain that avoids the peaks and troughs in workloads which have been evident in previous five-year investment periods.



Working together:

a common theme in our innovation strategy is to find better ways of working with partner organisations and customers, so as to deliver our common goals (as set out in the Well-being of Future Generations Act) more sustainably and more cheaply. Some noteworthy examples of the scope for collaborative solutions include:

- adopting successful techniques from the Catskills water supply catchment of New York State in the Brecon Beacons Mega Catchment

programme, where we will work with a wide range of partner organisations and landowners to improve raw water quality and reduce treatment costs

- a commitment from Welsh Water, Wales and West Utilities and Western Power Distribution to work together and to share appropriate customer information, so we can all do a better job in targeting help to those customers in vulnerable circumstances
- working with social landlords, government

programmes and community groups to promote Project Cartref, which will help achieve a 15% reduction in leakage and improved water efficiency, through working with customers to fix background leaks on their pipes and appliances, and

- creating our first Water Resilient Community in the Rhondda Fach, in which we will work with a wide range of local groups to help us better meet the unique needs of that community, while they help us to deliver some of our priority

objectives more effectively, such as help for customers struggling to pay their bills whom we are unable to contact through traditional channels

Responding to the view of our customers that we should help bring wider economic and well-being benefits to the community we serve, we will also continue to expand our programmes of environmental education for children in our region, the customers of the future, and our provision of recreation and access to the environment.



KEEPING OUR CUSTOMERS INFORMED AND INVOLVED

In our business plan, we have set out targets for 47 measures of success, both to 2025 and beyond, against which we can measure progress in delivering our plan.

We will publish this information each year for customers and stakeholders in an Annual Performance Report, which will also summarise the progress we have made against the 18 strategic responses set out in our Welsh Water 2050 vision. This comprehensive performance information, together with openness and

transparency on our policies for customer dividends and executive remuneration, will help to further build trust among our customers and stakeholders, in a way that is very appropriate for the provider of an essential public service.

We are also committed to regularly engaging with our

customers throughout the period to 2025 on issues that are of real importance to them, such as how we use any financial surpluses for their benefit via customer dividends. This continuing programme of customer involvement will build on the innovative techniques used for the first time during the planning for PR19 and will be supplemented by day-to-day decision making informed by our geospatial "customer sentiment" tracking system. This regular flow of information from customers

will both help us to fine-tune our operations during the period to 2025 and also to be well prepared to further develop our Welsh Water 2050 vision and distil future five-yearly business plans from a strong and ongoing understanding of our customers' priorities.





Dŵr Cymru
Welsh Water