Chapter 1

Risk and return

Risk and Return

1.0 Overview

In this section we address the following issues:

Section heading	Key representation	Relevant appendix
1.1 Cost of capital	Addressing the implications of the lower WACC and what it means for the package in the round. Detailed comments on beta, risk free rate and debt	Annex A – Board Assurance statement
1.2 Financeability	Addressing the implications of the lower WACC for HD	
1.3 Retail modification factors	Responding to the proposal to change the retail modification factors	
1.4 Allocation of totex between opex and capex	Providing an update on the opex and capex split	
1.5 Updated RoRE	Providing an update on our RoRE position	

1.1 Cost of Capital

The WACC plays a central role in the overall balance of risk and return. We very much welcomed the decision in 2017 to set out the early view and have consistently supported the range proposed at that time – one of the few companies to do so. The calculation of the early WACC was an important feature of PR19 because the degree of certainty we assumed it provided as part of the overall "package" helped support the submission of stretching totex and service plans – something that PR19 has achieved like no other previous price review.

Given Ofwat's long track record in setting the WACC and the view, justified at times, that companies overplay the impact of a reduction, we have been reticent in expressing our views on this topic at previous points in the price review process. However in light of the significant reduction put forward in the Draft Determination, accompanied by stretching service improvements and cost efficiencies we now strongly believe that Ofwat has not sufficiently considered the reasonableness of the WACC in the context of the overall package. This is important for the efficient delivery of outcomes that matter to our customers and the environment, including over the longer term. That is, the provision of a fair balance of risk and return is key to supporting stable and low cost financing conditions within which the substantial investments required for outcome improvements can be provided. This has therefore prompted our representation.

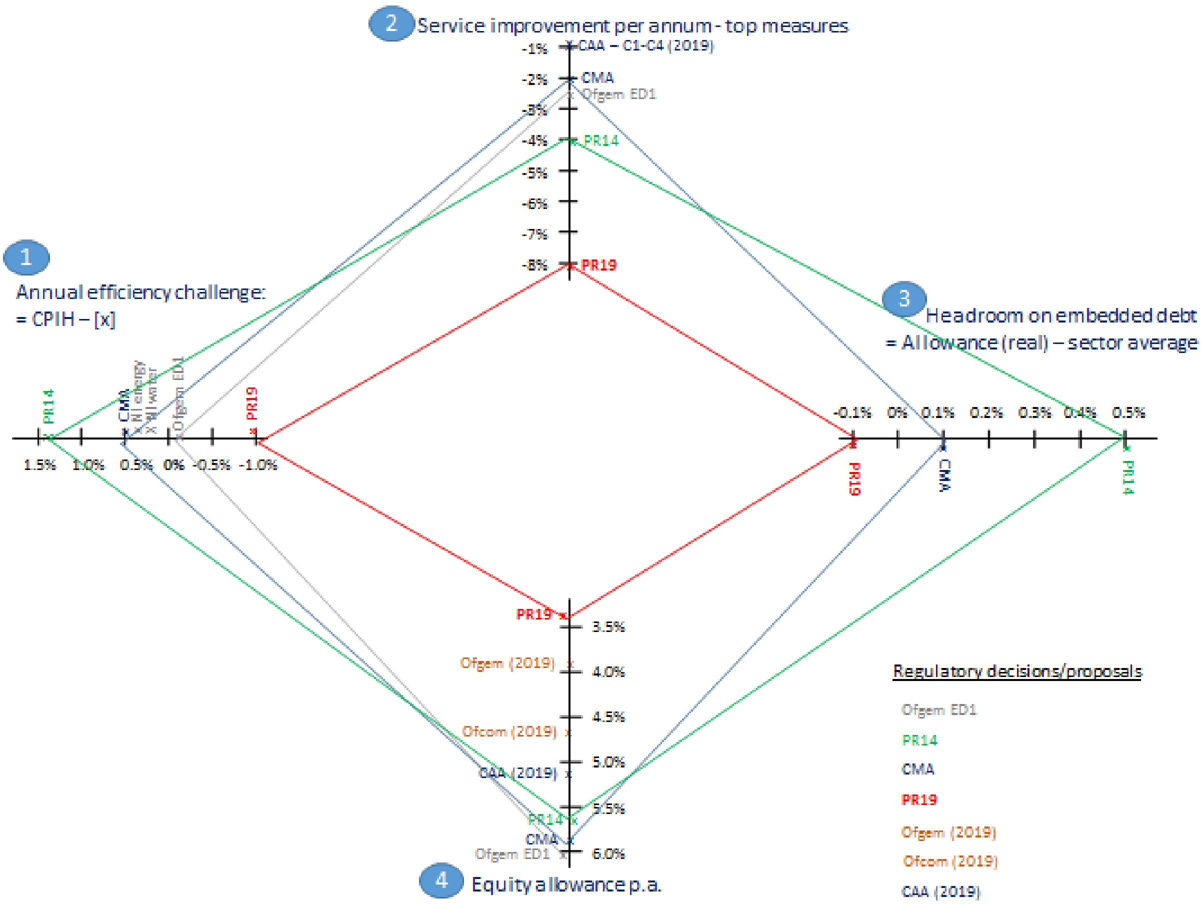
The proposal for a 21 basis point reduction in the WACC, and the suggestion of a further substantial reduction, would – if applied – represent a substantial shift in the balance of risk and return, on both an absolute and relative basis.

We have analysed the overall PR19 DD package against other regulatory decisions1 to assess whether the ask, reflected by the cost and service improvements, is fair given the commensurate return. This is illustrated in the figure below, whereby we have plotted what we consider to be the four primary factors impacting returns: 1 – assumed productivity improvements, 2 – required service improvements, 3 - headroom on the cost of debt (using

[1] This analysis has been carried out for PR14, the CMA decision on Bristol Water, Ofgem RIIO ED-1 and PR19. We have also included more recent regulatory decisions from the CAA and Ofgem.

headroom on embedded debt specifically); and 4 - the allowed (base) cost of equity. In this diagram the more stretching the decision, the closer the line is to the centre.

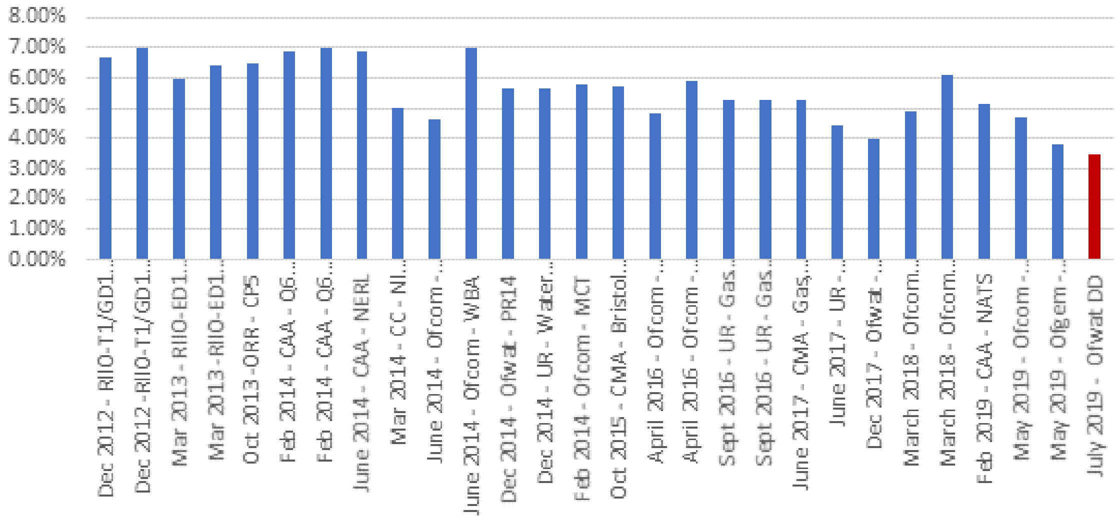
Figure 1 – Assessment of the package in the round



In forming a view on reasonableness, one would expect to see the regulatory decisions intersecting – for example one price review might have set more stretching service improvements but less demanding productivity improvements, and vice versa. However, as is illustrated by the chart, the sum of the PR19 decisions would seem to represent, by a significant margin, the most challenging review in recent history, for the lowest base return on equity. This is evident by:

- the extremely stretching service improvements for the comparative measures, which requires on average an 8% annual improvement (ie, reduction in incidents) otherwise penalties are incurred. This compares to the performance challenge of 2-4% set by the CMA, Ofgem and Ofwat in previous reviews;
- the most demanding productivity improvements compared to any other regulator in recent history, with the improvement being double what the CMA set and applying over and above the UQ efficiency challenge;
- no headroom, indeed a shortfall for the majority of companies on embedded debt , contrasting with PR14 and the CMA decision; and
- the DD proposed approach on beta and the risk free rate, which would result in the allowed cost of equity being lower than at any other time in UK regulatory history, as illustrated below. Only CCWater appears to have argued for a lower figure than in the DD, with the assessments in other consultant's reports, for example Frontier Economics and indeed Ofgem's May 2019 methodology document identifying a higher cost of equity estimate.

Figure 2 - Regulatory assessments of the cost of equity (RPI deflated)



We do not think that the resulting position on the WACC published in the DD is reasonable when viewed in the round. We can understand why, given experience of financing cost out-performance at previous controls, there is such emphasis being put on pressing for a lower WACC. However, the introduction of cost of debt indexation addresses what has been the principle source of past financing cost gains, and – as was highlighted above – the cost of equity proposed in the DD lower is the lowest in UK regulatory history.

We think it critical that the final WACC decision – including any potential changes to the DD proposal that may be considered – forms part of a determination that is reasonable and balanced when viewed in the round. That is, the appropriateness of the levels of stretch in other areas should be considered alongside the final view on the WACC to ensure that consistent and reasonable overall approach is being adopted.

In making this representation, we recognise that some updating of the early view to take account of more recent market information is to be expected. But to maintain strong incentives for business plans (for PR19 and future reviews), it is important to ensure that subsequent changes to the early view of the WACC are balanced, given the subjective nature of many components, consistent with the early view methodology, and made as a component of the package in the round.

The assessment of the WACC in the Draft Determination appears to have been undertaken as a 'fresh' and independent exercise. It does not appear to pay sufficient regard to the "in the round" approach that companies took when developing plans. Across each component within the CAPM framework Ofwat has considered in isolation and anew how each parameter should be assessed, which has led to a number of substantive changes.

There are three changes which we believe should be reconsidered to ensure that the overall package remains stretching but fair. These relate to:

- beta – focused on the timeframe over which the assessment is made;
- the risk free rate – relating to what weighting is given to nominal versus RPI linked gilts; and
- the cost of debt – relating both to the allowance for embedded debt and to what forward looking assumptions about the halo effect are reasonable given the expected credit rating of the notional company.

We consider these points in turn below.

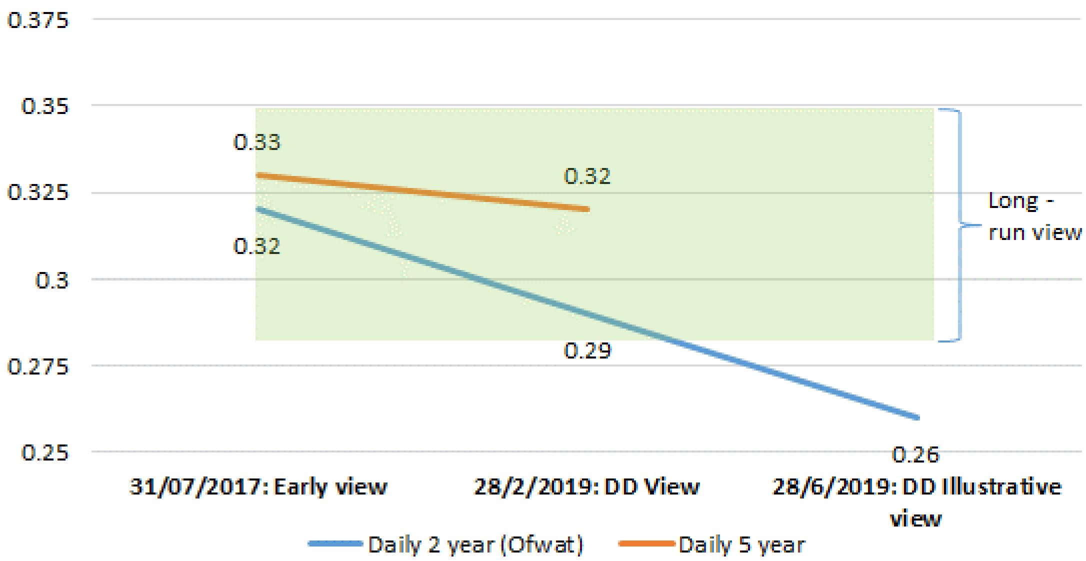
1.1.1 Beta should be derived using a longer-term view consistent with best practice

The estimation of beta is a key input into the cost of equity, to reflect the level of risk faced by investors in the water sector.

When estimating beta one of the most critical issues is the time period over which (listed utility) returns are assessed relative to the FTSE. This is because regulators are quite rightly concerned that temporal factors, such as the price review itself, can affect beta estimation. These factors can result in what is referred to as uninformative volatility. Observers of regulated utilities in the past two years will recognise two prime examples of such sources of volatility - the price review and the Labour policy of re-nationalisation.

In the DD a preference is expressed for using data over two years, on the basis that it captures more recent market evidence whilst mitigating the risk of uninformative volatility. However rather than mitigating this risk, we can observe that the use of the two-year data series makes the risk a reality. This is evident in the chart below, which shows: (i) there is significant volatility in beta using a 2-year data series, notably falling 10% in 4 months (0.29 to 0.26) and c~20% (0.32 to 0.26) since the early view; and (ii) there is significant divergence between the beta calculated using a 2-year data series and more medium and long term data series.

Figure 3 – Ofwat (unlevered) beta estimates



Divergence of the proposed two-year data series from the medium and long term view raises particular concerns. When the early-view WACC was presented, a key feature that supported the reasonableness of using a daily 2-year unlevered beta estimate of 0.32 was that it was broadly in line with the longer term daily 5-year unlevered beta estimate (0.33) and the average of a long-term range. That is not the case for the 28th February view of daily 2 year beta estimate of 0.29, or the 28th June 2019 estimate of 0.26, particularly since this beta would fall outside the long-term range – raising serious concerns of uninformative volatility.

We note that other regulators and academics have considered the measurement issue at length. Of particular relevance are the views of the CMA and the UKRN, both of whom have advocated calculating beta over a longer time period. More recently Ofgem has followed suit – which we highlight below.

In the Northern Ireland energy appeal the CMA initially considered a similar approach to Ofwat, calculating beta using both a 2-year window and a longer term data series (10 year). However the CMA ultimately decided to use the longer term view instead of the 2-year data set on the basis that:

> *Given that beta can vary over time we think that it is right to base our estimate on a relatively long run of data.* [2] **Central Markets Authority, 2014**.

More recently the issue of how to measure beta was considered in the UKRN cost of equity report on behalf of other regulators. Its 2018 report noted that:

[2] CMA, https://assets.publishing.service.gov.uk/media/535a5768ed915d0fdb000003/NIE_Final_determination.pdf

There is 'a quite strong prima facie case to use all available data to estimate, beta, ***not*** *just a relatively short recent sample.'* **UK Regulators Network, 2018**

Recommendation 2 of the UKRN report is also relevant here in that it sets out that the authors of the report are, on balance, in favour of choosing a relatively long time period, for example, 10 years, when estimating the WACC, but that more important than the choice of horizon per se is that all components of the CAPM-WACC are estimated using a methodology that is consistent with that chosen horizon. Furthermore, we note the comment by Burns that the extent of judgement and discretion required for beta estimation "…reinforces the obligation on regulators to examine the evidence as a whole, not rely solely on outlying estimates…" (p53-4). This point is highly relevant in a context where (as shown above) the 2 year beta can be seen to be diverging markedly from longer term estimates.

Finally whilst Ofgem is yet to publish its draft determination, in its Sector Methodology (May 2019) it has set out an expectation that it will not place any material value on using a short term equity beta:

We remain unconvinced that we should place material weight on short-term equity beta results....Our strong view is that the noise to signal ratio is particularly high within short-term results. **Ofgem, 2019.**

We understand the need to take into account more recent market evidence. But given the issues associated with using a short term 2-year data set, we believe the beta is better estimated using the daily 5-year beta. Such an approach would also appear to be more strongly aligned to the views of the UKRN study on beta, the CMA's decisions and other regulatory views.

1.1.2 The risk free rate should be based on nominal gilts, consistent with the early view, not on gilts linked to the discredited RPI index

The PR19 methodology marked an important shift in terms of how the effects of inflation should be taken into account, with Ofwat becoming the first regulator to move away from using RPI. In making the decision to abandon RPI and index prices using CPIH, Ofwat emphasised that the continued use of RPI lacks legitimacy with customers and stakeholders.

The reasons for abandoning RPI have been clearly and extensively set out by Ofwat and others:

UK Statistics Authority (UKSA): *RPI is a flawed statistical measure of inflation … taxes, benefits and regulated prices should not be linked to RPI … government and regulators should work towards ending the use of the RPI as soon as practicable. (January 2015)*

Ofwat: *RPI is losing its legitimacy: it is statistically flawed, is discredited and has been discontinued as a national statistic (May 2016).*

Office National Statistics: *Our position on the RPI is clear: we do not think it is a good measure of inflation and discourage its use (May 2019).*

Ofwat's assessment of the risk-free rate in December 2017 was consistent with this position. Evidence on RPI-linked gilt yields was not used, and instead the assessment was based on nominal gilt yields. This ensured consistency across the different aspects of the price review and enhanced the legitimacy of the PR19 framework.

For the DDs, however, Ofwat chose to depart from this approach when calculating the risk free rate, by using gilts linked to the discredited RPI, as illustrated below.

Table 1 - Weighting placed on nominal v RPI gilts

	Gilt Weighting	
	Early view	DD
Nominal 10 yr gilts	50%	0%
Nominal 20 yr gilts	50%	0%
RPI-linked 10-year gilts	0%	50%
RPI-linked 20 year gilts	0%	50%

This reliance on RPI gilts is also contrary to the views of Ofwat's own cost of capital advisers, Europe Economics, who noted that: As RPI diverges more and more from CPIH and does so in ways that have not been stable over time (as was discussed at length in our 2017 report), the case for placing sole reliance upon RPI-linked gilts as versus nominal gilts, has become weaker.

In practice, the case for not using evidence from RPI-linked gilts is even stronger than that presented by EE, because the extent of RPI's flaws can also be expected to generate risks over how indexation will actually be applied to existing RPI-linked gilts in the future. It is notable in this respect that the House of Lords Economic Affairs Committee January 2019 report 'Measuring Inflation'[3] expressed major concerns over the continued use of RPI to index existing index-linked gilts. The report recommended that the government decide whether RPI should continue to be published in its existing form for the purposes of existing RPI-linked gilts, or whether a process of adjustments should be made to RPI so that it converges with the single general measure (i.e. CPI or CPIH).

The case for moving away from RPI has been well made by different experts across the field – including the ONS, the Bank of England, the House of Lords and Ofwat itself. We think it important to the credibility of the regulatory framework that the methodology decision to stop using RPI is upheld, as was done in the early view WACC. This would ensure consistency across different aspects of the regulatory building blocks. For this reason our strongly held view is that the estimate of the risk-free rate should be based on nominal gilt yields – as proposed in the early view – and not based on gilts linked to the discredited RPI index.

1.1.3 The allowance for embedded debt is insufficient to fund our efficiently incurred costs, and assumed levels of future debt out-performance are not consistent with Ofwat's own assessment of credit ratings

Despite no material new information having become available with respect to embedded debt costs, the DD proposes a substantial reduction in the allowance relative to the early view (of 4.65%). This results in a nominal allowance (4.50%) that is lower than the cost of debt incurred by the average going into AMP7. While, given our expected embedded debt costs for PR19 (5.9%), we expected to earn a loss on embedded debt, the increased scale of that loss raises concerns over the reasonableness of the overall balance of risk and return that we face. In particular, we struggle to understand the case for putting so much less weight on WoC debt costs in the DD proposals – compared with early view and indeed PR14 and previous reviews – particularly in the absence of some form of countervailing changes that reflect the higher levels of embedded debt costs that WoC's typically face, and are 'locked-in' to.

Ofwat's proposals assume that new debt will be funded in line with the average of A/BBB non-financials (with a tenor of 10 year or more), less a deduction to reflect a 'halo effect' that water companies have when raising debt. The DD proposes that – based on further review of historical evidence - the halo effect should be increased from 15 basis points (as assumed in the early view) to 25 basis points. We do not believe the historic evidence on out-performance provides a reliable basis for the proposed increase in the 'halo effect' given the extent of pressures on company credit ratings, and believe the assumed level of out-performance should be kept consistent with the early view of the WACC, which already included a significant level of stretch.

[3] https://publications.parliament.uk/pa/ld201719/ldselect/ldeconaf/246/246.pdf

1.1.4 Conclusion

Our view has always been, and remains, that the DD and FD should be judged in the round – taking into account the totex, service challenges alongside the level of returns allowed for investors. To this end we have been reticent to engage in debates about how specific components that form the WACC should be calculated.

However, with the proposal for a lower WACC having been received after the fast track companies' DD, it is now apparent that the current position no longer represents a fair and reasonable package when viewed in the round. We are therefore making a small number of representations aimed at improving the balance of the position:

- Beta – use 5 year daily data to address the evident problems with the reliability of recent 2 year data, which would bring Ofwat more in line with CMA and other regulatory views
- Risk free rate – avoid using RPI gilts to estimate the risk free rate, and use nominal gilts to, consistent with the original PR19 methodology and wider expert views discrediting RPI.
- Debt – reconsider the proposed reduction to the allowance for embedded debt (by putting more weight on WoC embedded costs in line with the early view and previous reviews), and the proposed increase in the 'halo effect' given the challenges facing the notional company that cast significant doubt on companies' ability to outperform at historical levels.

Such adjustments would still ensure that the regulatory settlement at PR19 would be extremely stretching both in absolute and in relative UK terms, but would be more reasonable and better aligned to other regulatory and Government policy.

1.2 Financeability

At the appointee level, Ofwat's draft determination delivers a financeable plan under the actual and notional structure, which supports our target to maintain BBB+/Baa1 credit rating for AMP7.

The appointee financial ratios remain largely consistent with the ratios in our September plan submission and April response to the IAP.

1.2.1 Draft determination financeability

We have also reviewed the financeability of the individual controls in assessing whether the draft determination is financeable. As highlighted in the draft determination, the financial ratios for the wastewater network and bio resources controls remain weak and not financeable in their own right. Whilst the ratios for the water resources and water network controls are financeable, Moody's AICR and gearing (for water network) falls to a level one notch below our target rating of Baa1. We consider that it is important that the water controls should have sufficient financial headroom to support the wholesale entity, particularly as the wastewater controls are not independently financeable.

Water controls financial ratios – notional structure before reconciliation adjustments

	Water resources	Water network
Gearing	57.3%	**73.7%**
AICR	1.50	1.85
FFO / net debt	13.3%	10.8%
AICR (Moody's alternative)	**1.42**	**1.40**
FFO / net debt (S&P alternative)	12.1%	10.4%

We have also assessed the financial ratios for the actual company, which includes the impact of the PR14 reconciliations adjustments. Compared to the notional company the ratios are slightly stronger on an appointee basis and above the levels required to maintain a BBB+ / Baa1 rating.

1.2.2 Further reduction in the WACC

In the slow track draft determinations, it was noted that a further 37bps reduction in the WACC may be appropriate. We strongly disagree with this position and as noted in our response, believe the existing 21 basis point reduction is not supported by evidence – particularly in relation to beta and the risk free rate.

In this section, we have considered the impact of the proposed 37bps WACC reduction on the financeability of both the notional and actual company structures.

Financial ratios – notional structure before reconciliation adjustments

	Water resources	Water network	Appointee
Gearing	58.0%	**74.1%**	64.9%
AICR	**1.35**	1.78	1.63
FFO / net debt	12.6%	10.4%	11.5%
AICR (Moody's alternative)	**1.27**	**1.30**	1.63
FFO / net debt (S&P alternative)	11.4%	10.0%	10.7%

As Hafren Dyfrdwy has a relatively small opening RCV coupled with high RCV growth of 39.4% over the period, the lower WACC will have a moderate impact on the appointee ratios on average over the 5 years. The

Moody's AICR would however, deteriorate to only one notch above sub investment grade in the latter years of the period.

At a price control level, the two water controls would have ratios consistent with an investment grade credit rating, albeit at the lowest possible level for Moody's. We also note that at a wholesale level (combining water and waste) as shown below, we would be sub-investment grade on the Moody's AICR. S&P's FFO/net debt would also fall by one notch to BBB.

Wholesale financial ratios – notional structure before reconciliation adjustments

	5 year average
Gearing	66.5%
AICR	**1.18**
AICR (Moody's alternative)	**1.05**
FFO / net debt	9.6%
FFO / net debt (S&P alternative)	**8.9%**

We consider that with the wastewater controls not independently financeable and with revenue constrained to keep bills relatively stable over the period, the water controls should have sufficient financial headroom to ensure the ratios are investment grade at the appointee wholesale level. Two notches above sub investment grade would be an appropriate level of headroom to cover the uncertainty of outturn cashflows and remain investment grade over the period. An increase in the RCV run off rates would be required for both water controls in the event of such a material WACC reduction, to bring up the AICR to a level consistent with minimum investment grade.

We have also assessed the lower WACC on the actual company after adjusting for PR14 reconciliations. As with the draft determination, the actual company ratios are slightly stronger than the notional company on an appointee basis. The ratios would remain above the levels required for a BBB+ / Baa1 rating.

1.2.3 Board Assurance

We shared with the Board the forecasted financials resulting from the draft determination alongside the credit ratios and financeability assessment for both the actual and notional company structures. The Board reviewed and provided challenge as necessary, particularly on the impact of a further WACC reduction on the long-term resilience of the actual company.

The Board is satisfied that the draft determination would be financeable at the appointee level for both the notional and actual financing company and has made a statement (see Appendix A) which is included as part of this submission. The Board statement also covers the impact of the potential 37bps WACC reduction on financeability.

1.2.4 Jacobs Assurance

We also instructed Jacobs to carry out assurance on the;

- the key assumptions underpinning our Board's decisions on credit quality in response to the lower WACC assumed in Ofwat's Draft Determination; and the potential for a further reduction to the WACC at Final Determination;
- the financial model outputs and our interpretation of their implications for credit quality; and
- the narrative included in our representation on risk and return

Jacobs overall findings:

The Draft Determination (namely the reduction to the WACC of 21 basis points) results in financial ratios, at the appointee level, consistent with your target credit rating of BBB+/Baa1 credit rating for AMP7under both Ofwat's notional and your actual structure.

Ofwat has indicated in the Draft Determination the potential for a further 37 basis points reduction in the WACC for the Final Determination. You have stress tested the impact of this lower WACC. We note that this assumption produces a profile of declining ratios (eg the Adjusted Interest Cover Ratio in the latter years of the period would deteriorate to levels consistent with a credit rating of Baa2). The impact on the appointee's AMP7 average financial ratios is moderate.

We consider your narrative is consistent with your modelling assumptions and the subsequent outputs from that modelling. Your assumptions align with your agreed policy decisions. We understand that these assumptions have been fully discussed at Hafren Dyfrdwy Board.

1.3 Retail modification factors

In the DD, Ofwat made an intervention to alter our retail modification factors, resulting in a reduction in the revenue requirement. This would technically breach our licence, since the revenue requirement is enshrined by the PR14 Final Determination.

The retail modification factors were part of our PR14 Determination. The household retail control was set as a fixed amount of revenue per year, modified for any difference in customer numbers. An amount of additional revenue for customers of each type was part of the Determination, and was written into the company licence.

The intervention was described in the Past Delivery actions and interventions appendix (HDD.PD.C008.01a and HDD.PD.C008.01b), which has the effect of:

- replacing the separate retail modification factors for Dee Valley and Severn Trent with a weighted average for each type of water customer; and
- allowing less revenue than would have been calculated if the adjustment factors had remained at their original rates.

While the overall effect of this change is relatively small (£0.02m), the retail modification factors are part of the determination, and part of the licence. After the border variation, the licences of Severn Trent and Dee Valley were updated to reflect the separate modification factors that should apply in areas formerly served by each of the legacy companies. This is laid out in the updated table 4 of Condition B.21, which Ofwat published on its website. This means we have multiple retail modification factors – unlike every other company.

While our original calculation of the retail adjustment in our PR19 Business Plan did not fit into Ofwat's standard model, this is a consequence of the licence variation and subsequent Determination of multiple retail modification factors. This was done to ensure every customer was in the same position, as they would have been if the border variation did not take place.

Accordingly, under the terms of our licence we have to comply with all of the relevant modification factors. In our Business Plan the calculation satisfies this requirement and ensures that all customers are in the same position as they would have been if the border variation had not taken place.

The decision being applied in the DD does not satisfy that principle. It would change the retail modification factors and the resulting revenue allowance for AMP6. This would breach our licence. Charges for 2019-20 have already been set to recover revenues based on the PR14 Final Determination, and the DD decision would effectively change that determination.

<u>From a position of principle, we do not consider it appropriate to change the retail modification factors in a way that deviates from the PR14 Final Determination and the licence, particularly after charges have been set.</u>

1.4 Allocation of totex between opex and capex

Stephen St Pier's letter of 23rd August included an additional request for companies to confirm the split of wholesale totex between opex and capex. As per our plan and Ofwat's draft determination, we consider the AMP7 opex and capex split should be as follows:

Proportion of totex	Water resources	Water network	Wastewater network	Bio resources
Opex	65.10%	67.58%	56.07%	100.00%
Capex	34.90%	32.42%	43.93%	0.00%

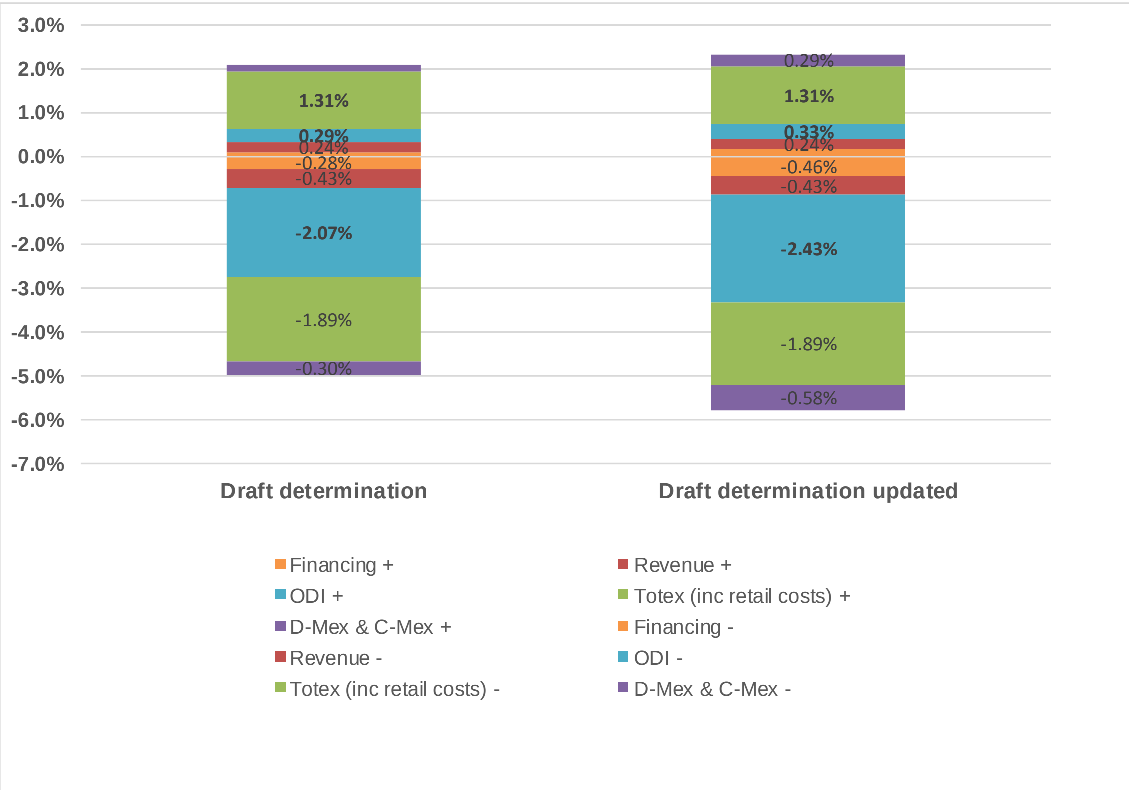
1.5 RoRE

We have updated table App26 in line with our response to the draft determination, including the ODI related changes set out in our response for:

- revised penalty rates for pollution, leakage, supply interruptions and low pressure;
- implementing a revised penalty collar for water supply interruptions;
- C-MeX; and
- Financing performance.

Our DD response has widened the RoRE range from +2.09% to -4.79% in Ofwat's draft determination to +2.33% to -5.78%. We discuss the changes in detail below.

RoRE range and its components



The outcomes section of our representation explains further the changes mentioned above for pollution incidents, leakage, low pressure and water supply interruptions. While the DD had estimated that the ODI range would be +0.29% to -2.07%, our proposed changes to the penalty rates, collars and deadbands indicates that the

RoRE range on ODI’s would now be slightly wider at 0.33% to -2.43%. Compared with the estimated range published in the DD, the downside is now 0.36% higher and the upside 0.04% higher.

On CMeX, we have revised the assumptions used in our plan to align the P10/P90 performance levels to the full amounts at which the standard reward/penalty would apply. The change results in a wider C-Mex RoRE range of +0.33% to -0.58%.

Financing performance has also been updated for the changes in the cost of debt assumptions used by Ofwat in the draft determination. With the ex-ante level of outperformance now assumed to be 25bps, we think the potential range of performance against the iBoxx could now be up to 50bps on both the upside and downside. As assumed in our plan, we consider the potential range of performance is around double the average of the ex-ante outperformance that Ofwat has observed from historical industry performance relative to the index. With Ofwat adjusting for the ex-ante level of outperformance up front, the potential upside reduces to 25bps and the downside remains at 50bps. The change results in a marginally wider financing RoRE range of +0.15% to -0.46%.

As part of our response, we have updated the draft determination financial model with the above changes.

Appendix A

Board statement

As a Board we want to deliver the best outcome for our customers. Critical to this outcome is ensuring we have stable and low cost financing conditions within which the substantial investments required for outcome improvements can be provided

We have reviewed the outcome of the Draft Determination and can confirm that our updated business plan for 2020-25 is financeable for that period on both the notional and actual capital structure under the Draft Determination WACC of 5.25% (nominal) and totex allowance of £163m. We have tested the financeability of our plan under a 37bp lower WACC scenario and the plan would also be financeable at an appointee level.

Signed

John Coghlan on behalf of the Hafren Dyfrdwy Board

Non-Executive Chairman