United Utilities

PR24 Business Plan

Investor Summary

October 2023

United Utilities

Water for the North West

Investor Summary

Our plan for 2025-30 is all about ensuring that we provide great water that makes the North West stronger, greener and healthier.

Operational highlights

- **A plan developed using a unique five counties, regional approach**
- **74% customer acceptability for our proposed plan**
- **Our plan reflects an approximate £22 real increase in bills every year, on average, across AMP8**
- **Our largest ever package of affordability support at £525 million to help more than 1 in 6 customers**
- **An ambitious plan to deliver our best ever service levels**

Financial highlights

- **Ambitious £13.7 billion totex programme, including £197m accelerated delivery programme and £107m transitional investment**
- **Driving around 14% efficiency into our plan using innovation, optimisation, robust cost challenge and effective use of markets**
- **RCV growth of 52% nominal across the AMP, resulting in RCV of £22.4 billion in FY30**
- **Plan submission adopts Ofwat's early view WACC consistent with Final Methodology**
- **Flexible financing options as plan is finalised over the month ahead**
- **Strong balance sheet, with 58% gearing at Mar-23, provides options for funding the capital requirement**
- **Based on Ofwat's WACC assumptions, and without assuming new equity, we would expect gearing to average 65% over AMP8**
- **Proposing a notional company RoRE incentives range of -6.3% to +4.4%**
- **Dividend policy expected to be announced following Final Determination**

Key Financials

£m (2022/23 prices)	2025-26	2026-27	2027-28	2028-29	2029-30
PAYG (operating costs and IRE)	854.4	885.1	904.8	918.8	946.2
RCV run-off	599.3	622.5	652.5	687.7	725.8
Return on capital	443.6	474.1	517.6	563.2	586.9
Revenue adjustments for PR19 reconciliations	71.4	71.4	71.4	71.4	71.4
Residential retail costs (nominal)	119.9	118.4	116.4	115.7	114.9
Retail margin – residential (nominal)	14.8	15.6	16.1	16.7	17.7
Retail revenue adjustments for PR19 reconciliations	13.2	13.3	13.3	13.3	13.3
Tax	-	46.7	25.3	16.5	26.1
Other adjustments	79.6	85.2	90.8	90.2	90.4
Allowed revenue	**2,196.2**	**2,332.2**	**2,408.2**	**2,493.6**	**2,592.8**

£m (2022/23 prices)	2025-26	2026-27	2027-28	2028-29	2029-30
K factor	10.5%	6.5%	3.4%	3.5%	4.0%
Average household bill (£)	481.11	506.29	515.81	530.96	556.17
Capital expenditure and RCV					
Capital expenditure	**1,371.5**	**1,779.3**	**2,243.1**	**1,962.1**	**929.9**
RCV – year-end (nominal)	**15,899.4**	**17,543.9**	**19,767.4**	**21,676.8**	**22,354.5**

Five counties approach

We know our region and the people that live, work and visit here. The towns, cities and beautiful landscapes of the North West are places we're proud to serve. We have built plans that deliver for the people and environment of each of the five counties of Cumbria, Lancashire, Cheshire, Greater Manchester and Merseyside.

Up and down the region we have been engaging with customers and stakeholders to understand what is important to them, in the place they live and work. There are different social and environmental conditions across the region, a place that has both some of the most remote and rural communities in England to some of its greatest cities. We are investing in new capabilities and structuring our operations so that we will deliver our plans and communicate our performance on a local basis, providing more transparency and insight about our service than ever before.

Customer acceptability

Our engagement approach has delivered deep levels of insight, supported by exceptionally high quality research. We have recognised customer priorities about what we should deliver and how we should deliver it. We have consulted with all customer groups – including vulnerable customers, hard to reach customers, households and businesses. Based on rigorous research studies across all groups, we are confident that 74% of customers support our proposed plan.

Customer Bills and Affordability Support

Our business plan will deliver services that customers value and we have taken robust action to ensure the lowest possible bills for customers. However, given the anticipated material bill increases, our customer engagement shows that many customers are understandably concerned about affordability challenges. To address this we plan to provide an unprecedented £525m of affordability support to those in need, including making direct financial contributions worth £200m.

We are not proposing to advance any revenue, either through RCV run-off (which we have aligned with the natural rates) or PAYG and are apportioning our carry forward adjustments between RCV and revenues in line with Ofwat's proposed PR19 reconciliation mechanisms, which bolsters financeability on an actual company basis.

We have used Ofwat's financial model to calculate expected bill levels, which are summarised in the table below.

Household customer bills (2022/23 prices)	2025-26	2026-27	2027-28	2028-29	2029-30
Wholesale revenues (£m)	1,965.34	2,096.16	2,168.09	2,267.57	2,410.08
Retail apportionment[(1)]	70.88%	70.93%	70.80%	70.64%	70.59%
Household customers ('000s)[(2)]	3,195	3,220	3,251	3,285	3,315
Average wholesale bill (£)	435.97	461.69	472.08	487.65	513.21
Average retail bill (£)	45.14	44.60	43.73	43.31	42.96
Average household bill (£)	**481.11**	**506.29**	**515.81**	**530.96**	**556.17**

Household customer bills (2022/23 prices)	2025-26	2026-27	2027-28	2028-29	2029-30
Average household bill, 2024/25 (£)	446.71	-	-	-	-
Change in bills, 2024/25 to 2029/30	**24.5%**	**-**	**-**	**-**	**-**

Business Plan Submission, Chapter 9, Table 9-5.

The average household bill across the five year period includes £3.17 related to the recovery from customers of the Competitively Appointed Partner (CAP) payments in 2025/26-2029/30, predominantly relating to DPC Haweswater Aqueduct Resilience Project (HARP).

Although a clear majority of customers support the proposed plan, we recognise that any increase in bills can mean that there are affordability challenges for some households. This is particularly the case when utility and council tax bills are rising during the ongoing cost of living crisis. Responding to this, we are proposing to put in place our largest ever package of affordability support. No one should worry about being unable to pay their water bill. Our proposal is to deliver an unprecedented package of over half a billion pounds of affordability support – some £525m – to help customers who might otherwise struggle to pay their bill. Based on our plan, this will include a £200m contribution from our investors which, as in AMP7, will be given precedence over any dividend payment. We expect the support package to help around 590,000 customers - more than twice as many as today - and meaning that 1 in 6 households will receive some form of financial support.

Outcome Delivery Incentives (ODIs)

Our overall service package provides ambitious levels of service at excellent value for money, demonstrating ambition in our service improvements whilst being mindful of cost pressures on customers and pace of delivery over AMP8 and the long term.

We are building on a strong track record of performance in AMP7 having delivered one of the stronger performances in the sector. We are targeting stretching performance levels based on historical performance and historical targets across the industry, in line with Ofwat's final methodology expectations.

Service improvements proposed include:

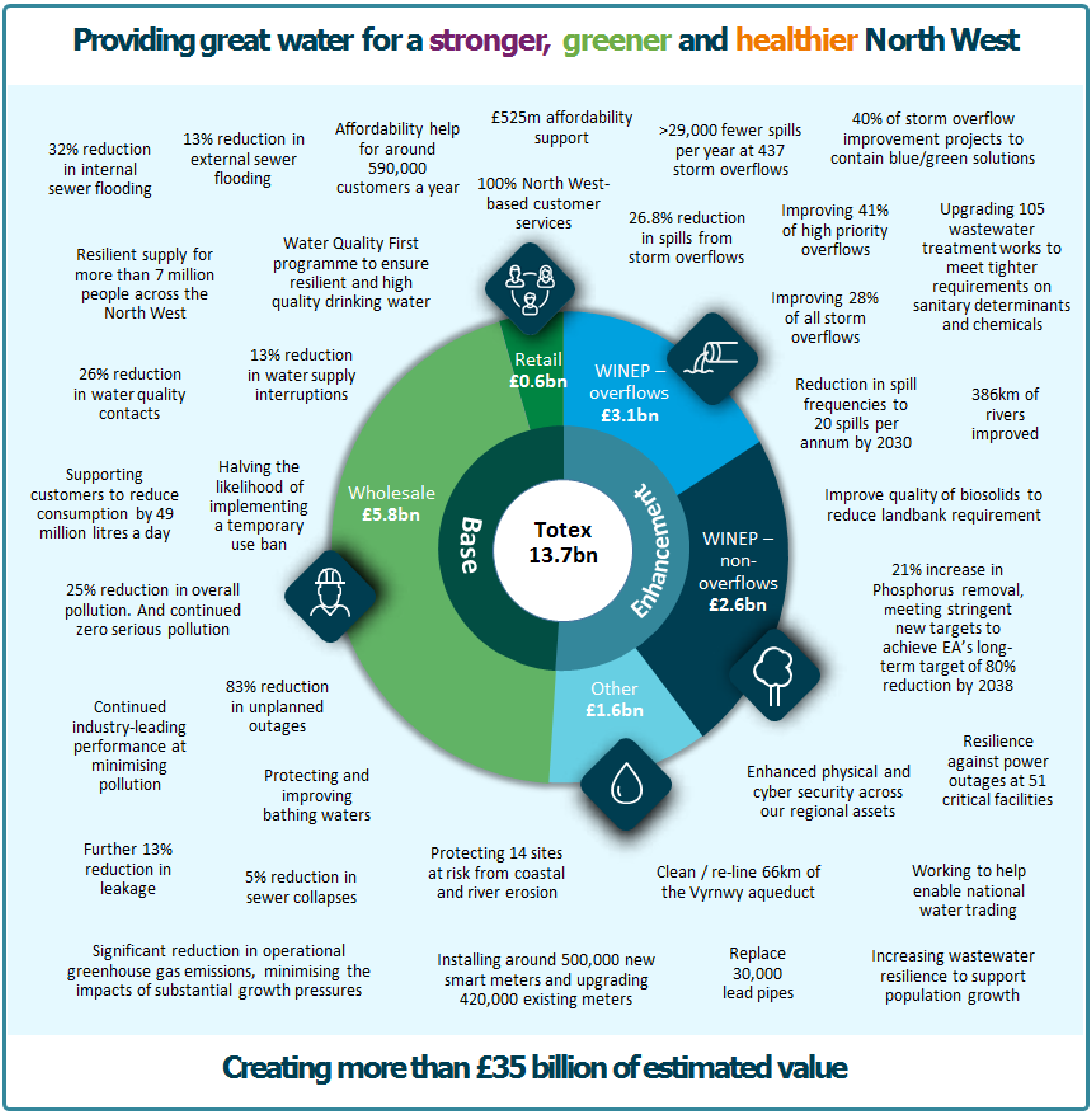
- **26.8% reduction in storm overflow spills during AMP8,** reflecting a 60% reduction over the decade to 2030
- A target of **zero serious pollutions** and a 25% improvement in performance on all pollution incidents by 2030
- **13% improvement in water supply interruptions,** representing an upper quartile level of performance
- **13% improvement in leakage performance,** in line with a 50% targeted reduction in leakage by 2050
- **32% fewer internal sewer flooding incidents and 13% fewer external sewer flooding incidents** by 2030
- **26% reduction in the number of water quality contacts received from customers** regarding the taste, smell or appearance of drinking water.

Within the package we have also included three bespoke performance commitments that we believe respond to particular needs of the region, based on enhancing the water environment at Windermere, improving water bill affordability for socially important non-household groups and a performance commitment focussed on reducing embodied greenhouse gases.
See Business Plan Submission, Chapter 5 for further details

Totex

We are committed to providing the best value for money for customers. This means improving performance, delivering on our legal and regulatory obligations and the key priorities of customers, and strengthening the long-term resilience of our services, all at the most efficient cost, making best use of innovation and markets to deliver service improvements and new obligations in a way that secures best value for customers and the environment.

Our £13.7 billion proposed total AMP8 expenditure (totex) is estimated to deliver more than £35 billion[1] of added value for the North West and support more than 30,000 jobs.



[1] Based on third party analysis from Arup: supplementary document *UUW36 – Total Value of the plan*

Total expenditure (post-efficiency and real price effects) split by price control

£m (FY23 prices)	Water resources	Water network +	Wastewater network +	Bio-resources	Wholesale	Retail	Total
Base costs	412	2,281	2,164	476	**5,332**	585	**5,917**
Cost adjustments	186	-	85	173	**444**	-	**444**
Base totex	**598**	**2,281**	**2,249**	**648**	**5,777**	**585**	**6,362**
WINEP – overflows	-	-	3,089	-	**3,089**	-	**3,089**
WINEP – other	105	-	2,305	195	**2,606**	-	**2,606**
DWI obligations	-	379	-	-	**379**	-	**379**
WRMP interventions	77	405	-	-	**482**	-	**482**
DWMP interventions	-	-	306	-	**306**	-	**306**
Other key priorities	1	54	259	135	**450**	-	**450**
Enhancement totex	**184**	**838**	**5,959**	**331**	**7,311**	**-**	**7,311**
Totex (net)	**782**	**3,119**	**8,208**	**979**	**13,088**	**585**	**13,673**

Business Plan Submission, Chapter 8, Table 8-2.

Creating the best value plan

We are acutely aware of the imperative to spend customers' money wisely, particularly given the scale of the investment required to meet new obligations in AMP8 and beyond. We have used internal and external challenge and insight to drive ambitious levels of efficiency into our plan at every step to ensure we are achieving the best value for money. Targeted cost reductions are summarised in the table below.

Efficient cost reductions included in our plan

£m (FY23 prices)	AMP7	AMP8 Base	Enhancement	Total
Additional efficiencies identified and applied in AMP7	411			411
Robust challenge of need, scale and phasing			1,581	1,581
Innovation and optimisation of solutions		333	830	1,163
Robust cost challenge and use of markets		375	376	751
Household retail efficiencies		24		24
Partnership funding contribution			95	95
Efficient cost reductions embedded into our plan	**411**	**732**	**2,882**	**4,025**

Business Plan Submission, Chapter 8, Table 8-3.

Our AMP8 enhancement programme

Our £7.3 billion enhancement programme represents the largest ever multi-AMP environmental improvement programme, delivering substantial benefits for the North West. 93% of enhancement totex is to meet regulatory and legislative drivers, including our AMP8 WINEP (which accounts for 78% of the programme), obligations from the Environment Agency (EA) and Drinking Water Inspectorate (DWI) outside the scope of the WINEP, and other interventions to meet the statutory obligations under our Water Resources Management Plan (WRMP) and Drainage and Wastewater Management Plan (DWMP).

Enhancement expenditure

Enhancement expenditure	Pre efficiency £m	Post efficiency £m
Overflows reduction plan and Advanced WINEP	3,157	3,089
Total WINEP obligations – storm overflows	**3,157**	**3,089**
Final effluent	966	945
Davyhulme	805	784
Wigan/Skelmersdale	353	344
Investigations	67	66
Flow monitoring and Event Duration Monitors	168	164
Sewage sludge drivers	173	170
DPC Management	28	27
Water resources	108	105
Total WINEP obligations – other	**2,668**	**2,606**
Vyrnwy re-lining in AMP8	154	151
Lead replacement	92	90
SEMD and NIS-D	62	61
Raw water quality deterioration	43	42
Total Non-WINEP obligations from EA and DWI	**351**	**344**
Smart metering	246	241
Leakage	148	144
Water trading	79	77
Water efficiency	21	20
Total Interventions to deliver our WRMP	**482**	**482**
Rainwater management	136	132
Wastewater supply and demand	140	137
Coastal and river erosion	29	29
Total Interventions to deliver our DWMP	**306**	**298**
Carbon Net zero	200	196
Sewer flooding	142	139
Power resilience	21	20
HARP DPC management costs	25	25
Wastewater reservoirs Phase 1	20	19
Green recovery	24	24
Improving resilience in biosolids recycling to agriculture	55	54
Bioresources preparatory work for alternative outlets	11	10
First time sewerage	5	5
Total Other key priorities	**503**	**493**
Total Enhancement expenditure	**7,478**	**7,311**

Business Plan Submission, Chapter 8, Table 8-8.

Long-term adaptive planning

The future holds unprecedented change with climate change, population growth, advances in technology, and evolving national and regional needs including the levelling up agenda and its aim to promote a growing North West economy. This creates challenges and opportunities. In order to respond to these changes, we have embraced adaptive planning in our long-term delivery strategy (LTDS).

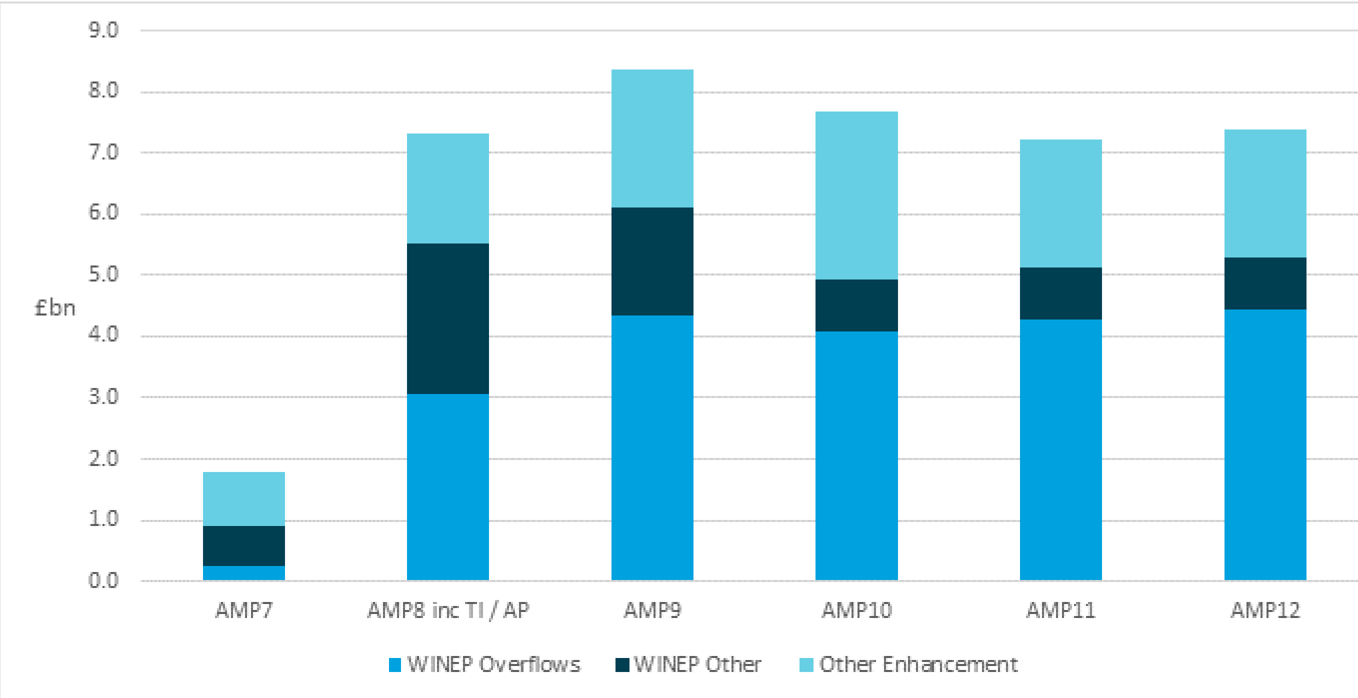
By building our plan for the next five years in the context of the longer term, we have been able to better understand the top priorities that require investment now, identify areas where preparatory work is essential to mitigate future risks, and find opportunities to phase investment until the requirement is more certain to minimise uncertainty and obsolescence risk and to maximise value for money.

Where possible we are making use of phasing and adaptive planning to ensure we meet statutory requirements in a way that balances costs across the AMPs and prioritises delivery of least, low, or no-regret measures first. We developed our AMP8 WINEP proposal within the long-term context to ensure that our plan is balancing investment across the AMPs and intervening at the most appropriate time. We have proposed phasing of schemes in the AMP8 WINEP, particularly where the outcomes of upstream investment may alter the solution needed downstream, or investigations are required to reduce uncertainty around decisions.

When looking to phase investment it is helpful to understand the level of expenditure likely to be required in future periods. We have estimated our planned expenditure for future periods out to 2050 (the end of AMP12) to deliver our ambitions across each wholesale price control. There is a core pathway, shown below, which we would expect to follow under most future scenarios, as well as a number of alternative pathways we may need to follow under different future scenarios (such as adverse climate change).

For the purposes of comparison, we have made a broad assumption that a similar level of efficiencies will be delivered in future periods as that identified for AMP8, though looking so far ahead we do not yet know if this will be possible or how it will be achieved. This shows that overall totex needs are expected to remain significantly higher than AMP7 out to at least 2050.

Long-term cost expectations for AMP9 and beyond following our core pathway



Business Plan Submission, Supplementary document, UUW12 - Long-term delivery strategy

RCV

£m	Opening RCV	2025-26	2026-27	2027-28	2028-29	2029-30
RCV (nominal)	**14,746**	**15,899.4**	**17,543.9**	**19,767.4**	**21,676.8**	**22,354.5**

Opening RCV / Midnight Adjustments

Boosted by our strong expected ODI performance over the last two years of the current AMP, alongside additional reinvestment and accelerated environmental spend to drive further environmental and customer benefits, we are expecting a carried forward value of c.£1 billion as at March 2025. The split between RCV and revenues (in accordance with Ofwat's regulatory true-up mechanisms) is broken down in the below table.

Carried forward value – RCV or Revenues (2022-23 FYA) (£m)

Carried forward value – RCV or Revenues (2022-23 FYA) (£million)	RCV	Revenues[1]	Total carried forward
Totex (customer share)	148.4	227.1	**375.6**
Defra accelerated programme	201.4	-	**201.4**
Additional tax allowance	-	(156.7)	**(156.7)**
ODI rewards	-	134.4	**134.4**
Transitional investment	104.2	-	**104.2**
Developer connections true-up	-	96.9	**96.9**
WINEP / NEP adjustments	91.9	-	**91.9**
RPI/CPI wedge true-up	-	61.6	**61.6**
Debt Indexation Mechanism (DIM)		57.2	**57.2**
PR14 Blind year adjustments	43.7	(0.3)	**43.4**
Green Recovery adjustments	24.0	0.8	**24.8**
Retail revenue reconciliation	-	14.9	**14.9**
Strategic regional water resources	(2.2)	(6.9)	**(9.0)**
Land sales	(8.1)	-	**(8.1)**
C-MeX	-	5.2	**5.2**
D-Mex	-	2.5	**2.5**
Total	**603.4**	**436.7**	**1,040.1**

[1]*Revenues shown pre-tax adjustments.*

Business Plan Submission, Chapter 9, Table 9-6.

WACC

For our plan submission we have adopted Ofwat's 'early view' WACC provided in the final methodology. We recognise that the WACC will need to be updated at the final determinations taking account of the latest available market evidence. It is widely acknowledged that the WACC for PR24 will be higher than at PR19, driven by the step-change in interest rates and the macro-economic environment observed since the start of 2022 that has continued during 2023, which inevitably results in a higher cost of capital for both debt and equity.

When Ofwat makes its final determinations on the WACC, we expect this this to be a fair and balanced position reflecting not only quantitative matters but also considering the vital qualitative components. These include the significant capital investment needs for the sector and investor choices around deploying their capital in assessing a global opportunity set (with many competing demands such as the renewal of infrastructure in response to climate change and pathways to net zero.)

As part of our consideration of the proposed WACC guidance/methodology, we commissioned Frontier Economics to set out their view of the cost of capital using a 30 June 2022 data cut-off for an initial report and a 30 April 2023 cut-off for an update report.

Ofwat PR19 and PR24 early view cost of capital and Frontier Economics view

	Ofwat PR19 (Dec-19)	Ofwat 'early view' PR24 (Sep-22)	Frontier Economics* (Apr-23)	
			Low	High
Gearing	60%	55%	55%	55%
Risk-free Rate	-1.39%	0.47%	1.23%	1.95%
Equity Beta	0.71	0.58 – 0.64	0.60	0.64
Cost of Equity	**4.19%**	**4.14%**	**4.44%**	**5.32%**
Cost of Debt	2.14%	2.60%	2.68%	2.79%
WACC	**2.96%**	**3.29%**	**3.47%**	**3.93%**

*Translated to 55% gearing

Business Plan Submission, Chapter 9, Table 9-2.

Financing the plan

We approach the plan from a robust position, with one of the lowest gearing levels in the sector at 58% today. This uniquely positions us to tackle the challenge of delivering and funding our investment programme in AMP8 and beyond, and what is clear is that we have options and flexibility around funding this capital requirement.

In order to align with the Ofwat methodology, our PR24 submission assumes that the programme is funded with equity and debt, with equity sized to maintain our current A3 rating with Moody's /A- senior unsecured debt rating with Fitch. Recognising that Ofwat will be updating their WACC assumption for draft determinations next summer, we have adopted Ofwat's 'early view' cost of capital in our business plan submission. On this regulatory basis, our PR24 submission assumes notional equity of £1.35 billion, out of a total capital requirement of around £5.2 billion. This gives rise to average gearing across the AMP of 63%.

Alternatively, if the investment programme was funded entirely with cash and senior debt, we would expect gearing to average around 65% across the AMP. This is based on our full £13.7 billion totex plan, coupled with Ofwat's early view WACC. This also assumes a continuation of our current dividend policy, and no outperformance or rewards.

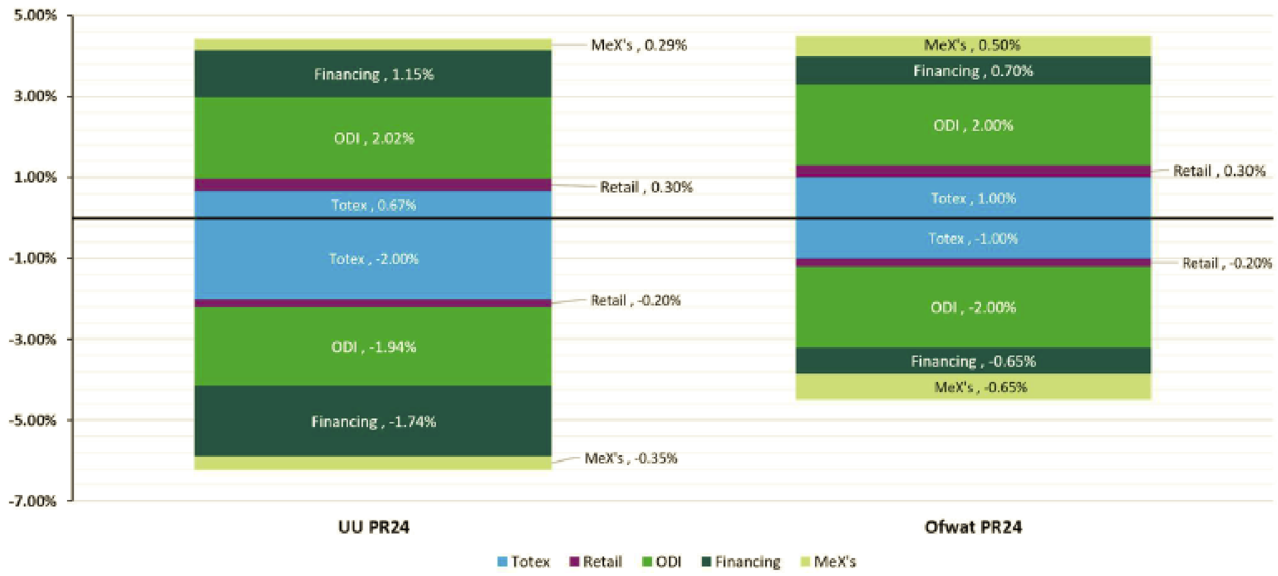
By way of illustration, if the WACC was c.60 bps higher – in line with an AMP8 independent WACC assessment undertaken by Frontier Economics c.3.9% – we would see average gearing levels around 1.5% lower across the AMP. If adaptive planning decisions led to a £1 billion deferral of totex into AMP9, then that would result in a further 1% reduction on average. The combination of both would see group gearing averaging 63% over the AMP, and remaining within our target range of 55-65%.

Return on Regulated Equity (RoRE)

Our plan suggests an overall RoRE range of -6.28% to 4.43%. This demonstrates a broadly downward skewed risk profile, reflecting the stretching costs and performance targets we have set in our plan, but with clear opportunities for rewards in the event of exceptional performance improvements in AMP8, and clear (and significant) penalty consequences in the event of underperformance.

We believe that this represents a reasonable balance of risk and return across out plan, and is consistent (on a component basis) with Ofwat's guideline RoRE ranges that it expects to apply to each source of RoRE variation.

Proposed PR24 UUW RoRE range



Source: Ofwat PR24 RoRE Chart tool 1.0 and submission data tables RR30.

Responsible approach to sharing outperformance and dividends

We have a strong long term track record of sharing outperformance with customers and other stakeholders across 2010-25. This includes:

- Totex reinvestment of £1,170m, with shareholder contribution of £535m
- Company funded pension deficit repair contributions of £310m (in excess of regulatory allowance)
- Support for customers in difficult financial circumstances of £565m, with a shareholder contribution of c£380m.

In total, this represents over £2 billion of reinvestment over the period, of which £1,225m was met through shareholder funds reinvested in the business for the long term rather than distributed as dividends.

CommUnity Share 2030

In AMP7, we committed to providing £71m of company funded support as well as financial benefits for customers and communities if dividends or gearing were to rise significantly above thresholds set in our business plan. We propose to further improve this for AMP8 with our CommUnity Share 2030 commitment, which comprises three key sources of benefits for customers:

- **Shareholder funded financial support for customers:** Based on our submitted business plan we would propose to provide £200 million of company funded, customer support schemes within the base element of the commitment, targeting improved affordability.
- **Gearing incentive:** In the event that UUW gearing exceeds 70%, we guarantee to share half of the financial benefits arising from gearing exceeding 65%. This provides assurances to customers that they share any upside from higher levels of gearing.
- **CommUnity dividends:** In the event that UUW pays dividends that are in excess of 3% of RoRE above the base cost of equity we guarantee a 1:1 matching contribution for customer benefit on the excess.

Dividend Policy

We recognise the importance of dividends to our shareholders, however, as in previous price reviews, our dividend policy will not be decided by the Board and announced until we have received our final determination.

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Water for the North West