

11 August 2023

**Submission to the Industry and Regulators Committee for its *Follow-up inquiry into Ofwat, the water industry and the role of the Government***

## **Introduction**

The Global Infrastructure Investor Association (GIIA) is the membership body for the world's leading institutional investors in infrastructure and advisors to the sector. Our members are responsible for \$1.6tn of infrastructure assets under management across 70 countries. In the UK alone, our members manage assets in the water, energy, transport and telecoms sectors totaling some £225bn.

In water specifically, GIIA members have stakes in 10 of the 15 regional water companies in England and Wales, supplying more than 37 million customers.

GIIA has noted a statement by Ofwat on 29 June that 'overall, the sector is continuing to attract international capital and is especially attractive to long term investors such as pension funds', a suggestion subsequently supported by Defra in oral evidence to the Committee on 18 July.

This submission represents the views of GIIA and is informed by feedback from a range of investors in the water sector from among our membership. Over the last year, we believe investor confidence in the water sector has deteriorated significantly and is most probably at an all-time low. This is reinforced by feedback from our most recent surveys of GIIA members which tell us that the UK has become a markedly less attractive destination for investment. Our pulse survey in autumn 2022 showed that the UK had in six months switched from most to least attractive Western European investment destination ( <https://giiia.net/insights/pulse-survey-q4-2022-europe> ). Our latest survey in spring 2023 shows some recovery for the UK, but with the biggest challenges being 'political instability' and an 'unattractive regulatory regime' compared to the rest of Europe ( <https://giiia.net/insights/pulse-survey-q2-2023-europe> ).

The UK is in a global race for private capital, with huge fiscal incentive packages now offered to investors in both the United States and European Union. Unable to match these, the UK must instead compete on the quality of its policy and regulatory environment, including in the water sector. Our members seek investment opportunities across the globe and they are rightly concerned that the UK must act to drive up investor sentiment.

## **Current Analysis**

Investment in water has been markedly higher since privatisation, water quality is better, leakage rates are down and cost efficiencies have kept bills largely flat for 15 years. Despite these improvements in the sector, investment has not kept pace with public expectations. In recognition of this, the industry has brought forward plans for a £10 billion programme to tackle the historic problem of sewage overflows over the next seven years.

Whilst the reasons behind this are complex and varied, in our view a primary contributing factor has been the regulatory framework, which over recent years has systematically restricted rather than promoted investment. A conscious decision to prioritise lower bills in the short term (lower than most European peers) rather than addressing long term requirements has stored up problems for the future.

In addition to long-standing requirements for maintenance and modernisation, there are now significant, new and additional investment needs driven by climate change, population growth and rising environmental standards placing even great pressures on water companies and their investors.

Much of the industry's investment programme is further driven by the requirements of the Water Industry National Environmental Programme, which prioritises high levels of capital expenditure to improve environmental outcomes but risks squeezing necessary investment in asset health.

At a time when public finances are stretched significantly, and the water sector urgently requires new investment, decisive action must be taken to reboot investor confidence and unlock the changes needed to deliver a resilient water sector in a way that is affordable for customers.

## **Recommendations for change**

We believe the Government must play an important role in unlocking additional investment. The actions we recommend include:

*Setting a long-term plan for the water and wastewater sector, by:*

- giving Ofwat an explicit duty to promote investment
- establishing and reinforcing outcomes-based 2050 targets
- ensuring the Environment Agency and Natural Resources Wales take explicit account of the economic consequences of the requirements they place on the sector

*Establishing clear policy objectives for regulators to implement, by:*

- providing guidance to Ofwat about how to strike the balance between funding from today's customers and from future generations
- re-initiating work on social tariffs for the sector and giving Ofwat guidance on how companies should recover costs from different categories of customer
- using the Strategic Policy Statement to make promotion of investment a specific objective for Ofwat, and providing similar guidance to the Environment Agency and Drinking Water Inspectorate

*Rebuilding confidence in long-term investment, by:*

- enshrining the Regulatory Capital Value in companies' licences, giving investors faith that future policy and regulatory decisions will respect the need for previous investment to be remunerated

- maintaining a robust merits-based appeals regime

We hope this submission is helpful in providing a balanced view to the committee of the challenges facing the water sector, together with some thoughts on what needs to change to get the sector back on track.