

Final Business Plan

Severn Trent Water - Explanation of our plan to deliver now and in the future

OVERALL STRATEGY FOR 2010-2015 PERIOD AND BEYOND

In December 2007 we published our Strategic Direction Statement (SDS) setting out our 25-year vision. In August 2008 we published our Draft Business Plan (DBP), setting out the steps we will take over the next five years in working towards delivering the objectives we set out in the SDS. This Final Business Plan (FBP) refines the proposals set out in the DBP, taking into account feedback from Ofwat and other stakeholders and additional work to increase the robustness of our analysis.

Since the DBP was produced, the economic environment has deteriorated significantly. This underlines the need to set bills at a level which domestic customers and businesses can afford. It also means that the future costs of financing are more uncertain and that price limits need to be set at a level which allow us to withstand economic fluctuations.

The FBP has been put together in a holistic and balanced way and has been produced directly from our business planning process. The outcomes of our plan are consistent with our SDS and deliver improvements which all stakeholders want, while ensuring that our plans are affordable. This includes:

- **Lowest possible bills** – average household bills will rise by 4% in real terms by the end of the period.
- **Improved services** including increased network resilience and reducing sewer flooding.
- **Environmental improvements** delivered through improving sewage treatment.
- **Increased spending on assets** to ensure that the environmental and drinking water quality improvements achieved since privatisation are maintained.
- **Challenging efficiency targets.**
- **A financeable plan** which strikes the right balance in keeping prices low and maintaining investor confidence.
- **Sustainable solutions** including promotion of catchment management, sustainable drainage solutions, increased renewable electricity generation, and taking into account carbon impacts in all the decisions on our programme.

In developing the plan to meet our objectives we were faced with a number of significant challenges, in particular:

- Our objective of delivering lowest possible prices is affected by upward pressures on our operating costs such as rates, abstraction charges and Traffic Management Act costs, which outweigh the challenging efficiencies which we have included in the plan.
- Our plans to reduce greenhouse gas emissions are being offset by a number of upward pressures, the most significant of these being new environmental quality standards.

Price limits need to be set which enable us to finance the plan. A period of negative inflation would reduce our income levels and damage our financial ratios, which could affect our ability to raise finance on reasonable terms. We have put forward proposals on how price limits can be set to manage this risk.

Our plan makes progress on improving services which customers think are worthwhile, maintains our drive for lowest prices, and delivers environmental improvements. This is possible as a result of the very challenging efficiency targets which we have set. When final decisions on prices and outputs are made by Ofwat it is essential that the overall balance of the plan is maintained.

PRICE LIMITS AND EFFECT ON AVERAGE BILLS (2007-08 PRICES)

	2009-10	2010-11	2011-12	2012-13	2013-14	2014-15
Proposed price limit		3.1%	0.6%	0.6%	0.6%	0.6%
W Indicative price limit (water service)		8.9%	1.1%	1.0%	0.6%	0.1%
1 Average measured household bill	132.2	139.8	139.9	140.5	140.6	140.4
2 Average unmeasured household bill	145.7	162.7	164.6	165.5	165.7	164.5
2 Average household bill	142.0	156.5	157.9	158.6	158.8	158.2
S Indicative price limit (sewerage service)		-1.9%	0.1%	0.3%	0.6%	1.1%
1 Average measured household bill	129.0	127.0	126.9	127.0	127.4	128.4
2 Average unmeasured household bill	148.3	146.0	146.3	146.6	147.3	148.4
2 Average household bill	141.8	138.1	137.6	137.2	137.2	137.8

QUALITY AND SERVICE IMPROVEMENTS IN 2010-2015 PERIOD AND IN THE LONGER TERM

Our plans include the following improvements in the next five years. These are all consistent with our SDS targets for long-term improvements:

- Significant increases in our resilience to the failure of a water treatment works or aqueduct, benefiting over 1.9 million customers.
- Separating joint supply pipes to improve water pressure for over 11,000 customers.
- Schemes to ensure that we continue to meet drinking water standards, benefiting over 500,000 customers, and catchment management schemes to protect drinking water quality in future.
- Balancing supply and demand by
 - Reducing leakage by more than 12 litres per customer per day.
 - Increased metering, with 42% of customers metered by 2015.
 - Encouraging more efficient use of water.
- Reducing sewer flooding incidents by around 100 per year.
- Meeting new sewage treatment standards at 92 sites to improve river quality.
- Reducing pollution incidents by around 80 per year by 2014/15.
- Reducing odour from sewage treatment works at over 50 sites.
- Keeping carbon emissions stable, despite upward pressures e.g. from environmental improvements.

WHAT IS DRIVING THE CHANGES IN BILLS? (2007-08 PRICES)

			Water	Sewerage
Average household bill in 2009-10			141.98	141.83
Plus	(1) past efficiency savings and outperformance		3.66	-4.38
	(2) maintaining base services		9.59	-4.25
	of which			
	a) changes in revenue	Water	5.98	2.20
	b) changes in operating costs to maintain current services	Sewerage	8.67	3.80
	c) changes in costs of maintaining assets		0.74	-4.08
	d) changes in impact of taxation		-2.84	-2.84
	e) the change in the cost of capital		-2.96	-3.33
	(3) maintaining and enhancing security of supplies to all customers		2.85	3.08
	(4) the impact of improvements in services		5.78	9.74
	of which			
	a) drinking water quality	Water	2.48	
	b) environmental improvements	Sewerage	0.14	7.08
	c) Improvements in service levels		3.16	2.66
	(5) scope for reduction through future efficiency improvements		-5.64	-8.18
Average household bill in 2014-15			158.22	137.84

ESTIMATE OF EXPENDITURE NEEDS (2007-08 PRICES)

		Annual average for the 2010-2015 period (£/property/annum)	
		Water	Sewerage
1	Operating costs to maintain current services to consumers	78.8	61.3
2	Operating costs to improve services to consumers and protect the environment	1.8	2.7
3	Cost of maintaining assets to deliver current services to consumers	46.3	45.6
4	Cost of improving assets to deliver improvements for the environment and consumers	23.6	27.7
		Pre-tax cost of debt and post-tax cost of equity basis	Fully post-tax basis
5	Assumed cost of capital (%)	5.8%	5%

For further information go to: www.stwater.co.uk