OUTLOOK
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Analyst Contacts

Stefanie Voelz +44.20.7772.5555
VP-Sr Credit Officer
stefanie.voelz@moodys.com

Paul Marty +33.1.5330.3371
Associate Managing Director
paul.marty@moodys.com

Neil Griffiths-Lambeth +44.20.7772.5543
Associate Managing Director
neil.griffiths-lambeth@moodys.com

Regulated Water Utilities – UK

Outlook remains negative on tough price review

Summary

Our outlook for the UK Water sector remains negative. Public, political and regulatory scrutiny remains high amid serious concerns over the companies' operational and financial performance. There is a risk that this will result in a less favourable risk-return profile that could further weaken the sector's credit quality and make it hard to attract necessary funding. Water companies in England and Wales are currently in the midst of a price review process that will set cost allowances, performance targets, returns and bills for the next five-year regulatory period, which runs from 1 April 2025 to 31 March 2030, known as AMP8. Companies' representations, published in August 2024, confirmed our view that the July draft determinations provide significantly greater risk than opportunities on both total expenditure (totex) and outcome delivery incentives (ODIs).

» **Low achieved returns reflect sector underperformance.** Operational underperformance, driven by total spending above allowances and performance penalties, has reduced operating cash flow and resulted in a weak adjusted interest coverage ratio (AICR), averaging around 1.0x to date in the current five-year period. The sectorwide cumulative achieved return on regulatory equity (RORE) is also low at 2.9%, below the average base allowance of 4.1%.

» **AMP8 draft determinations imply increased operational risk.** Totex and ODI risks remain elevated in AMP8, because of a significant increase in capital spending, carrying with it associated execution risks, as well as higher operational incentive rates, which exacerbate the penalty risk from underperformance.

» **Allowed returns may not be sufficient to attract investors.** Companies called for a higher allowed return to reflect the greater risk they are being asked to bear. Although all companies submitted the required "board assurance" statements, confirming that their business plans are deliverable and financeable, several made these statements contingent on their expectation of significant changes between draft and final determination.

» **Higher risk means weaker credit quality.** Final determinations are typically less onerous than drafts. However, we believe the sector's business risk is growing with ongoing public, political and regulatory pressure diminishing investor confidence.

» **What could change our outlook:** We could change the outlook to stable if Ofwat's final determination for the next period, to be published in December 2024 or January 2025, proves supportive of companies' investment needs or management and shareholders take mitigating action to bolster credit quality. Companies' representations in response to the draft indicate that many are laying the groundwork for an appeal to the Competition and Markets Authority (CMA), if the risk and return profile is not rebalanced in their favour.

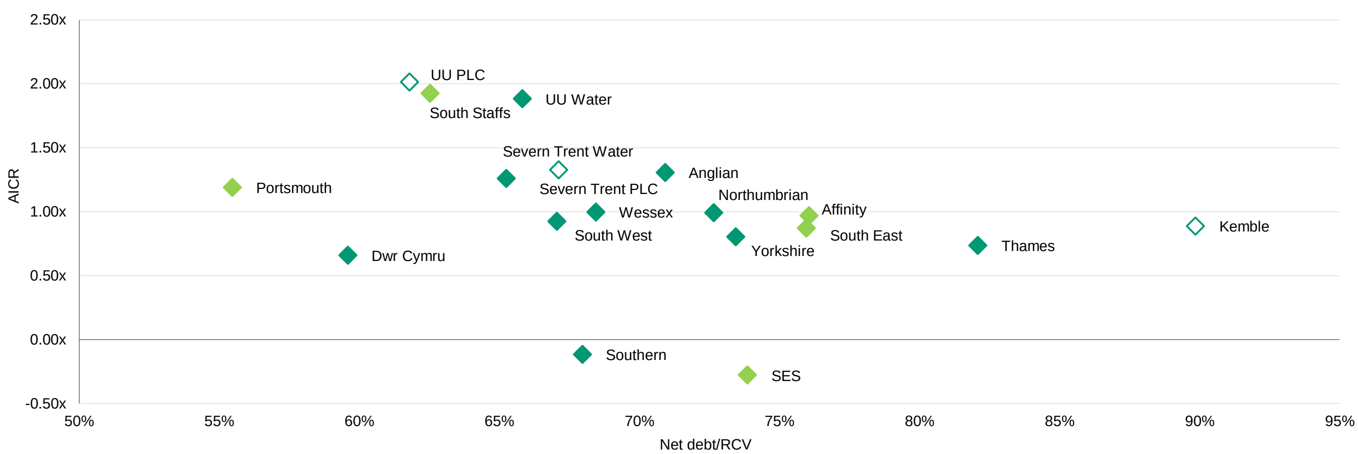
Outlook definition

The negative outlook reflects our view of credit fundamentals in the UK water sector over the next 12 to 18 months. Sector outlooks are distinct from rating outlooks which, in addition to sector dynamics, also reflect issuers' specific characteristics and actions. A sector outlook does not represent a sum of upgrades, downgrades or ratings under review, or an average of rating outlooks.

Low achieved returns reflect sector underperformance

Companies' performance in the current regulatory period, known as AMP7, which runs until 31 March 2025, has deteriorated because most companies are overspending on their cost allowances and incurring performance penalties. This is credit negative as it reduces cash flow available for debt service. Companies' AICR, one of the key metrics we monitor, remains weak (see Appendix for detailed FY 2023/24 credit metrics), averaging around 1.0x for the rated companies over the first four years of AMP7 (see Exhibit 1). This also reflects volatile macroeconomic conditions over most of the current regulatory period. Companies will receive an uplift to their regulatory capital value (RCV) and revenue at the end of the period to compensate for rising costs and interest rates (see also our 2024 water sector outlook), which we expect to improve the baseline ratio for all companies over the next period.[1] However, draft cost allowances and performance targets point to a continuing risk that companies will not be able to earn allowed returns.

Exhibit 1
Companies' AMP7 AICR has been weak, averaging around 1.0x for the sector
Moody's adjusted metrics, average FYE March 2021 — FYE March 2024



Dark green filled = operating companies, water and wastewater; dark green lined = holding companies; light green filled = operating companies, water only. South West Water is a three-year average between 2021/22-2023/24 as the company was not rated before July 2024, and Kemble is a three-year average between 2020/21-2022/23 as the Kemble group has not yet published FY 2023/24 accounts.
Source: Moody's Ratings

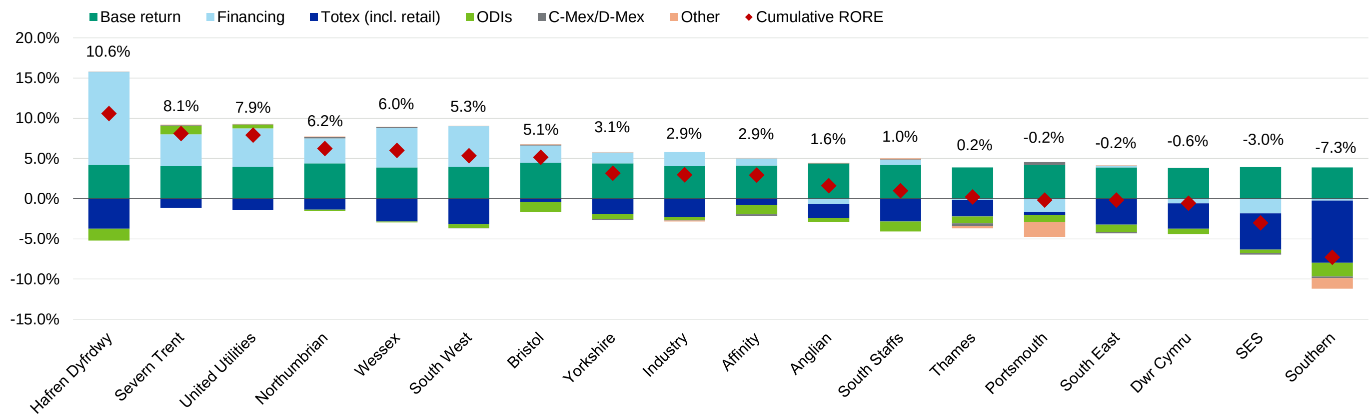
Weak operational performance, exacerbated by tough regulatory targets, may make it harder for companies to attract equity investment in the future. An unfavourable risk-return profile will ultimately increase the cost of funding and therefore the bills paid by consumers.

Exhibit 2 shows that over AMP7 to March 2024, operational performance resulted in a reduction in the achieved regulatory return on equity (RORE, calculated on the basis of notional equity at 40% of the regulatory capital value or RCV) for all companies. While RORE is an equity measure, it also illustrates how cash flow generation has been declining across the sector.

Combined underperformance against totex allowances, performance targets and service measures has reduced the sector RORE by around 2.7 percentage points on average over AMP7 to date, ranging between an almost negligible reduction (-0.01 percentage points) for Severn Trent Water Limited (Baa1 stable) to almost -10 percentage points for Southern Water Services Limited (funded through SW (Finance) I PLC, Baa3, review for downgrade).

This is partially mitigated by a number of companies reporting financing outperformance on a notional basis, which has added, on average, 1.7 percentage points to the cumulative sector RORE to date. Overall notional funding cost outperformance (after hedging) accounts, on average, for roughly half the sector's reported financing cost outperformance, with the remainder linked to benefits from changes to the tax regime, in particular additional capital allowances.

Exhibit 2
Companies' reported AMP7 RORE is reduced by operational underperformance



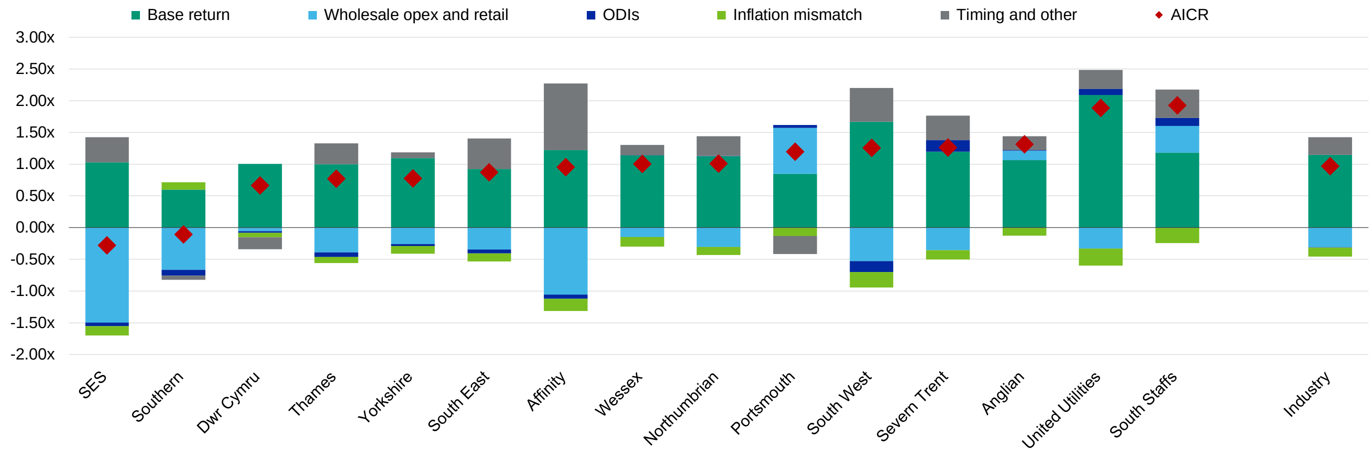
Source: Companies' annual performance reports FY 2023/24

Ofwat calculates financing cost outperformance by taking companies' actual nominal cost of debt and deflating with actual inflation to arrive at a company's real cost of debt, which is then compared with the real cost of debt allowance. On this basis, companies with a larger share of nominal fixed rate debt will exhibit higher cost of debt outperformance in a high inflation environment, as has been the case in recent years. However, companies' cash flow will only benefit from higher inflation over time as their RCV grows and future returns are earned on that larger asset base, while cost overruns and performance penalties have an immediate adverse impact on cash flow and credit ratios (see Exhibit 3).

Exhibit 3

Cost overruns, performance penalties and inflation mismatch have significantly reduced companies' AICR over AMP7 to date

AICR build-up average FYs 2020/21-2023/24



Inflation mismatch is the difference in revenue when comparing prior year November CPIH, used to determine allowed revenue, and FY average CPIH, which is a better reflection of companies' cost drivers. Timing and other includes under-/overrecovery of revenue because of volume changes, non-appointed and other operating income as well as differences between regulatory and statutory reporting.

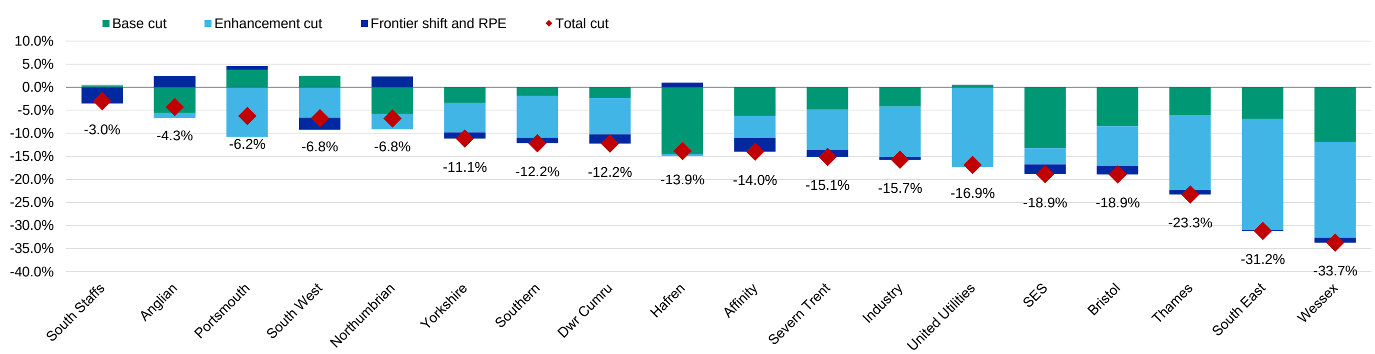
Source: Moody's Ratings

AMP8 draft determinations imply increased operational risk

In July 2024, Ofwat, the economic regulator for water and wastewater companies in England and Wales, published its draft determination for AMP8. The draft determination imposed a sizeable cut in total expenditure, or totex, to £88 billion, 16% below companies' request of £105 billion (both after frontier-shift[2], see Exhibit 4), and materially increased reward and penalty rates for ODIs.

Exhibit 4

Totex shortfall based on draft allowance compared with companies' original plans

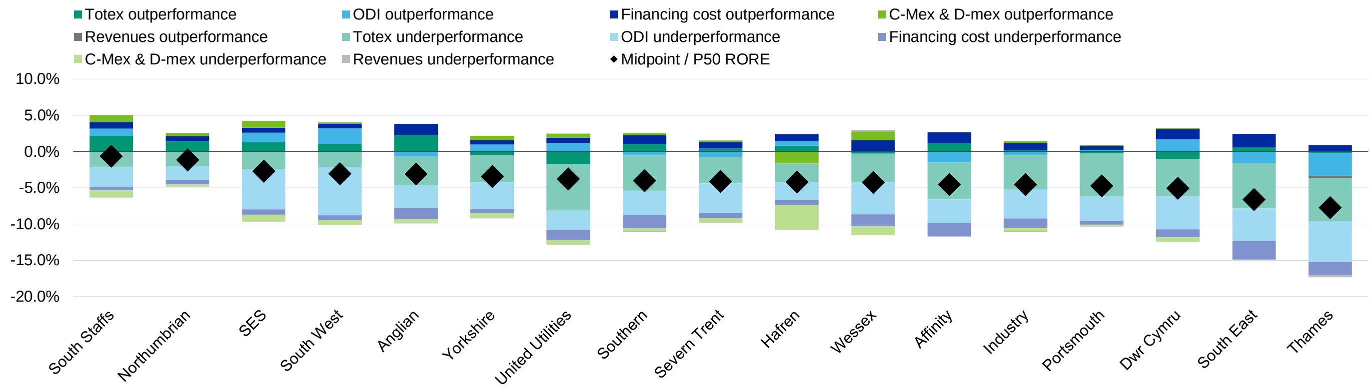


Source: Ofwat's draft determinations

In their representations, most companies believed they would not be able to earn allowed equity returns, because of risks associated with their totex programme and ODI performance expectations. The midpoint of the RORE ranges presented by companies points to the sector potentially underperforming base RORE by around 4.6 percentage points. This sits within an additive[3] average range of +0.9 percentage points and -10.6 percentage points on RORE for the industry, indicating a clear downside skew (see Exhibit 5).

Exhibit 5

Companies' expected ranges of RORE upside or downside over base returns under Ofwat's draft determination (before mitigating measures and representations)



Midpoint reflects P50, where disclosed.

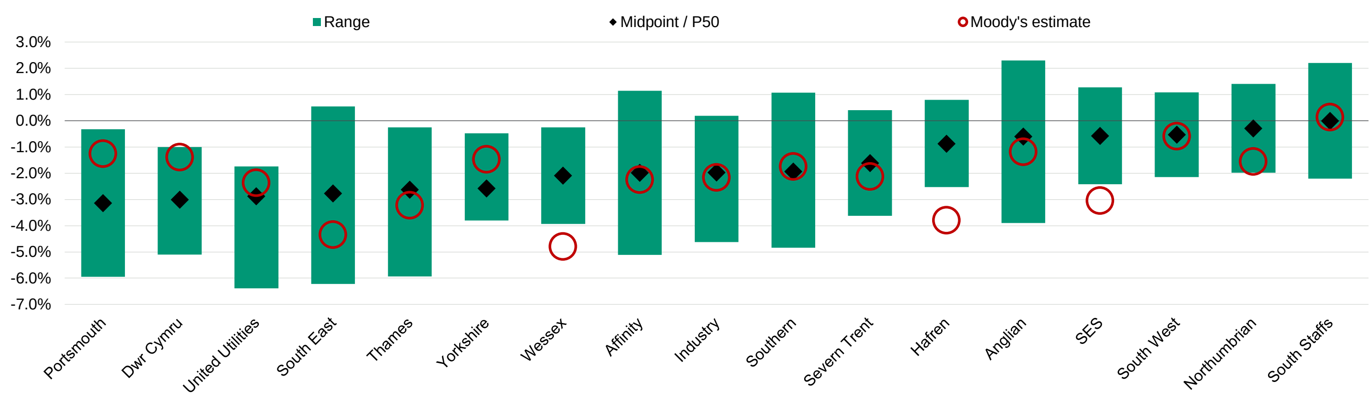
Source: Companies' business plan data tables and commentary, republished as part of representations

Totex risks reflect cuts made by Ofwat at the draft stage, but may be exacerbated by price control deliverables that reduce flexibility in adjusting the programme to changing circumstances.

In their representations to Ofwat's draft determination, companies indicated a potential totex upside (after applying the relevant sharing rates) of only around £500 million on underspend compared with a downside of £12 billion on overspend against allowances, with the midpoint assuming a £5-6 billion downside exposure (post-sharing) on overspend. The latter would result in a RORE reduction of around 2.0-2.2 percentage points for the sector from totex underperformance. This compares with the RORE reduction of around 2.2 percentage points we estimated if companies spent their initial business plan requests rather than the draft allowances.

Exhibit 6

Companies' expected RORE impact from totex performance based on Ofwat's draft determination

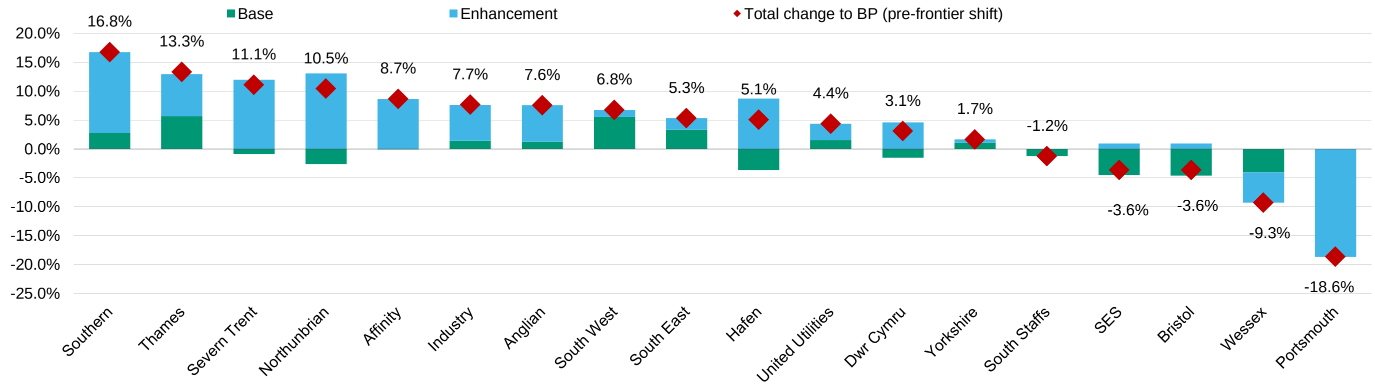


Totex performance includes wholesale and retail costs as well as risk associated with price control deliverables per company representations, before mitigating measures. South West includes Bristol. RORE impact reflects sharing of over- and underspend with customers depending on different sharing rates applied to different cost categories. There is also an overarching aggregate sharing mechanism, whereby any out-/ underperformance impact of totex allowances, which results in a +/-2 percentage point change in RORE would be shared 50% with customers.

Source: Companies' business plan data tables and commentary, republished as part of representations and Moody's Ratings

Companies' representations also included an overall increase in their totex request of almost 8% to £115 billion (before frontier-shift), including cost adjustment claims (see Exhibit 7). Many companies included further evidence on additional base cost requests, stating that historical cost assumptions that underpin Ofwat's econometric cost models remain too low to cover future spending needs, in particular for asset maintenance. Increased enhancement requests largely reflect new cost information and additional guidance on new environmental obligations that companies will be legally required to deliver. We expect Ofwat to consider these additional data points when preparing its final determination.

Exhibit 7
Most companies increased their totex request in DD representations



Source: Ofwat's draft determinations; companies' business plan data tables, republished as part of representations, and Moody's Ratings

In their representations on ODIs, companies have argued that:

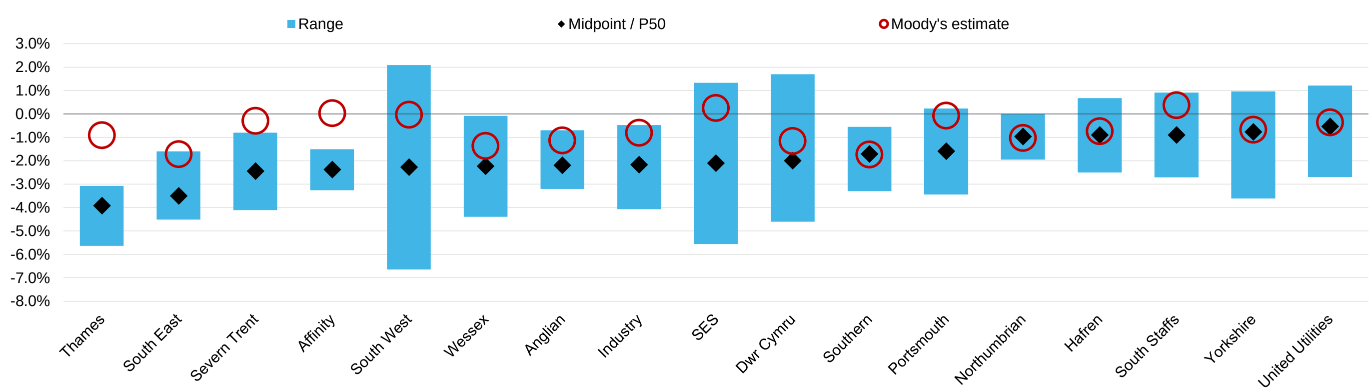
» The starting point is wrong, as it assumes that companies would achieve AMP7 final year performance target levels, when many are underperforming.

» The trajectory of improvement is not feasible, given the funding provided and the uncertainty around performance against newly introduced targets.

» The sizeable increase in incentive rates for performance commitments, which carries over from AMP7 without applying deadbands or caps/collars, creates material risk. This is because performance may be affected by weather patterns and is not always fully within management control.

The material downside skew could result in a RORE reduction from ODI performance for the industry of between -0.5 percentage points (£1.2 billion penalty exposure) and -4.1 percentage points (over £10.5 billion penalty exposure), with a midpoint RORE reduction of around 2.2 percentage points (over £5.5 billion of penalties). Our previous estimate was a net penalty of around £2 billion for the industry based on business plan forecast performance (or -0.8 percentage points on RORE). This estimate excluded external sewer flooding penalties for Thames Water Utilities Ltd. (CFR: Caa1 negative), because of significant inconsistencies in setting targets compared with performance levels – including these would have added around £1 billion to our estimate for the sector.

Exhibit 8
Companies' expected RORE impact from ODI performance based on Ofwat's draft determination



Excludes service measures and for our estimates also excludes external sewer flooding for Thames Water because of inconsistencies between targets and expected performance. High and low range of ODI performance based on draft determination per company representations, before mitigating measures. There is an aggregate sharing mechanism where a RORE impact of more than +/- 3 percentage points is shared 50% with customers and a more than +/- 5 percentage points is shared 90%. South West includes Bristol.
Source: Companies' business plan data tables and commentary, republished as part of representations, and Moody's Ratings

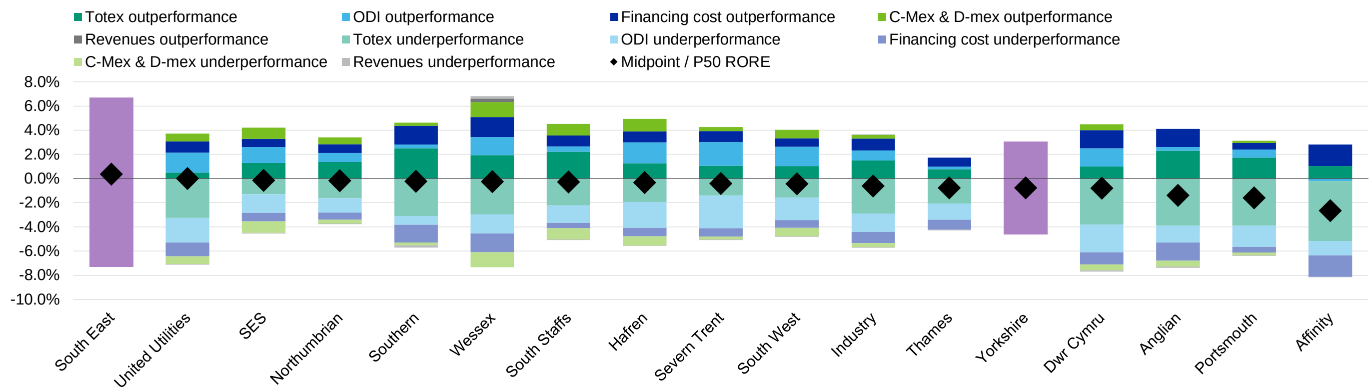
In addition to the above, companies estimated that customer, developer and business/retail service measures could add penalties on average, with the midpoint for the industry an almost £83 million penalty (or a 0.03 percentage point RORE reduction).

Based on companies' representations to Ofwat's draft determinations, we estimate that the industry could exhibit a reduction in the AMP8 AICR of around 0.4x on average, when considering the midpoint of ODI performance ranges. However, the worst case scenarios presented by companies could extend to AICR reductions between 0.5x and 1.0x for ODI underperformance. Looking at the risk of totex overspend, we estimate that overspending on allowances on the basis of companies' representations could – if primarily debt-funded – result in an increase in gearing of between 5% and 10% of the RCV (post-sharing). However, there is significant uncertainty in our forecast, because of likely changes in totex allowances and performance incentive calibration in the final determinations.

Taking account of mitigating measures and adjustments to the draft determination as provided in companies' representations, water companies believe that the risk profile could be improved (see Exhibit 9). However this will require Ofwat accepting most of the companies' proposals, which is unlikely.

Exhibit 9

Companies' expected ranges of RORE upside or downside over base returns under Ofwat's draft determination (after mitigating measures and representations)



South East and Yorkshire did not provide a detailed breakdown of the unmitigated risk profile in their commentary. Midpoint reflects P50, where disclosed.
Source: Companies' business plan data tables and commentary, republished as part of representations

Allowed returns may not be sufficient to attract investors

We believe that the current price review process creates material risks for the sector. If the final determination maintains a significant downside skew and achieved returns are therefore likely to fall short of what is allowed, it will hinder companies' ability to attract funding for growing investment needs. Increased funding costs would compound companies' difficulties.

In their representations, companies called for a higher allowed return to reflect the greater risk they are being asked to bear. Updating Ofwat's methodology for latest market data on cost of debt and the risk free rate would indicate an allowed return in the range of 3.7%-4.1%, compared with Ofwat's draft determination of 3.66% and an average return of around 4.4% requested by companies (all wholesale weighted average cost of capital, CPIH-deflated).

Exhibit 10

Companies' representations ask for sizeable increase in allowed returns

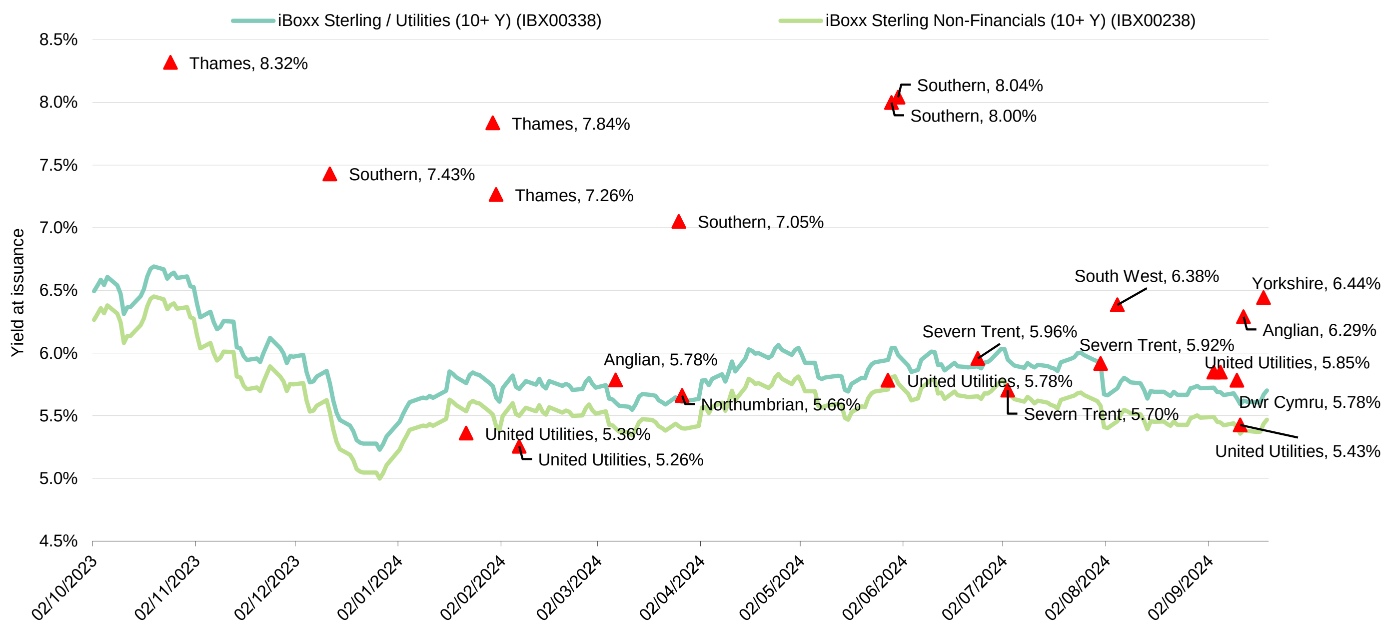
	PR19 (Ofwat FD)	PR19 (CMA - WaSCs)	PR24 (Ofwat DD)	PR24 (WaSCs reps)
Gearing	60%	60%	55%	55%
Cost of debt	2.14%	2.18%	2.84%	3.26%
Cost of equity	4.19%	4.73%	4.80%	5.79%
Appointee WACC	**2.96%**	**3.20%**	**3.72%**	**4.40%**
Retail Margin	0.04%	0.08%	0.06%	0.00%
Wholesale WACC	**2.92%**	**3.12%**	**3.66%**	**4.40%**

All returns presented as vanilla (pretax cost of debt and post-tax cost of equity) weighted average cost of capital, CPIH-deflated. PR24 (WaSC reps) is the average for nine water and sewerage companies that included detailed representations on the allowed return.
Source: Ofwat, companies' representations to PR24 DD and Moody's Ratings

Exhibit 11 illustrates that companies' cost of debt from recent issuance is higher than implied by the draft determination, but we expect Ofwat to take latest market evidence into account when setting final allowed returns.

Exhibit 11

Companies' recent issuance has been above the index used by Ofwat to determine cost of new debt allowances



Ofwat's methodology applies the average of the A and BBB-rated iBoxx GBP non-financials 10+ indices (over a one month period) when setting the cost of new debt allowances, deflated by a long-term 2% CPIH assumption to arrive at the real cost of new debt. At the draft determination, the regulator removed the previously applied 15 bps reduction to the index. The draft determination allowed cost of debt assumed that the portion of new to embedded debt is on average 26:74 over AMP8.
Source: Factset

Although all companies submitted the required “board assurance” statements, confirming that their business plans are deliverable and financeable, several made these statements contingent on significant changes between draft and final determination.

Higher risk means weaker credit quality

Regulatory and political pressure is unlikely to abate, but final determinations are typically less onerous than drafts as regulators respond to companies' additional evidence. Ofwat will publish its final determinations in December 2024 or January 2025. Should companies decide to appeal these to the CMA, the ultimate AMP8 settlement may not be known before autumn 2025, because the CMA typically has six to twelve months to process the appeals.

We believe the sector's business risk is growing, largely driven by the following:

» **Highly negative public perception**: The persistent critical narrative around wastewater treatment and discharge, leakage and dividends – even if not always justified – makes it harder to convince customers of the need for bills to rise to fund improvements. Customer affordability will also remain a key concern for Ofwat and influence its decision on overall cost allowances.

» **Political and regulatory focus on enforcement**: Public concern increases pressure on government and regulators to set more demanding targets and impose tougher penalties for failure. Critically, fines and penalties will remove funding from companies most in need of improvement.

» **Policy uncertainty ahead of expected review**: The new government has described "a broken water system" and promised a "full scale review" to "fundamentally transform how our entire water system works".[4] Vocal campaigns have successfully focused attention on wastewater but the Environment Agency highlights the need for new water resources to avoid drinking water shortages by 2050. The cost of improving resources and environmental performance as well as to prepare for future growth and the rising impact of climate change means that trade-offs and compromises will be necessary if bills are to remain affordable. An overarching long-term strategic direction that balances stakeholder priorities would support investment but fundamental transformation could come at the expense of regulatory track record, something that has previously underpinned confidence. The review brings uncertainty at a key moment.

» **Weakening investor sentiment**: Uncertainty and volatility will weigh on the appetite of institutions that have previously invested in the UK water sector on the assumption that monopoly providers of an essential commodity, operating under a long-standing regulatory framework, would enjoy stable and predictable returns at least at their cost of capital. The impact will vary according to companies' circumstances. Shareholders in Thames Water have branded the current regulatory arrangements uninvestable and the company is facing a liquidity shortfall that could lead to a near-term distressed exchange.[5] Investors will have many other options, outside the water sector, to deploy capital with sizeable decarbonisation investment globally. A smaller pool of investors in the sector and higher funding costs will ultimately also increase consumer bills.

All of the above point to a less supportive environment for regulated water utilities in the UK. The regulatory regime's stability and supportiveness, as well as companies' ability to earn a fair return, are key factors under our rating methodology for regulated water utilities. We will review our score for either or both of these factors when assessing companies' credit quality. Against this background, companies would need to strengthen their credit ratios to maintain their current credit quality.[6] More highly leveraged companies will face greater credit risk as they have less financial flexibility to accommodate weakening business fundamentals. They may also face more difficulty in attracting new equity funding to bolster credit quality, particularly if their performance is below average.

We could change our sector outlook to stable, if the final determination for the next regulatory period proves supportive of companies' investment needs or management and shareholders take risk mitigating action to bolster credit quality.

Appendix – Key credit metrics and ratings summary

As at March 2024, the weighted average gearing across the companies we rate is around 70%. This includes our adjustments, for example, for pension obligations, but is broadly in line with Ofwat's reported 'unadjusted' weighted average regulatory gearing. The weighted average AICR across rated companies is around 0.7x (Exhibit 12), and largely represents allowed returns, plus non-appointed income and performance effects, divided by interest. In our calculation, we typically remove excess fast money, that is the revenue allowance significantly exceeding planned operating costs, as well as in-period revenue profiling to smooth bills. We do not include income from grants and contributions, which companies may report as part of operating cash flow, because this aims to support capital investment into new connections.

Exhibit 12

UK water companies' key ratios and debt profile as at 31 March 2024

Issuer	Rating	Moody's adjusted AICR	Moody's adjusted gearing	Reported gross debt (£ 'millions) [7]	Reported net debt (£ 'millions) [7]	% of debt fixed (excl. IL debt)	Average nominal cost of fixed-rate debt (excl. IL)	% of debt index-linked (incl. swap positions) [8]	Average real cost of IL debt [9]
Anglian Water Services Ltd.	A3	1.1x	69.0%	8,362	7,360	28%	5.7%	60%	1.5%
Dwr Cymru Cyfyngedig (Welsh Water)	A3	0.8x	60.4%	4,671	4,567	11%	4.1%	84%	1.6%
United Utilities Water Limited	A3	1.2x	65.8%	10,614	9,357	31%	3.8%	45%	0.9%
Affinity Water Ltd.	Baa1	1.3x	76.1%	1,461	1,386	13%	3.7%	87%	1.6%
Northumbrian Water Ltd.[1]	Baa1	0.7x	73.5%	3,831	3,819	55%	4.5%	37%	0.8%
Severn Trent Water Ltd.	Baa1	1.0x	63.5%	7,675	7,249	69%	3.9%	28%	1.8%
South West Water Limited	Baa1	0.4x	70.1%	3,330	3,304	66%	3.9%	14%	4.1%
United Utilities PLC [2, 3]	Baa1	1.4x	61.6%	10,159	8,760	31%	3.8%	45%	0.9%
Wessex Water Services Ltd.	Baa1	0.5x	68.9%	2,969	2,963	55%	4.1%	31%	1.7%
Portsmouth Water Ltd. [4]	Baa2	0.8x	39.8%	244	128	9%	3.0%	90%	3.3%
Severn Trent Plc [2]	Baa2	1.1x	62.9%	8,259	7,331	69%	3.9%	28%	1.8%
South East Water Ltd.	Baa2	0.6x	77.5%	1,353	1,351	29%	4.0%	55%	2.9%
South Staffordshire Water Plc [5]	Baa2	1.3x	70.6%	393	372	28%	4.0%	72%	3.3%
Sutton & East Surrey Water plc	Baa2	-0.3x	78.6%	321	275	12%	5.6%	67%	2.9%
Yorkshire Water Services Ltd.	Baa2	0.7x	69.3%	6,315	6,265	36%	3.3%	57%	2.7%
Southern Water Services Ltd.	Baa3	-0.6x	70.1%	5,372	4,858	26%	4.5%	73%	2.1%
Thames Water Utilities Ltd.	Caa1	0.6x	82.9%	17,483	16,208	36%	5.0%	55%	1.1%
Total Industry (OpCos only) [6]		**0.7x**	**70.7%**	**74,465**	**69,533**	**37.8%**	**4.3%**	**51.7%**	**1.6%**

Notes: Operating company debt amounts and interest rates based on regulatory annual performance report (APR)
[1] consolidated metrics, including Kielder funding;
[2] debt numbers adjusted for fair value and foreign exchange derivatives; debt split and interest cost assumptions aligned with operating company APR;
[3] data are based on United Utilities Group PLC;
[4] debt numbers include shareholder loans, but Moody's adjusted metrics exclude these from gearing;
[5] debt numbers exclude debt premium of £11.7 million as at March 2024;
[6] average is based on operating companies reported APR data across the sector for debt and interest information, but Moody's metrics (weighted by RCV) for rated issuers only;
[7] reported debt numbers per operating companies APR, table 1E; holdings per annual atatutory accounts;
[8] IL debt includes mostly RPI-linked debt, but can include a small portion of CPI/CPIH-linked debt;
[9] weighted average cash cost of RPI- and CPI/CPIH-linked debt.

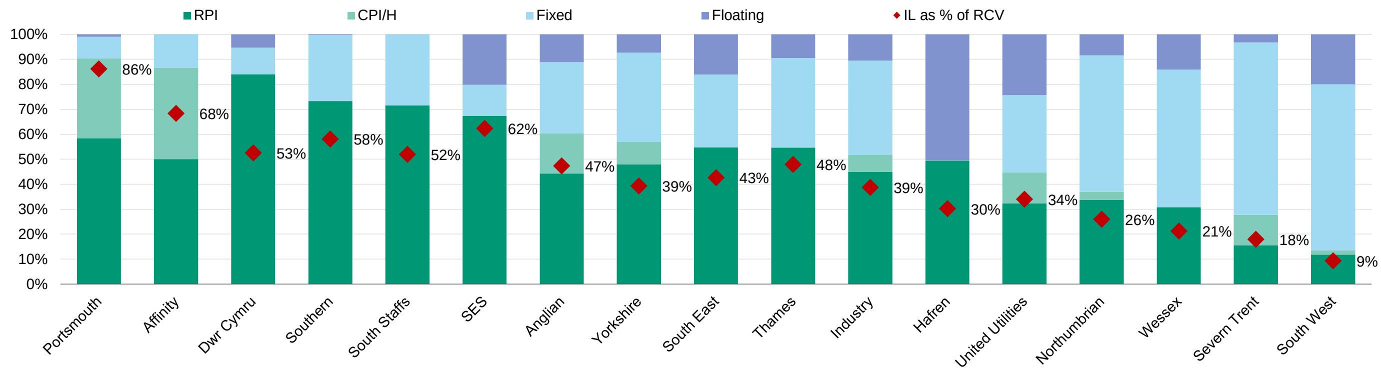
Source: Moody's Ratings on company and regulatory data

As at March 2024, 52% of the sector's debt was inflation-linked, on average, (45% to the retail prices index or RPI, and 7% to the consumer prices index or CPI, including an adjustment for housing costs, referred to as CPIH), equivalent to around 39% of the industry's RCV (see Exhibit 13). Companies with a below average proportion of inflation-linked debt, in particular Northumbrian Water Ltd. (Baa1 stable), Wessex Water Services Ltd. (funded through Wessex Water Services Finance Plc, Baa1 stable), Severn Trent Water and South West Water Limited (Baa1 negative), would see larger financing outperformance (based on Ofwat's notional RORE calculations) in a high inflation environment, but may exhibit an overall higher cash interest cost and therefore lower AICR.

Exhibit 13

Around half the sector's total debt is inflation linked

Debt split as at March 2024



Source: Companies' annual performance reports FY 2023/24

Some of the inflation-linked debt has been created synthetically through swaps. For companies that have entered into highly covenanted structures, termination payments under certain interest rate derivative transactions, including for inflation-linked swaps, are typically treated as super senior to the payment of senior debt principal.

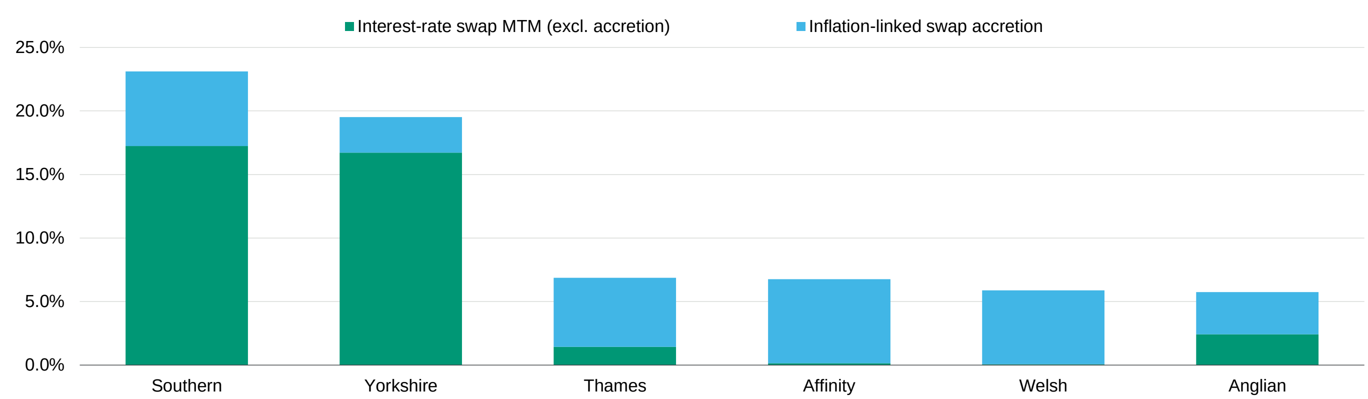
To assess the potential risk, we monitor the mark-to-market (MTM) value of these liabilities. The MTM value is a combination of market expectations around forward-looking interest and inflation rates and accumulated inflation accretion. The latter is typically already included in reported gearing, but the amount would still rank ahead of other senior creditors.

Exhibit 14 summarises reported derivative MTM (excluding accretion) as well as cumulative accretion values for interest-rate derivatives (including inflation-linked swaps) as a percentage of companies' RCV as at March 2024, for companies under highly covenanted financing structures. Southern Water and Yorkshire Water Services Limited (funded through Yorkshire Water Services Finance Limited and Yorkshire Water Finance plc, with senior debt issuance rated Baa2 and junior debt issuance rated Ba1, both with stable outlook) have by far the largest exposure.

Exhibit 14

MTM liability for interest rate derivatives, including inflation-linked swaps, as a percentage of RCV

As at March 2024

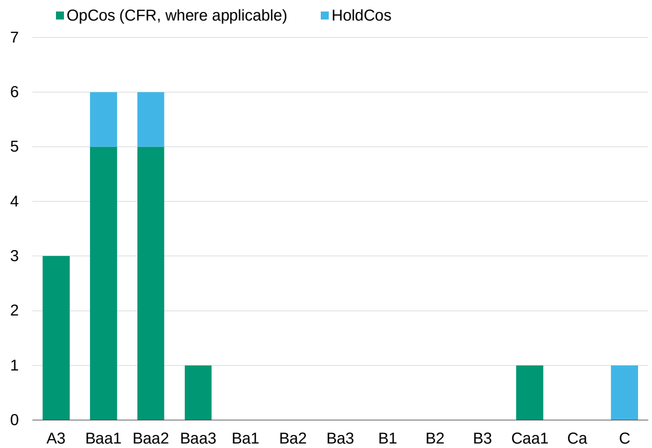


Most interest rate derivatives rank super senior, although pari passu ranking is possible. Companies may report their overall MTM value as adjusted for credit risk, which reduces the reported obligation.

Source: Companies' annual performance reports FY 2023/24 and Moody's Ratings

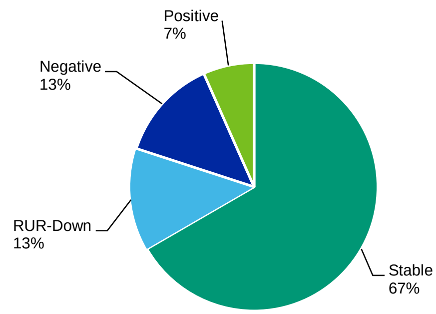
All issuers covered in this outlook are based in England and Wales. We rate 15 operating companies, some of which have a corporate family rating (CFR) and issue (typically via finance subsidiaries) one or two classes of debt (notched from the CFR). We also rate three holding companies. Most water company groups have a stable outlook, but where companies face particular risk from the recent draft determinations, the rating outlook is negative or ratings are on review for possible downgrade; one deeply subordinated holding company (Kemble) is in default.

Exhibit 15
Rating Distribution



Ratings accurate as at the date of this report.
Source: Moody's Ratings

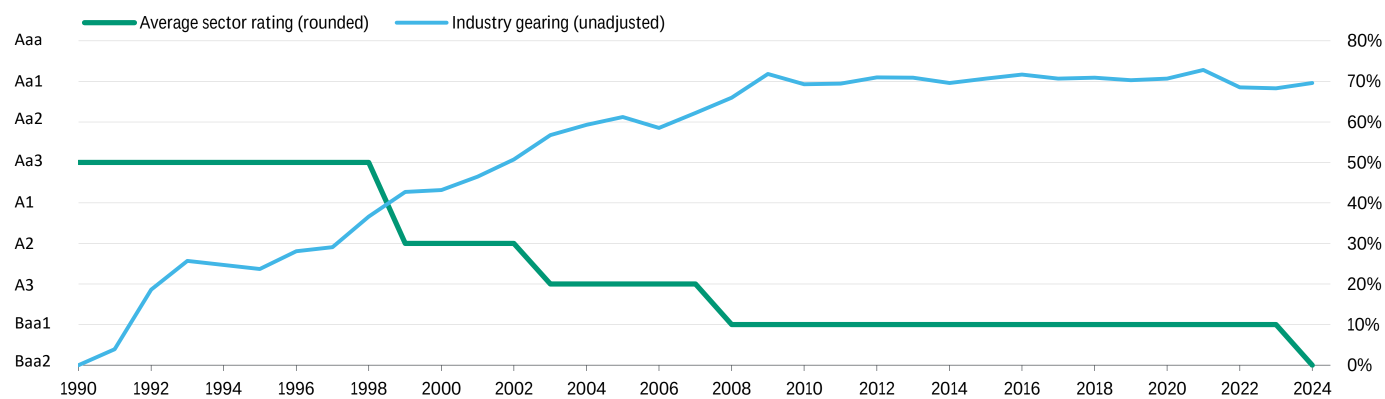
Exhibit 16
Outlook Distribution (OpCos/Families)



Outlooks accurate as at the date of this report.
Source: Moody's Ratings

The average sector rating, based on rated operating companies and excluding holdings, is now Baa2.

Exhibit 17
Rating History (average OpCo ratings against average regulatory OpCo gearing over time)



Industry gearing is the RCV-weighted average of regulatory gearing as reported by companies to Ofwat. Sector rating is the simple rounded average of corporate family rating, where applicable, or senior secured and senior unsecured ratings of operating companies (or their guaranteed finance subsidiaries, where the operating company is not rated directly) and excludes holding company or subordinated debt ratings.
Source: Moody's Ratings

Exhibit 18 provides a summary on the individual issuers' ratings and outlooks.

Exhibit 18
Ratings and outlooks as at the date of this report

	Rating Type	Rating	Outlook
Anglian Water			
… Anglian Water Services Limited	CFR	A3	Stable
… Anglian Water Services Financing plc	Senior Secured (Class A)	A3	Stable
Dwr Cymry/Welsh Water			
… Dwr Cymry Cyfyngedig	CFR	A3	Stable
… Dwr Cymru (Financing) UK Plc	Senior Secured/Subordinated	A3/Baa2	Stable
Northumbrian Water			
… Northumbrian Water Limited	Senior Unsecured	Baa1	Stable
… Northumbrian Water Finance Plc	Senior Unsecured (Backed)	Baa1	Stable
Severn Trent			
… Severn Trent Plc	Senior Unsecured	Baa2	Stable
… Severn Trent Water Limited	Senior Unsecured	Baa1	Stable
… Severn Trent Utilities Finance Plc	Senior Unsecured (Backed)	Baa1	Stable
South West Water			
… South West Water Limited	Senior Unsecured	Baa1	Negative
… South West Water Finance plc	Senior Unsecured (Backed)	Baa1	Negative
Southern Water			
… SW (Finance) I PLC	Senior Secured (Class A)	Baa3	RUR-Down
Thames Water			
… Thames Water Utilities Limited	CFR	Caa1	Negative
… Thames Water Utilities Finance Plc	Senior Secured (Class A)/Subordinated (Class B)	Caa1/C	Negative
… Thames Water (Kemble) Finance PLC	Senior Secured (HoldCo)	C	Stable
United Utilities			
… United Utilities PLC	Senior Unsecured	Baa1	Stable
… United Utilities Water Limited	Senior Unsecured	A3	Stable
… United Utilities Water Finance Plc	Senior Unsecured (Backed)	A3	Stable
Wessex Water			
… Wessex Water Services Finance Plc	Senior Unsecured (Backed)	Baa1	Stable
Yorkshire Water			
… Yorkshire Water Services Finance Limited	Senior Secured (Class A)	Baa2	Stable
… Yorkshire Water Finance plc	Senior Secured (Class A)/Subordinated (Class B)	Baa2/Ba1	Stable
Affinity Water			
… Affinity Water Limited	CFR	Baa1	Stable
… Affinity Water Finance (2004) Plc	Senior Secured (Class A)	A3	Stable
… Affinity Water Finance Plc	Senior Secured (Class A)/Subordinated (Class B)	A3/Baa3	Stable
Portsmouth Water			
… Portsmouth Water Limited	CFR	Baa2	Stable
South East Water			
… South East Water (Finance) Limited	Senior Secured (Backed)	Baa2	RUR-Down
South Staffs Water			
… South Staffordshie Water plc	Senior Unsecured	Baa2	Stable
Sutton & East Surrey			
… Sutton & East Surrey Water plc	Senior Secured (Backed/Underlying)	A1/Baa2	Positive

Source: Moody's Ratings

Endnotes

1 The companies' updated data tables include an RCV uplift of around £4 billion and revenue uplift of £1.8 billion for the sector (in 2022/23 prices). RCV uplift is particularly high for Portsmouth Water, as it will reflect additional totex approved through the cost adjustment mechanism for the Havent Thicket reservoir.

2 Ofwat reflected overall allowances after adjusting for ongoing frontier shift efficiency savings as well as costs that would be adjusted for real price effects. Excluding these adjustments, companies asked for almost £107 billion and Ofwat allowed £91 billion.

3 Risk may not necessarily be additive. Some companies also provided simulated ranges, which are typically narrower than additive ranges due to interdependencies between different cost and performance scenarios.

4 https://www.gov.uk/government/speeches/steve-reed-speech-on-the-water-special-measures-bill

5 https://www.moodys.com/research/Moodys-Ratings-downgrades-Thames-Waters-CFR-to-Caa1-negative-outlook-Rating-Action--PR_496371

6 Please refer to the appendix of our sector report 'Regulated Water Utilities — UK: Ofwat's draft determination increases sector risk', published 14 August 2024.

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