

## **Possible range of economic impacts of Covid-19 on the water sector**

### ***Joint work of Ofwat, Water UK and selected water companies***

- 1.1 Water UK and Ofwat<sup>1</sup> will be working collaboratively to understand better the impact the Coronavirus (Covid-19) pandemic is having and could potentially have in the future on water companies<sup>2</sup>, the risks and opportunities this presents and resulting impacts on customers, investment/investors and the environment.
- 1.2 This note sets out our joint view of the intended purpose of the collaboration and the scope of the work and the terms of engagement.

### **Purpose**

- 1.3 Covid-19 has had a significant impact on UK society and the economy and the effects of the illness and the measures to contain could be felt for some time to come. The impact of Covid-19 on the water sector is at present unclear and requires study. Both Ofwat and the industry have decided to work together in the spirit of open dialogue to explore the issues that may arise and further our collective understanding.
- 1.4 It is not the purpose of this work to arrive at definitive agreed positions about the final impact of Covid-19 nor prescribe how individual companies should respond. The work will, however, seek to further our understanding of how its impacts might manifest themselves and to help identify ways in which the sector could respond most effectively (both of which may vary by company and region). This will inform Ofwat's regulatory response and may provide insights into actions that may be taken by others.

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<sup>1</sup> Water Services Regulation Authority.

<sup>2</sup> This work is intended to focus on, but may not be limited to, the 17 largest water and waste water wholesalers.

## Scope

- 1.5 The joint work will consist of three work streams.
- 1.6 **Work stream 1**, will aim to develop a set of common economic, social and behavioural change scenarios that the sector may be subject to. These scenarios will help to identify the range of possible impacts on the sector.
- 1.7 The macroeconomic element is expected to include a review of emerging and existing expert evidence on macro-economic forecasts. This work stream is also expected to identify key relevant social and behavioural factors which may occur and affect the water sector and source relevant evidence on potential impacts.
- 1.8 These scenarios are intended to form a common basis for comparison and stress testing of various Covid-19 effects.
- 1.9 **Work stream 2** will identify which aspects of water company businesses may be significantly impacted (positively or negatively) in the scenarios developed in Work stream 1 and analyse the impact that Covid-19 has had on these identified aspects to date. It will also consider what mitigation activities the sector has (or could have) undertaken or may still be able to undertake.
- 1.10 There will be no boundary set on the number of factors that may be considered but neither will it aim to be exhaustive – if an issue is considered by either Ofwat, Water UK or the participating water companies to be important, it will be investigated.
- 1.11 This work stream will also aim to capture any opportunities that may arise to do things differently and deliver improvements for customers, opportunities for investment/investors and/or enhancements to the environment. The work will also identify where gaps in evidence exist and any actions required to close those gaps.
- 1.12 **Work stream 3** will look to estimate how companies may be affected under the scenarios developed in Work stream 1. This will be done both on a conceptual basis, and through engagement and testing with selected water companies taking into account company specific impacts. The purpose of this work is to identify the different responses that may be required by companies (including options that the water companies have not considered) to reduce the negative effects attributable to Covid-19 and to maximise any potential gains. This work will recognise that price controls are set with an expectation that water

companies and their investors will need to deal with changing circumstances, including exogenous shocks.

- 1.13 The testing undertaken will provide useful insight into how the participating companies might respond in different scenarios. It will not be assumed that such a response would be the only possible one by that company or preclude that a different company might choose a different course of action in a similar set of circumstances.

## Engagement

- 1.14 The work will provide an input to, and can be expected to inform, future decisions that either Ofwat, Water UK or individual companies will need to make, although it is understood that it would not be the only evidence relied upon. It is therefore important that engagement facilitates open dialogue and ensures that differences of view are respected.
- 1.15 Ofwat and Water UK have formed an Advisory Group of 4-5 representatives each from industry and Ofwat with the former chosen to reflect the diversity of companies, including a water-only company. The Advisory Group will oversee all three work streams and will seek to develop a common understanding of the above issues although views among individual members may vary. Each member of the Advisory Group will have equal ability to comment on each work stream. Ofwat and Water UK will have access to all information collected during the course of the project. Subject to appropriate safeguards to manage information that may be considered confidential, each member of the Advisory Group will have access to the information generated.
- 1.16 Ofwat and the sector will be supported by a consulting firm<sup>3</sup> who will provide expertise and resource, undertaking all three work streams alongside Ofwat, Water UK and the participating water companies.

## Timescales and resource

- 1.17 Ofwat, Water UK and the participating water companies will put at the disposal of the project the relevant experts necessary for the successful conclusion of
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<sup>3</sup> Frontier Economics Ltd.

the project, including those whose role it would normally be to deal with the range of economic impacts of Covid-19 on the business. This is to ensure that the work is not academic in nature and can serve a useful purpose in the future.

- 1.18 While the work streams are set out sequentially, it is expected that there will be a degree of overlap of the work streams being developed and earlier work streams may need to be revisited in light of information uncovered later in the process.