



Water UK City Conference: 2008 Investor Survey

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Value of the survey

- Politicians & Regulators
 - *Improve awareness in decision making*

- Companies
 - *Understand what their existing and prospective investors' think*

- To investors
 - *Non-attributable voicing of views to policy makers*
 - *Enhances own awareness of the issues*
 - *Enhances understanding of other investors' views*



Structure

- Summary
- General financing and valuation issues
- Investor views on risk
- Investor views on the regulatory regime
- Challenges



IN SUMMARY...

- Ofwat and the regime are generally viewed positively by investors
- Water is relatively well placed to continue to finance significant capital programmes
- Investors value: transparency, consistency and communication
- There remain some concerns
 - *Credit market uncertainty*
 - *Risk increased*
 - *Uncertainty around Ofwat's objectives*
 - *More information on how and why*
 - *Some proposals unwelcome*
 - *Need long term view (and evidence) in setting prices*
- Reminder that capital is global

Credibility and confidence are easier lost than won



GENERAL FINANCING AND VALUATION ISSUES

- Premium to RAV
- Prospects for funding
- Perspectives on industry trends



Premium to RAV

- Main drivers of the premium to RAV (36 responses)

	Demand side issues	Stable regulatory regime	Financing out-performance	Opex and capex out-performance
Not at all	6%	6%	0%	6%
Occasional relevance	6%	8%	3%	36%
Relevant determinant	14%	17%	22%	39%
Significant determinant	33%	28%	53%	17%
Dominant determinant	42%	42%	22%	3%

- How will the premium move over the next five years? (34)

- 53% - *premium will decrease*
- 29% - *stable*
- 18% - *unsure or no view*



Prospects for funding I

- How does the current average cost of debt finance compare to 2004-05? (36)
 - *53% higher; 17% similar; 25% lower; 6% no view*

- Do investors have concerns for long term funding of the water industry? (36)
 - *36% yes; 61% no; 3% no view*

- Can you conceive of circumstances in which debt markets may not provide all the remaining funds needed by water companies? (36)
 - *67% yes; 31% no; 3% no view*

- What are the prospects for the cost of finance for the next five years compared to current levels? (35)
 - *Difficult to predict - hence a mixture of views*



Prospects for funding II

- Expect rights issues or dividend cuts over the next five years? (35)
 - *40% yes; 40% no; 20% no view*
 - *Similar between debt and equity*

- What would be your reaction be? (35)
 - *20% positive; 23% neutral; 46% negative; 11% no view*
 - *Debt more positive (36%) than equity (11%)*

- Do you think such issues will be a major source of funds? (35)
 - *9% yes; 86% no; 6% no view*
 - *Similar views debt vs equity*



Perspectives on industry trends

- Does the type of equity owner affect debt investment decision? (26)
 - *70% (debt only) yes*

- Attitude towards higher gearing (36)
 - *Mixed – 28% positive; 42% neutral; 25% concerned; 6% no view*
 - *Equity (41%) more positive than debt (17%)*

- Attitude towards trend of more water companies being held privately (36)
 - *Mixed – 31% positive; 31% neutral; 31% concerned; 8% no view*
 - *Equity positive (61%) and debt negative (50%)*

- How important is it for quoted equity to continue to play a part in financing water companies? (35)
 - *Mixed – 23% not important; 29% marginally important; 26% important; 23% very important*
 - *35% equity not important vs 8% debt*

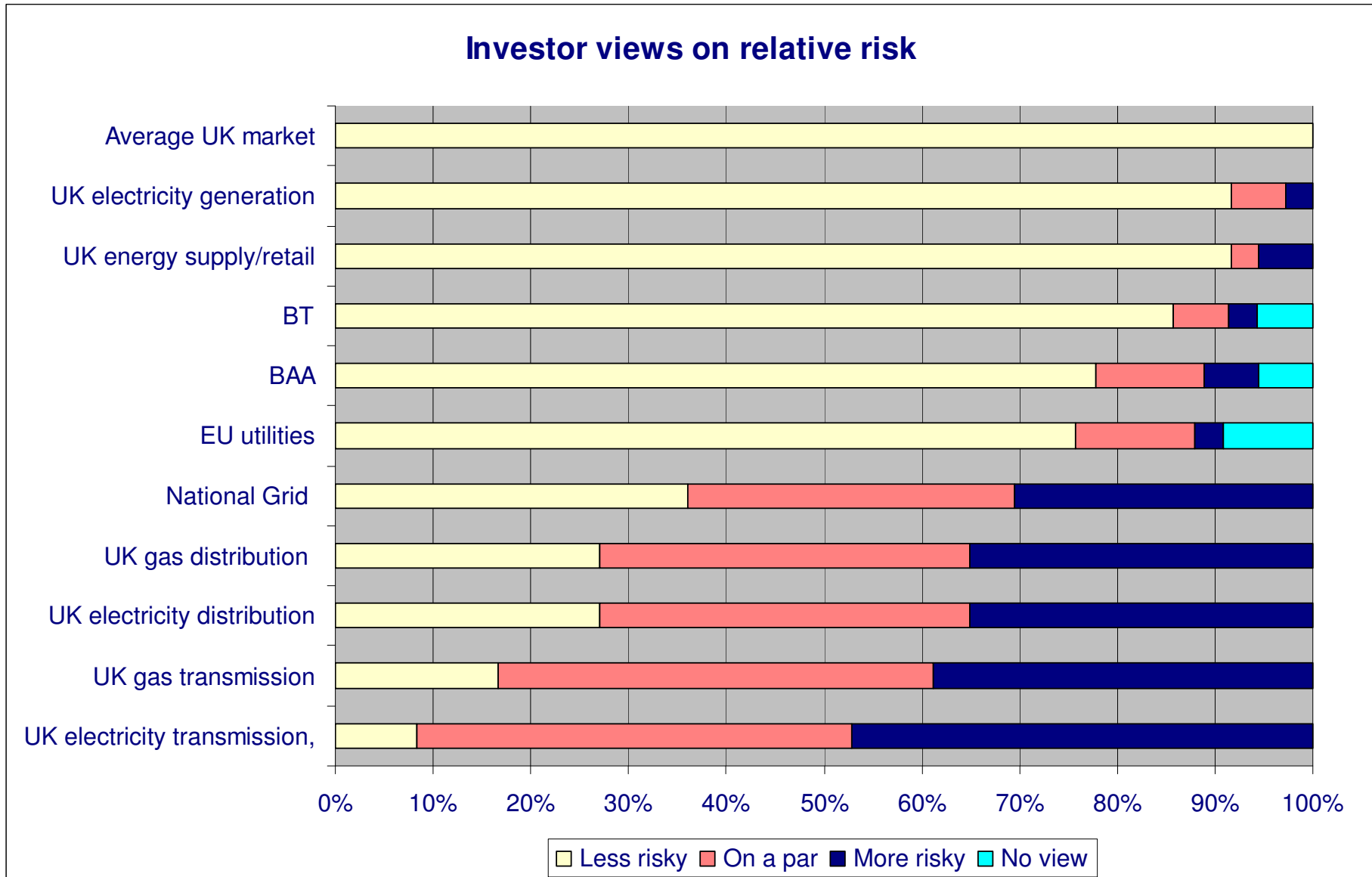


INVESTORS VIEWS ON RISK

- Relative risk
- Key risks and changes since PR04



Relative risk





Key risks and changes since PR04

- Key risks for water companies? (37)
 - 78% management (35% 2003)
 - 78% regulation (61% 2003)
 - 59% force majeure (37% 2003)
 - 49% political (29% 2003)

- 72% rated regulation as the top risk; 20% management (19)

- How have the following risks changed since PR04? (34)

	Increased	On a par	Decreased	No view
Political	43%	43%	11%	3%
Regulatory	57%	26%	17%	0%
Management	26%	46%	29%	0%
Force Maj.	41%	53%	6%	0%



INVESTORS VIEWS ON THE REGULATORY REGIME

- Ofwat's objectives and proposals for PR09
- General views on the regime



Ofwat's objectives (20)

- What is Ofwat trying to achieve at PR09? Has this changed since PR04?
 - Don't know*
 - No change*
 - Change*



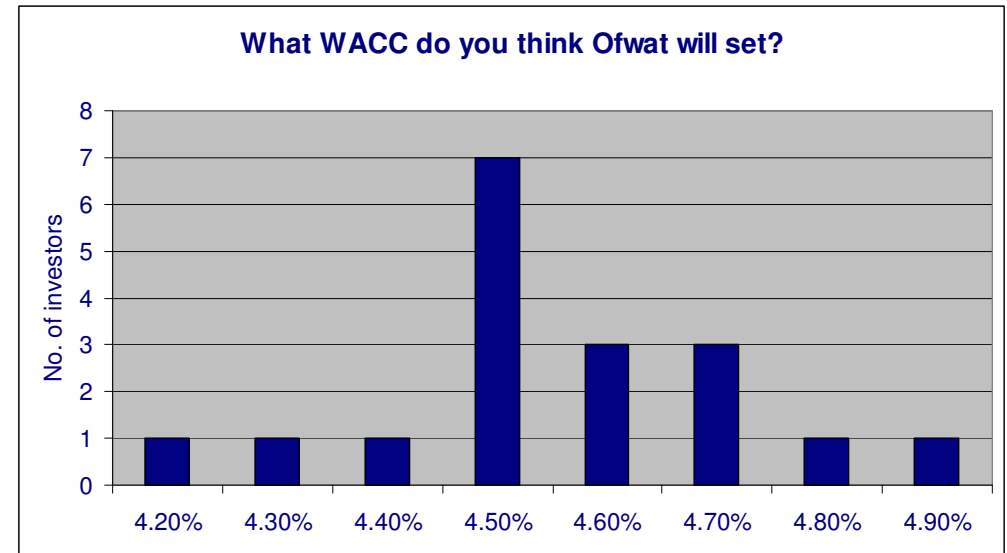
Ofwat's methodology consultation (36)

	Summary	Posit	Neutral	Neg	Need info	No view
Ofwat's methodology consultation	Slightly -ve	28%	28%	36%	na	8%
Revenue corrected price control	+ve	58%	11%	19%	8%	3%
Assume a % of IL debt	Slightly +ve	33%	25%	25%	14%	3%
Menu regulation	Mixed / info	22%	11%	25%	39%	3%
No SCP on WACC	Slightly -ve	17%	29%	31%	9%	15%
Removal of current NIs	-ve	17%	25%	47%	6%	6%
No need for financeability uplifts	-ve / info	14%	19%	31%	31%	6%
Shorter term evidence for WACC	-ve	14%	6%	64%	14%	3%
Link WACC to market measure	-ve / info	11%	6%	56%	28%	0%
Ofwat's competition proposals	-ve	8%	11%	58%	19%	3%



Cost of capital

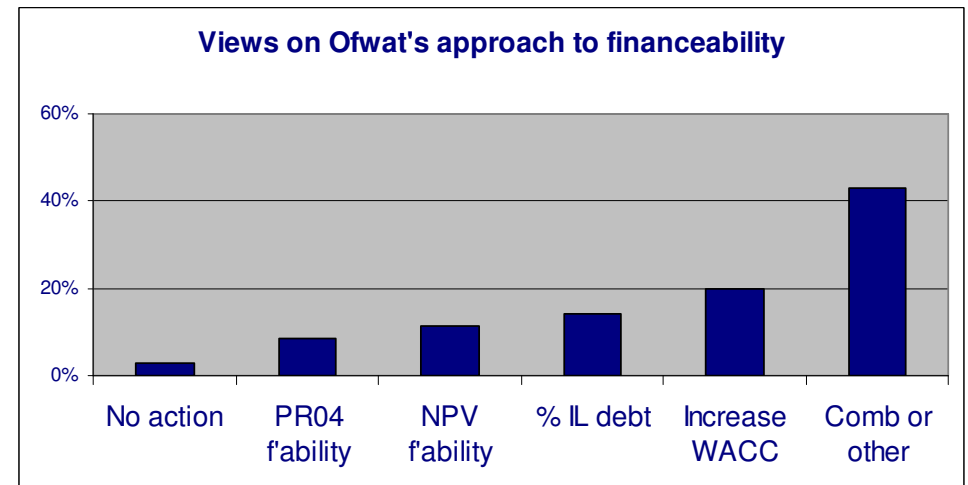
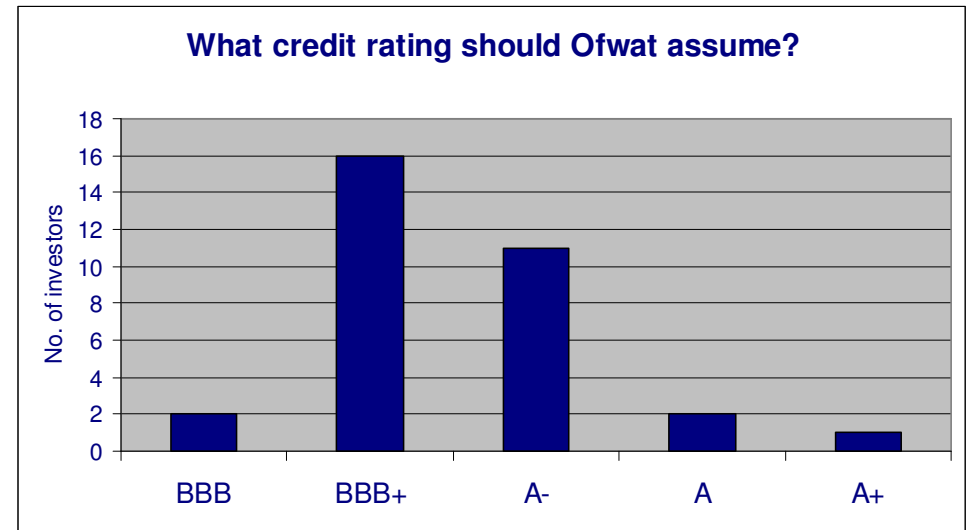
- What WACC do you require Ofwat to set?
 - *Difficult question*
- What WACC do you think Ofwat will set? (18)
- What level of gearing should Ofwat assume? (27)
 - *89% between 55 - 65%*
 - *11% between 66 - 70%*
- In future should the regulator continue to apply the small company premium? (26)
 - *35% Yes; 23% No; 42% No view*
 - *2005 70% Yes*





Financeability

- What credit rating should Ofwat assume? (32)
 - 97% take action
- Ofwat response to regulatory package breaching key financial ratios (35)
 - 97% take action
- Should Ofwat set prices consistent with rating agency views of investment grade? (34)
 - 85% yes; 15% no





Competition

- What form of competition would be desirable? (36)
 - *58% negative on Ofwat's proposals*
 - *Very limited support for wholesale (10%) or retail (7%) competition*

- What do you think of the water merger regime? (35)
 - *69% would like to see change; 8% status quo; 22% neutral*
 - *2005 40/30/30*



Challenges

- How should regulation evolve given changing ownership; capital structures and public policy?
- To what degree is short term market evidence (credit boom/crunch) useful in setting prices for the long term?
- Will Ofwat's proposals lessen transparency and market understanding? Will this affect companies' cost of capital?

Credibility and confidence are easier lost than won