Kirstin Baker

Chair

The Competition and Markets Authority

The Cabot

25 Cabot Square

London E14 4QZ

22nd April 2025

Dear Ms. Baker,

Water PR24 price redetermination – CPP Investments' response to the CMA's call for third party submissions

I am writing to you on behalf of the Canada Pension Plan Investment Board ("CPP Investments") in response to the CMA's Call for third party submissions regarding the Water PR24 price redeterminations. This submission does not aim to delve into the technical aspects of Anglian Water's ("Anglian" or the "Company") Statement of Case. Instead, I wish to provide a broader perspective from a global equity infrastructure investor on the investability of the UK water sector and highlight the key challenges we believe arise from the PR24 Final Determination.

CPP Investments as a global infrastructure investor

CPP Investments is a global investment management organisation that invests the funds transferred from the Canada Pension Plan ("CPP") that are not needed by the CPP to pay current benefits, with a mandate to maximise returns without undue risk of loss. Our purpose is to help provide a foundation upon which more than 22 million Canadians build their financial security in retirement. Operating autonomously from government, we have an investment-only mandate, purposefully unencumbered by political direction. Our unique governance structure distinguishes us from a sovereign wealth fund.

As of December 31, 2024, the Fund had ~C$700 billion (£377 billion) of assets under management across eight global offices. The European region accounts for 19% of the Fund, equivalent to C$136 billion (£76 billion). CPP Investments opened the London office in 2008 and since then it has grown to be the largest global office outside Canada, with approximately 250 employees. CPP Investments currently has ~C$33 billion (£18 billion) invested in the UK with 20 investment strategies operating out of London. The Fund is projected to reach, in nominal terms, C$2.0 trillion (£1.2 trillion) by 2040 and we expect our UK investments to increase in line with the overall trajectory of the Fund.

Since 2006, CPP Investments has been the largest shareholder in Anglian Water, with a 32.96% stake. We invested in Anglian Water because we were attracted by the opportunity to invest in a company that at the time benefited from a stable regulatory framework, long term investment requirements and the ability to generate predictable long-term cash flows. During our 19 years of ownership, we have actively supported the management team's strategic vision for the business, as endorsed by Anglian customers in various forums. This includes making significant additional investments beyond our regulatory commitments and reinvesting returns from operational outperformance back into the business.

The investability challenge of the PR24 Final Determination

PR24 marks an inflection point in the UK water sector, with a significant shift towards growth in investment in Regulatory Capital Value ("RCV"). The Final Determination ("FD") for Anglian Water includes an unprecedented Totex plan of £11 billion (real 2022-2023 prices), an increase of >50% from the prior regulatory period. To fund this, Ofwat's PR24 FD business plan effectively requires Anglian Water to raise £306 million of new equity into the business while existing investors are required to forego £1.5bn of cash dividends[1] to support business growth.

A "zero-dividend" dynamic represents a fundamental shift towards a higher risk investment proposition for infrastructure equity investors like CPP Investments. However, rather than recognising this, Ofwat has set an allowed Return on Regulated Equity ("RoRE") of 5.10%, which in nominal terms is below other regulated sectors globally that we perceive as having lower risk profiles, including electricity transmission and distribution in Great Britain and Italy, and energy and gas utilities in the United States. Moreover, this low headline return is unlikely to be achievable due to the PR24 FD carrying significant asymmetric risks with a skew to the downside, such as via excessively punitive Outcome Delivery Incentives ("ODI"), as laid out in detail in Anglian's Statement of Case.

In this context, we firmly believe that the balance of risk and return in the FD is fundamentally mis-calibrated and insufficient to compensate equity for the underlying risks of the investment proposition. This is a continuation of the mistakes made during AMP7, where most of the companies were not able to achieve the headline allowed return due to a combination of Totex allowance overspend and ODI net penalties. This dynamic is even more relevant amidst the current macro-economic environment characterized by higher interest rates and intense competition for infrastructure capital in the UK and globally.

Underfunding of Base expenditures despite challenging performance commitments

As the largest shareholder of Anglian Water, we acknowledge the need for significant operational performance improvement and support the management team in achieving these targets. However, we believe the PR24 Final Determination fails to provide the necessary Base expenditure allowances for the company to meet these performance commitments.

While it is crucial to set allowances that incentivize efficient operating performance, Base expenditure allowances should enable companies to manage their operations and undertake essential asset maintenance. Ofwat's current approach relies on retrospective models to determine allowances, while simultaneously increasing deliverables from the already stretched base envelope. This has led to structurally embedded underfunding of base operations and capital maintenance activities across multiple AMPs.

As a result, we estimate that the FD leaves Anglian with c. £500 million of unfunded Base expenditures, severely compromising its ability to manage capital maintenance risks, especially when combined with

[1] Based on the PR24 notional capital structure - 55% ND / RCV. Net equity injection based on Notional equity of £1,797 million minus dividends of £1,491 million.

the restrictive effects of the ODI and Performance Commitment Deliverable regimes which Anglian anticipates will result in c. £240 million of penalties. This situation has tangible impacts on customers and resilience, including increased risk of critical asset failure, inability to meet expected performance improvements, and disproportionate costs for future customers to remedy past underfunding.

Unnecessary complexity of the regulatory framework

As investors, we view the UK water regulatory framework as among the most complex globally. We believe the regime must be simplified and stabilised if the sector is to be successful in the global competition for capital, noting the Ofwat forecast £12.7 billion of new equity will be required over the 2025-30 period.

Instead, PR24 further complicates an already needlessly esoteric system. New mechanisms like prescriptive price control deliverables and adjustment mechanisms compound already complex and overlapping incentives via ODIs, cost-sharing, and clawbacks, reducing flexibility for management to allocate funds efficiently and effectively. From an investment perspective, the unnecessary complexity of the regulatory model with a multitude of competing parameters makes forecasting financial and operational outcomes extremely challenging, further increasing risk and lowering our confidence that allowed returns may be achievable.

We support a move toward a simpler, outcomes-focused regime that embeds asset health in core funding and provides proportionate incentives to companies. Without simplification, regulatory risk will remain a barrier to the equity investment the sector urgently needs, with companies focused on near term compliance over long-term resilience and delivering for customers.

Conclusion

We are proud of our investment in Anglian Water and remain keen to support the business to drive better outcomes for customers, the environment and other stakeholders, while ensuring a reasonable return on investment in the best interest of CPP Investments contributors and beneficiaries. However, the extent of our support will ultimately depend on the balance of risk and return of the investment proposition and how this compares to alternative investment opportunities globally.

As it stands, at a point in time when new equity is required to be raised to fund the business, the FD falls some way short of representing a sufficiently attractive investment proposition for experienced infrastructure investors such as CPP Investments.

As you progress with the FD redetermination, we trust you will carefully consider the issues raised in this submission to ensure a fair and balanced regulatory outcome — one that reflects the interests of both current and future stakeholders, while safeguarding the long-term investability of the sector.

Yours sincerely,

[redacted]

James Bryce

Managing Director, Head of Infrastructure

CPP Investments