

Competition and Markets Authority
The Cabot
25 Cabot Square
London E14 4QZ

By email: waterPR24references@cma.gov.uk

10 June 2025

Dear CMA,

RE: Water PR24 Redetermination References – Approach and prioritisation - Third Party Submission

- 1.1 We write to you as the holders of 100% of the ordinary shares of HDF (UK) Holdings Limited, the holding company of South East Water Limited (**South East Water**), in response to the CMA's published consultation regarding its approach and prioritisation in relation to its work on the PR24 redeterminations.
- 1.2 The purpose of this letter is to provide context which we ask the CMA to consider, in its approach to ensuring an appropriate balance of risk and return, which allows for the overarching financeability and investability of the price determination. In turn, this is closely linked with determining the weighted average cost of capital (**WACC**) during the course of the PR24 redetermination process.

2 Backgrounds of the shareholders

- 2.1 Utilities Trust of Australia (**UTA**) is an open-ended core infrastructure fund for institutional investors with a long-term investment horizon and a low-to-moderate appetite for risk. UTA's portfolio is utilities focussed, with assets in transport, energy, water and data infrastructure in Australia and the United Kingdom.
- 2.2 NatWest Pension Trustee Ltd (as trustee for the NatWest Group Pension Fund (Main Fund Section)) (**NatWest Pension**) is a corporate pension fund with a portfolio of over £33.6 billion, invested across multiple sectors.
- 2.3 Desjardins Group (**Desjardins**) is the largest cooperative financial group in North America, with total assets of CAD 470.9 billion. Its 25% stake in South East Water is held through three entities: Régime de rentes du Mouvement Desjardins, a private pension fund serving 86,000 participants; Desjardins Financial Security Life Assurance Company, the group's life and health insurance arm serving over 5 million Canadians; and Certas Home and Auto Insurance Company, a leading provider in the home and auto insurance market.

3 Use of CAPM model

- 3.1 We note the CMA's intention to continue to use the Capital Asset Pricing Model (CAPM), subject to cross-checks, as its primary model in relation to the cost of equity.¹
- 3.2 While we agree that the CAPM model is an important tool, we have concerns around the weight placed on it in determining the cost of equity, and the adequacy of cross checks used. We believe such models should be considered in the context of the broader economic environment, having regard to the implications on the financeability of a company in practice. The CMA's PR24 redeterminations will have a significant impact on the financeability of South East Water as well as the wider water industry.
- 3.3 As investors, we regularly use a number of tools, including the CAPM model, in determining where to invest. However, ultimately, we would take a total view on associated risk and expected return and how that compares to international alternatives.

4 Attracting new capital

- 4.1 In assessing the different models put to the CMA, we ask that the CMA also consider the overarching context and the real-world implications of miscalibrating the cost of capital.
- 4.2 In order to meet the PR24 FD outcomes, water companies will need to attract significant new investment. However, PR24 FD introduces an inflexible investment program due to price control deliverables and exposes companies to significant penalties under the outcome delivery incentive framework. As a result, the risk associated with PR24 FD is disproportionately high compared to the allowed return and skewed to the downside, making it unattractive compared to other available investments.
- 4.3 Moreover, the FD fails to take into account company specific characteristics and, in turn, South East Water does not have a reasonable prospect of achieving the allowed return. In combination, this makes the water sector – and South East Water in particular – unattractive compared to other available investments or uses of capital. In comparison, in particular when taking into account the expected penalties arising from the PR24 FD, investors could make equivalent or higher returns, with much less risk exposure, by buying gilts or investment-grade corporate bonds.
- 4.4 The decision to make a new investment in a company or sector is fundamentally different to the decision by investors to protect the value of their existing investment. If we did not already have significant investments in South East Water, we would not allocate capital to the water sector (including South East Water) at this time based on the PR24 FD. It is important that the CMA understands the distinction between these two different scenarios when determining the cost (and likely availability) of capital.

¹ CMA, *Water PR24 redetermination references – approach and prioritisation*, page 21, [81].

5 Recent equity raises

- 5.1 We understand that Ofwat views South East Water's recent equity raises as indicative that the PR24 FD is financeable.
- 5.2 However, our participation in the recent equity raises by South East Water was driven by the need to preserve the company's financial resilience and to protect our existing investment in the company, in light of changes in rating agency guidance and rising levels of risk in the sector. These methodological changes stem from growing concerns about the stability and predictability of the regulatory regime, which has directly raised the threshold for maintaining credit ratings across the sector.
- 5.3 Our decision to defend our existing investment should not be interpreted as an endorsement of the PR24 Final Determination, nor as an indication that we consider it to be financeable.

6 Next steps

- 6.1 We are grateful for the opportunity to provide our views on the CMA's proposed approach and prioritisation in relation to PR24 and would be happy to engage further with the CMA in relation to the issues raised in this letter.

Yours sincerely,

UTA International Holdings 1 Pty Ltd

[Redacted signature]

NatWest Pension Trustee Limited as trustee of NatWest Group Pension Fund, Main Section

[Redacted signature]

Head of Legal, Compliance & Operational Risk

[Redacted signature]

Chief Executive Officer

Régime de rentes du Mouvement Desjardins

[Redacted signature]

Manager and Head of Infrastructure Investments

[Redacted signature]

Director Infrastructure Investments

Desjardins Financial Security Life Assurance Company

[Redacted signature]

Manager and Head of Infrastructure Investments

[Redacted signature]

Director Infrastructure Investments

Certas Home and Auto Insurance Company

[Redacted signature]

Manager and Head of Infrastructure Investments

[Redacted signature]

Director Infrastructure Investments