

## **WATER COMPANIES MUST PROVE THEY ARE REALLY LISTENING TO CUSTOMERS**

It is clear from water companies who shared best practice at a water customer conference in Birmingham in January that industry investment in customer communications, engagement and research has increased beyond anything delivered during the 2014 Price Review or before.

Some companies are now using different communication tools alongside traditional consultation channels to engage a larger number and more diverse range of customers in their business plan proposals. For example, we are already seeing companies segmenting their customers based on attitude and use of interactive tools.

The benefit for companies is that real dialogue produces better informed feedback, which companies can use to produce plans that really do improve customer satisfaction and trust.

It is only a few months before water companies submit their 2020-25 business plans to regulator Ofwat. From a consumer perspective, what should we expect companies to do with their plans so that the outcome of this price review can be regarded as a good deal for customers?

### **Low and acceptable bills, even after inflation**

In December 2017, Ofwat published its final methodology for how it will assess business plans and set price determinations next year for the 2020-25 period. Part of this saw Ofwat set an assumed cost of capital (the assumed cost companies incur for raising finance to deliver investments) of 2.4%, the lowest the sector has seen. This is welcome news for customers as the cost of returns to shareholders and interest to lenders can take up to a third of the average customer bill.

In this context – and with Ofwat set to challenge companies proposed costs in their plans to ensure services are delivered efficiently – we believe there is scope for companies to meet customers' expectations while keeping bills low, even when the inflation that is added to water and wastewater charges annually is taken into account.

While the lower cost of capital may help make this happen, there is a risk that companies could look to offset lower financing costs and a tougher efficiency challenge by looking at other areas of their business plan where they can increase

value for shareholders.

Companies may be tempted to propose greater financial incentives so the rewards are juicier for improving services, or they may look to increase short-term revenue or make claims for exceptional costs that they say are unavoidable. These are all proposals that must be challenged if they emerge.

### **A long-term outlook – serving current and future customers**

While the price review sets price limits for five years from 2020, business plans should be part of a longer-term strategy to address risks to safe, reliable services, both now and in the future.

Future customers should not pick up the tab for a failure to invest in long-term resilience now. However, the pace and impact on bills must be acceptable to customers. We want to see companies striking the right balance on intergenerational fairness and that involves understanding consumers' short and long-term priorities.

### **How the customers' voice should shape plans**

We welcome greater customer engagement, which leads to a better understanding of the diverse and potentially conflicting views of different customer groups. This diversity should be reflected in the plan.

Engaging with customers on what they want and expect can no longer be a one off piece of customer research during a price review. The water sector should mimic the behaviour of truly competitive markets and have an on-going dialogue with those they serve or wish to serve, with new approaches to service trialled, tested and adjusted.

### **Service commitments that customers value**

Business plans should identify and propose long-term outcomes to benefit customers with a range of specific performance commitments that target companies to achieve these outcomes.

In their plans, water companies should ensure that the commitments they propose (such as a targeted reduction in leakage or the number of supply interruptions) should be based on credible evidence of customer requirements and priorities.

### **Helping more vulnerable customers – an opportunity to go further?**

While water companies offer vulnerable customer assistance, for example social tariffs, our evidence shows that over 80% of customers who currently struggle to pay their bills receive no assistance whatsoever.

Indeed, assistance is patchy differs across companies, with some successful schemes close to their limits. Others have a very low profile and therefore low take up by those in need.

Research we conducted in 2013 revealed that many customers did not support the concept of paying a company a reward, what many saw as 'doing the day job'. For the 2019 Price Review, Ofwat has increased the overall size of the ODI rewards that companies can propose.

We expect companies to engage with customers to see whether they agree with the principle of these incentives and, if they do, financial rewards should only apply for service improvements where a company is seen to have reached an exceptional level of performance, reflecting areas of the service customers view as a priority.

Without customer support, the potential bill increase from rewards, on top of inflation, is likely to generate a negative reaction from customers at a later date.

### Testing the plan for customer acceptability

It's important that final business plans - both the price and service improvement proposals – are tested for customer acceptability.

In 2013, the average level of customer acceptability was 74%. We think the companies should be more ambitious and look to achieve at least 80% customer acceptance.

Water companies should also understand the profile of customers who find the plan unacceptable, understand their reasons for rejecting the plan, and address their concerns.

In conclusion, business plans that are underpinned by great customer engagement, offer affordable and acceptable prices, and act as a milestone toward an ambitious long-term plan to improve the resilience and reliability of services, will go a long way to ensuring this price review is a success for customers. It will boost levels of customer satisfaction and trust.

This is the outcome the Water Watchdog is challenging companies to deliver as they prepare their plans in 2018.