Chapter 8: Financing our plan

8. Financing our plan – aligning risk & return

In this chapter we show that our plan is financeable. We demonstrate that we understand the risks associated with our plan, how we are managing risk and that we are resilient to a range of shocks and stresses over the long-term.

We highlight the need for additional equity to underpin the plan and our expectation that this should result from the strategic review that our current shareholders are undertaking

We present the allowed returns shareholders could receive and the circumstances in which dividends will be paid. We also show how our executives will be rewarded for strong performance.

A. Overview

1. We are financeable on an actual and notional basis after incorporating various components of our PR24 business plan as specified by Ofwat, including TOTEX, official forecasts of inflation, the early view of allowed return and retail margin, PAYG levels and RCV run-off rates.
2. However, our financeability is dependent upon:
    - Additional equity from 2024/25 and into AMP 8 (modelled at £35m) that is expected following the conclusion of the ongoing strategic review (in addition to the £22m receivable in 2023/24);
    - Ofwat's acceptance of our TOTEX plans, and related efficiency assumptions;
    - Retaining a RCV run-off rate of 7% consistent with PR14 and PR19 levels;
    - No downward movement in Ofwat's early view of allowed return and the inclusion of a company-specific uplift to the cost of debt after customer consultation of 30bps; and
    - Effective and efficient debt raising activity from late 2023 onwards, including re-financing of our indexed-linked bond commencing in 2027.
3. On this basis we will be financially resilient throughout the period to 2033 as evidenced by our stress-testing of various Ofwat and company-specific scenarios. All scenarios are met with the exception of two extreme scenarios (a 10% OPEX increase scenario and a RPI uplift scenario) and the combined scenarios. In the extreme and downside scenarios, in order to deliver the planned customer service, the Company may need to retain financial resilience through a combination of suspending dividends or seeking additional equity. Our attractiveness to equity and debt finance would also be enhanced by the actions we are proposing to reduce energy price risk and the probable downside skew in our returns (as detailed in this chapter).
4. Our forecast financial metrics indicate the Company achieving, on average across AMP 8, a credit rating of Baa1 under Moody's assessment criteria, albeit marginally, with as a minimum a solid credit rating of Baa2. Achieving and maintaining a Baa1 credit rating will require the Company to deliver through AMP 8 a solid operational and regulatory performance, TOTEX spend in line with final allowances from Ofwat, continued equity

injections as detailed in our financing plan for 2023 to 2026, and with the absence any severe adverse macro-economic factors.

5. To solidify a Baa1 rating we would require substantially more equity – potentially a further £15m to £20m – given our historic financing structure with its large portion of RPI linked debt.
6. Our dividend and executive pay policies included in Appendix SES065 conform to Ofwat's Final Methodology and take account of recent letters from Ofwat to CEOs across the sector on enhancing dividend and executive pay policies.
7. Our assessment of risk associated with delivery of our business plan identifies an asymmetric RoRE range skewed to the downside, primarily due to the exposure to the large adverse financial impacts of not meeting some of the ambitious performance commitment targets, notably PCC and business demand reductions, and not achieving financing efficiency. The downside skew is probably exacerbated by likely financing underperformance in AMP 8 from our long-term inflation linked bond if inflation remains high. This downside risk can, to some degree, be mitigated via Ofwat accepting our proposals for the introduction of lower ODI rates or additional collars on certain PCs and our company-specific uplift in the allowed cost of debt as part of our determination.
8. This chapter provides full details on our plans and analysis.

B. Financing structure

9. At the time of issuance of this business plan our existing financial structure remains as detailed in our 2023 Annual Performance Report, with net debt as at 31 March 2023 consisting of:
   - Our index linked (RPI) bond (£197.8m);
   - Bank revolving credit facilities (RCF) (totalling £75.0m);
   - Debentures (£0.1m);
   - Short term loan facilities (£22.0m) that have subsequently been repaid; and
   - Cash and short-term deposits (£38.9m).
10. Our credit rating at the date of this submission is Baa2 with a stable outlook, with gearing at c77% as at 31 March 2023.
11. Our primary source of debt financing – the index-linked bond issued in 2001 – has underpinned our investment programme since it was issued and contains special protections which have strengthened our credit worthiness through specific requirements that protect our creditors. These include:
    - Financial covenants on interest cover (ICR), adjusted interest cover (AICR) and gearing – breach of which triggers dividend and cash lock-up clauses to protect the interests of the business;
    - Requirements for funding reserve accounts which provide for one month's operating reserve as well as debt service payment and reserve account;
    - Annual certification of 'no changes' in the regulatory or operating environment that would have a material impact on our ability to comply with covenants; and
    - A special purpose holding company sitting immediately above the Company, with independent directors whose permission is required to make dividend payments to shareholders.

12. In recent years, as disclosed in our previous APRs, this historic financing structure has proved challenging in the face of increased levels of RPI inflation and the lack of flexibility afforded to some degree by the index-linked bond issued in 2001, where archaic covenants – such as AICR – have resulted in an overly complex use of short term capital to mitigate such ratios (not contemplated in the original bond agreement).
13. Recent periods of high inflation have resulted in the amount payable by the Company under this index-linked bond to significantly increase. This is due to recent sharp RPI increases, resulting in increased gearing levels, despite inflation increases to our RCV (with RCV increasing based on the lower CPIH index). Combined with the higher inflation-based pressures on collection of revenues and operational and capital expenditure levels, the increased gearing has reduced the headroom available to raise additional debt within the business in the future.

Financing strategy to 2030

14. Taking into account the above matters, and considering our delivery plans for 2025 to2030, the following financing strategy is being implemented by the Company:
    - **Additional equity** – to fund the ongoing CAPEX programme and address the recent pressures on gearing from inflation our incumbent shareholders have committed £22m of equity into the Company up to March 2024. As of 30 September 2023, £7m has been received, with a further £10m due on 15 December and the remaining £5m due on 15 March 2024. This has enabled the Company to offset, to an extent, the continued pressures on gearing from indexation of the index-linked debt. The £22m committed funding provides resilience in 2023/24 financial year and underpins the entry point into AMP8 however further equity as noted is required to 2030.
    - **Debt diversification and liquidity** – with our revolving credit facilities maturing in July 2024 (£50m) and March 2025 (£25m) we have already commenced refinancing, with a private placement transaction planned to close in November 2023, which will allow for a longer-dated debt instrument to be put in place. Further private placement debt transactions are planned for 2025-30 as part of our AMP8 overall financing, although the timing and amounts of such transactions may be dependent of the results of the strategic review as referenced below.
    - **Refinancing of our index-linked bond** – commencing 2027, our index-linked bond starts to mature at c£50m per year up to 2031. We have therefore incorporated into our AMP 8 financial model refinancing of these amounts with individual debt instruments which will have different maturities, therefore allowing a diversification of debt maturity profiles that we have not been able to achieve since 2001.

Future equity injections – the strategic review of the Company

15. As noted in our APR 2023, our shareholders have commenced a strategic review of the Company, together with the other entities in the East Surrey Holdings (ESH) Group, which may lead to the sale of the Company. This strategic review is envisaged to complete on or before 31 December 2023.
16. The letters of support which provide the £22m of equity in aggregate (referred to above) to the Company between July 2023 and March 2024, will remain in place for the next 14 months up until December 2024. If, as a result of the strategic review the current shareholders are no longer in place, the current shareholders will use best endeavours to ensure that (through the process of transferring ownership) the new shareholders will provide the necessary financial support to the Group. In the event that the strategic review results in the sale of the Company, the Board expects that as part of the process of transferring the Company's water supply licence to a new owner, it would be required to confirm appropriate ongoing funding arrangements.

17. To maintain financial resilience during AMP 8 and beyond (as noted in the financial resilience section of this chapter), further equity support will be required. This is primarily to ensure gearing is maintained at appropriate levels (between 67% and 73%) to ensure we have sufficient headroom under our covenants and ensure financial resilience. Within our AMP 8 modelling, an equity injection in aggregate of £35m has been assumed as a base case. Once the results of the strategic review are known, the mechanism and exact amounts for such an equity injection will be clarified. The modelled debt and equity injections for AMP 8 are provided below:

Table 1: Equity Injections from 2024/25 to 2029/30

£m (nominal)	2024/25	2025/26	2026/27	2027/28	2028/29	2029/30	Total
New debt additions in AMP	0	2	19	18	16	14	69
Equity injections in AMP	10	20	5	0	0	0	35

Source: SES analysis

18. In addition to the assumed equity injection noted above from our shareholders, we have also modelled a £7.6m dividend in 2028/29 from the non-appointed business and reinvested into the appointed business.

19. Our financial model, which underpins our business plan, has taken account of the above matters – current committed equity injections, short-term refinancing, refinancing of our index-linked bond and future equity injections – in the consideration of financeability detailed later in this chapter.

C. Cost of capital

20. In line with the PR24 Final Methodology, in our business plan submission and the associated financial models we have adopted Ofwat's 'early view' of the appointed weighted average cost of capital of 3.29% (CPIH, real) with one deviation to include a company-specific adjustment to the cost of debt of 30bps (resulting in an extra £1.65 on the average annual bill.)

21. We note the wider sector-wide concerns expressed on Ofwat's early view of the cost of capital and have included in Appendix SES046 - Cost of Debt and Cost of Equity, the external reports provided to various companies in the sector by KPMG challenging the cost of capital. We will await Ofwat's views on these reports and associated recommendations as part of the draft determination in 2024.

22. As in prior business plan submissions, we believe a company-specific adjustment to the cost of debt is justified. This is to address the unavoidable additional costs that we incur in raising debt financing due to our relatively small size and the infrequency with which we raise substantive debt. The majority of our customers did not oppose such an uplift. Refer to Appendix SES018 – Customer Research Output Reports – E. SCP, for a report on this cost of debt adjustment, together with the results of our specific customer-based research on this matter. Our evidence for the small company premium is included within Appendix SES005 – Explaining Our Costs – E. SCP Evidence.

D. Tax and pensions

23. Given the funding surplus in our defined benefit pension scheme (at £8.4m at 31 March 2023), as noted in our APR 2023, no pension deficit payments are expected to be required for 2025-30, with the scheme closed to further members. We do not expect to access this surplus during AMP8. Our defined contribution scheme is expected to continue to be funded at rates similar to AMP7.

24. Based upon the assumed levels of revenue and TOTEX spend, tax has been calculated at the standard rate of 25% with an assumption for deferred tax based on the movement in the defined benefit pension scheme and capital allowances driven by the Company's capital investment programme. We have assumed that capital expenditure continues to be 100% allowable for capital allowances and all interest restrictions remain in place, consistent with AMP7.

E. Financeability

Financeability – on an actual basis

25. Our financial modelling for 2025-30 takes account of all the various components specified by Ofwat – including TOTEX, official forecasts of inflation, the early view of allowed return and retail margin, PAYG levels and RCV run-off – and demonstrates that we can generate cashflows sufficient to meet our financing needs.

26. As noted in the Final Methodology, we have assessed financeability on an actual basis before taking account of any reconciling adjustments to revenue for past performance in PR19.

27. The Board's assessment of financeability is performed through the consideration of key financial metrics. While those financial metrics that Ofwat have noted in the Final Methodology have been considered in table 2 below, for our Company the main financeability metrics are those that ensure our compliance with the financial covenants associated with our index-linked bond (in particular a bond gearing limit of 75% at the start of each AMP and 80% during the AMP itself).

28. These covenants generally impose tighter financial constraints than the metrics used by the independent credit rating agencies. Annual compliance with financial covenants is subject to external assurance and certificates of compliance with the broader covenants associated with the index-linked bond are issued annually to the independent Controlling Finance Party. The financial covenants are designed to protect the interests of bond holders from any weakening of our financial strength that might jeopardise annual interest payments or repayments of principal when they become due. This is achieved by control of the release of dividends by a special purpose holding company – with independent directors – between the appointed business and its beneficial owners, and the obligation to certify annual compliance with covenants before dividends are released. Thus, failure to comply with covenants will lead to an immediate and effective prohibition of dividend payments until the situation has been rectified.

29. As noted later in this chapter, we have incorporated RCV run-off rates consistent with prior years.

30. With the additional equity and noting the other key points explained in para. 2 above, the Company continues to be compliant with our bond covenants through the business plan period and up to 2033, in line with the 10-year time horizon in our annual long-term viability statements. These bond covenants, applied when a business plan is submitted, are tighter than those that operate on a year-to-year basis and are specifically designed to ensure that there is headroom to provide financial resilience against unplanned events.

31. The annual ratios shown in our business plan data tables are:

Table 2: Bond Covenants

		Target	2025/26	2026/27	2027/28	2028/29	2029/30
ICR	Ratio	1.60	1.83	1.79	1.66	2.52	1.89
AICR	Ratio	1.10	1.18	1.17	1.19	1.99	1.62
Bond gearing	%	75.0%	66.3%	67.7%	70.3%	71.9%	73.3%

Source: SES analysis
The minimum ratios noted are in accordance with the Collateral Deed of our long-term index linked bond, the ICR ratio required throughout the AMP at the calculation date is to a ratio of 1:1.3, giving a 30 basis point uplift to act as a contingency.

Financeability - on a notional basis

32. Our business plan complies with the obligations of the above financial covenants, which apply to our actual financial structure.

33. Through compliance on these metrics – we are also financeable on a notional basis, whose structure is different in two key areas:

- Assumed gearing – of less than 55.0% throughout the AMP.
- Composition of external debt and the interest rate assumed to be payable on that debt - that Ofwat's notional structure adopts interest rates materially lower than the interest rate actually payable on our historic borrowings.

34. Based upon the notional model where gearing ranges from 51.90% to 52.89%, with an average gearing of 52.45% across the AMP, this results in favourable interest and credit metrics and proves the Company to be financeable on a notional basis.

Targeted credit ratings

35. On an actual basis, we expect that, through the Company's implementation of its business plan on average across AMP 8, we achieve a credit rating of Baa1 under Moody's assessment criteria, albeit marginally, with at a minimum a solid credit rating of Baa2. Achieving and maintaining a Baa1 credit rating will require the Company to deliver through AMP 8 a solid operational and regulatory performance, TOTEX spend in line with final allowances from Ofwat, continued equity injections as detailed in our financing plan for 2023 to 2026, and with the absence any severe adverse macro-economic factors.

36. Further increases in equity would aid to strengthen the case for a Baa1 rating, but with our continued indexation pressures on the RPI linked debt, and the actual cost of raising debt in AMP 8, we estimate that a further £15m to £20m of equity would be required to solidly achieve a Baa1 credit rating.

37. The notional model also indicates credit metrics that would allow a credit rating of Baa1 as an average throughout the AMP.

RCV run-off rates

38. The same RCV run-off rates have been used for both the water resources and the network plus controls, as shown in the Table 3 below.

39. We are conscious that such RCV run-off rates (at c7.0%) remain at the high-end previous sector wide RCV run-off rates and above the limits identified by Ofwat in the Final Methodology of 4.5% for the price controls relevant for our Company.

40. However, we consider the Company's RCV run-off rates appropriate for our Company given:

- **Intertemporal fairness** – the RCV run-off rates are consistent with AMP6 and AMP7 and provide consistency across the generations of customers;
- **Affordability** – by submitting our plan with a 7% run-off versus Ofwat's intended 4.5% there is a c£40m bill impact over the AMP, which we consider based on average bills remains affordable for customers and provides the consistency in bill prices noted above;
- **Upper limits** – the proposed run-off is consistent with PR19 methodologies and provides consistency across the AMPs. In addition, we are proposing £56.0m of enhancement investment in AMP8 and this is set out in our LTDS core adaptive pathway. A reduction of RCV run-off rate from 7% to 4.5% would result in a £41m reduction in revenue which would have a significant impact on our capital programme and in particular our ability to deliver on our enhancement initiatives which are required to deliver a number of statutory and regulatory obligations, increase resilience and deliver service improvements in line with our customers' priorities.
- **Financeability** – the Company's financing strategy has been built over the years on an assumed level of return, if this assumption was to change in terms of run-off rate an estimated additional c£40m additional funding either through debt or equity would be required.

Table 3: RCV Run-off rate across AMP 8

	2025/26	2026/27	2027/28	2028/29	2029/30
RCV run-off rate	7.0%	7.0%	7.0%	7.0%	7.0%

Source: SES analysis

Table 4: Actual RCV Run-off rate in AMP 8

	2020/21	2021/22	2022/23		Average
Closing RCV (£m, nominal, year end prices)	269.8	298.3	334.0		300.7
Run-off rate (£m)	20.7	21.8	22.7		21.7

Source: SES analysis

PAYG ratios

41. We have used the flexibility provided by the PAYG ratio to smooth bill profiles, whilst retaining the same average value for the PAYG ratio over the five-year period. This average value is based on the 'natural' proportion of operating expenditure to TOTEX.

Tables 5 and 6 show the calculation of the 'natural' rate and how this has been modified for the network plus price control to achieve a smoother bill profile. Our water resources PAYG ratio has not been modified in this way, on the basis that modifications to achieve a more acceptable bill profile is appropriate for a monopoly service but could interfere with market signals in the potentially competitive market for water resources.

Table 5: Network plus PAYG ratios

2022/23 price base	2025/26	2026/27	2027/28	2028/29	2029/30
Opex (£m)	36.99	36.60	35.40	34.94	35.10
Capex (incl. DS) (£m)	36.12	41.59	38.40	30.50	29.24
Grants and contributions – Opex (£m)	1.69	1.68	1.66	1.64	1.63
Grants and contributions– Capex (£m)	1.00	1.00	1.00	1.00	1.00
TOTEX (£m)	73.11	78.18	73.81	65.44	64.34
Natural PAYG ratio[1]	50.8%	46.8%	47.9%	53.3%	54.5%
PAYG ratio used in BP	43.0%	44.4%	49.1%	56.2%	58.1%

Source: SES analysis

Table 6: Water resources PAYG ratios

2022/23 price base	2025/26	2026/27	2027/28	2028/29	2029/30
Opex (£m)	6.23	6.16	5.95	5.88	5.91
Capex (£m)	0.63	1.16	1.31	0.36	0.32
TOTEX (£m)	6.86	7.32	7.27	6.23	6.22
Natural PAYG ratio	90.8%	84.2%	81.9%	94.3%	94.9%
PAYG ratio used in BP	90.8%	84.2%	81.9%	94.3%	94.9%

Source: SES analysis

F. Financial resilience

42. As noted above we have set out the key financial ratios for the Company under its index-linked bond covenants and assuming we perform in line with its business plan for the

[1] Natural PAYG rate calculated as ratio of opex to TOTEX, where TOTEX includes developer services spend.

actual capital structure. The adherence to those ratios drive our conclusions on financeability and our targeted credit ratio on an actual basis and – due to the strict nature of the bond covenants – also implicitly build in a level of financial resilience.

43. To demonstrate to the Board our financial resilience, and similar to the work performed for our annual long term viability statement, we have considered under a range of potential downside scenarios our ability to finance our operations and planned investments.

44. We have performed such stress testing up to 2033 (in line with our LTVS 10-year time frame), looking at both Ofwat prescribed scenarios and our own company specific scenarios. Consistent with our annual LTVS work, we assess resilience in terms of the headroom available for us (under our bond gearing covenant) to incur additional borrowing if needed to address liquidity matters arising from such scenarios.

Stress testing – Ofwat scenarios

45. We have tested our resilience (defined by the availability of headroom against gearing) across the various stress scenarios. In all cases (with the exception of OS1 TOTEX underperformance across 5 years, OS5 high inflation and OS9 combined scenario of TOTEX underperformance, ODI penalties and financial penalties) we have sufficient headroom to be financially resilient against these scenarios. In the scenarios noted above which we consider to be severe we would mitigate the impact through additional equity and cessation of dividends.

    A description of the scenarios we have stress tested our plan against can be found in Appendix SES048 – Financial Stress Testing Scenarios.

Stress testing - Company specific scenarios

46. In addition to the Ofwat scenarios we have also tested our plan against our own company specific scenarios as detailed in Appendix SES048. In all cases we manage the scenario within our gearing headroom.

G. Our assessment of risk and RoRE ranges

47. In this section, we describe our assessment of the potential risks we face in delivering our business plan and the resulting Return on Regulated Equity (RoRE) ranges using the high and low cases from data table RR30.

Assessment of risk

48. Our assessment of risk to provide the upside and downside scenarios; the high case (P10) and low case (P90) scenarios[2], has been prepared based on Ofwat's Final Methodology. The ranges presented below are consistent with the components of risk in Ofwat's indicative RoRE range as set out in Appendix 10 to the PR24 Final Methodology and exclude the impact of any uncertainty mechanisms.

49. We produced our estimates using a combination of historical and forward-looking analysis of SES Water-specific and industry wide cost and ODI data, as well as management

[2] Ofwat has asked companies to identify a 'high' case and 'low' case. This is commonly known as a P10/P90 analysis:
- P90 performance: Upside risk is measured at the P90 level which equates to a performance level where there is only a 10% chance of performance being better.
- P10 Performance: Downside risk is measured at the P10 level which equates to a performance level where there is only a 10% chance of performance being worse.

Source: footnote 2 (p. 161): https://www.ofwat.gov.uk/wp-content/uploads/2019/12/PR19-final-determinations-Delivering-outcomes-for-customers-policy-appendix.pdf judgements, where appropriate. In assessing the risks associated with the delivery of our plan, we have been conscious of the need to consider:

- The potential interactions and possible correlations between individual components of risks; and
- That additive ranges of the risk associated with individual incentives and components of the RoRE could exaggerate the true P10 and P90 of our business plan.

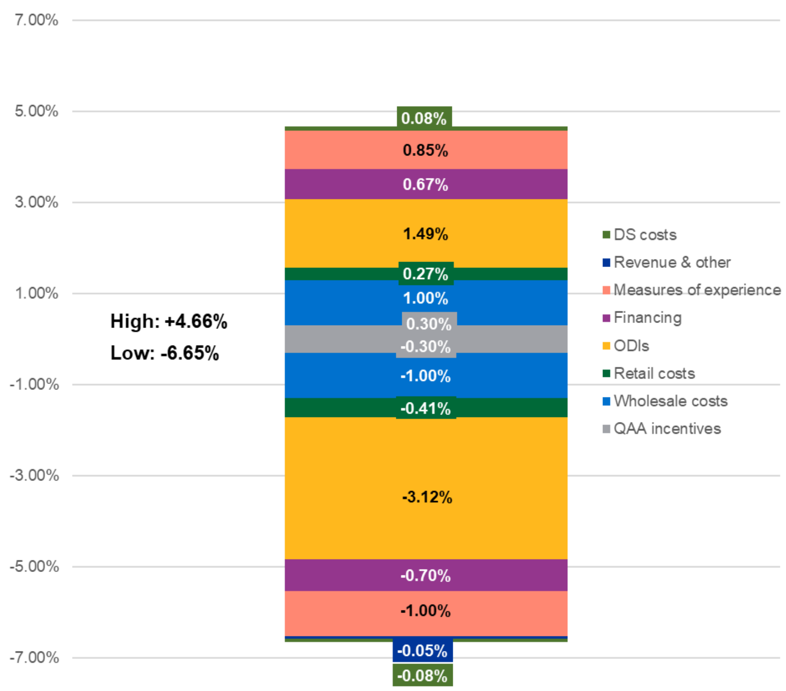
50. We have sought to account for this, in particular via the management judgements we have applied to develop our risk ranges and the likelihood of scenarios of out or under performance, e.g., in individual ODIs, occurring together. The assumptions and analysis that has informed our assessment of RoRE ranges is set out in Appendix SES069 - RoRE Assumptions and Ranges.[3]

Assessment of RoRE ranges

51. In Figure 1 below, we present our PR24 RoRE range (P90/P10) for the notional company. The overall RoRE range for our plan is -6.65% to +4.66%. The range is calculated by adding together the ranges for TOTEX, finance costs, measures of experience, ODIs and revenue mechanisms, and so assume that the highest, or lowest, levels of all the component ranges could be achieved simultaneously.
52. Our P90 range is slightly lower than Ofwat's P90 estimate of +4.80%. However, our P10 estimate of -6.65% is significantly lower than Ofwat's P10 estimate of -4.85%. This difference is driven by our P10 forecast for ODIs, which sits outside the -2% central estimate range that Ofwat adopted in its indicative range for the price control period, together with a wider RoRE range for C-MeX in measures of experience.
53. In our view the overall ODI package remains negatively skewed, driven by the downside risk we consider is associated with the stretching ambitions and performance targets reflected in our plan and how we expect Ofwat may set the PR24 company-specific and common PCLs. In particular, this is driven by the PCC and business demand performance commitments, as described in Appendix SES024 – ODI Design and Calibration and Appendix SES069.

[3] This also acts as our supporting data table commentary for RR30.

Figure 1: SES view of PR24 RoRE risk ranges (P10/P90) – notional company



Source: SES analysis
Note: Ofwat's RR24 RoRE chart tool and charts did not work as intended at the time of preparing our business plan, as such we have produced our own RoRE risk ranges chart. Our chart is formatted in the same way as the Ofwat PR24 Final Methodology Appendix 10 Figure 2.1 (page 11).

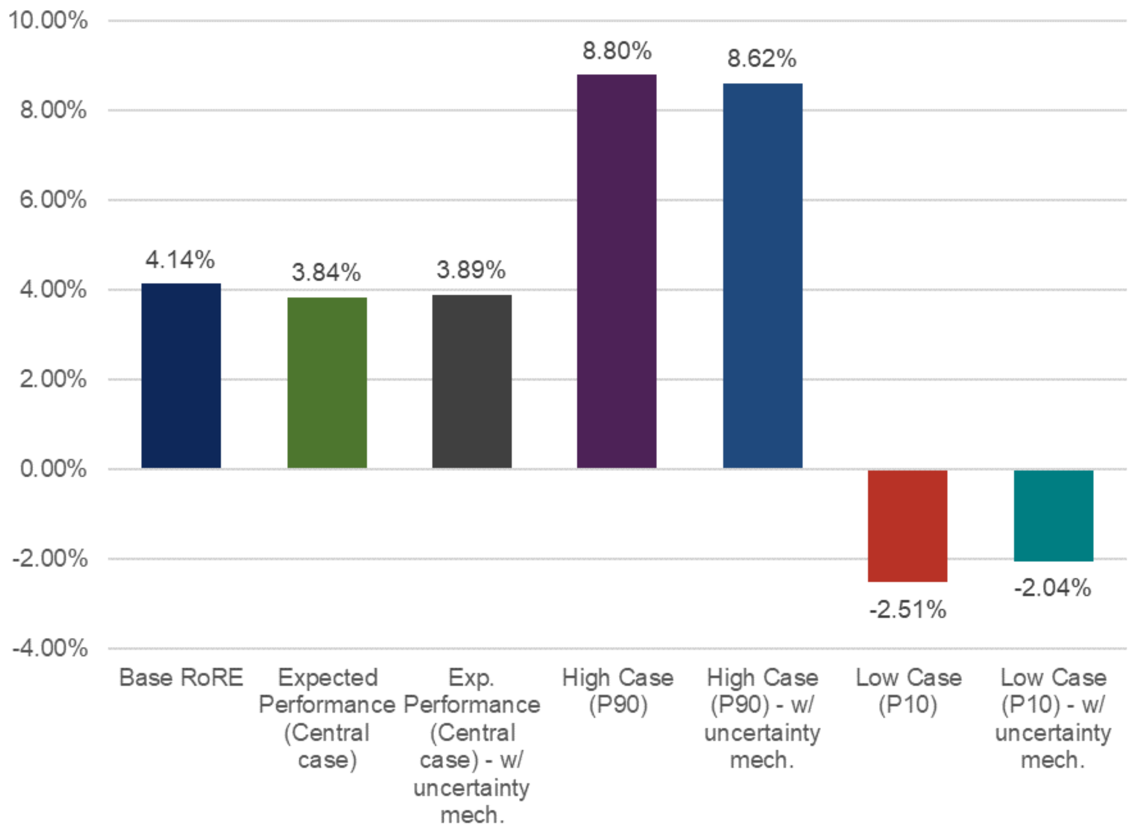
54. Assuming a Base RoRE of 4.14%, we would expect to earn 3.84% under our central case[4], assuming the notional company capital structure. As noted above, this is driven by the ODI package that based on current information we assess to be negatively skewed. Under our P90 assumptions, we estimate we could earn up to 8.80% RoRE[5], whereas under our P10 assumptions, RoRE would be -2.51%[6].

55. If we were to also include our estimate of the possible impact on RoRE of us underperforming the allowed cost of embedded debt under our actual capital structure, we would expect this to have a detrimental impact on the overall RoRE we can achieve, which could be lower than the P10 estimate shown in Figure 1 above.

56. In Figure 2 below, we present a summary of our PR24 RoRE range and the impact of the ODI uncertainty mechanisms we have proposed as part of our business plan submission – see Appendix SES024. In delivering our AMP8 plan, the downside P10 case represents a scenario in which events prevent us from delivering our performance commitments targets and we also incur additional operating and financing costs and results in a negative RoRE of -2.51%. This would be an extreme and unlikely scenario, as we would not generally expect to underperform across all PCs and other areas at once.

[4] 3.84% = 4.14% Base RoRE – 0.30% forecast underperformance RoRE in central case
[5] 8.80% = 4.14% Base RoRE + 4.66% forecast outperformance RoRE in our P90 case
[6] -2.51% = 4.14% Base RoRE – 6.65% forecast underperformance on RoRE in our P10 case

Figure 2: Summary of SES view of PR24 RoRE ranges



Source: SES analysis

57. Where our proposed ODI uncertainty mechanisms – see Appendix SES024 – are applied our:

- Expected Performance (Central case) increases to 3.89%;
- High Case (P90) scenario decreases to 8.62%; and
- Low Case (P10) scenario is reduced by c. 0.47%, to -2.04%.

58. The following assumptions were made to produce this analysis:

- RoRE calculations are post-tax;
- TOTEX sharing factor of 50:50 applied;
- ODI sharing factors applied;
- ±3% RoRE: SES retains all rewards and penalties;
- >3% but <5% (and >-3% but <-5%) RoRE: a sharing factor of 50:50 is applied;
- >±5% RoRE: the sharing factor is reduced to 90%.

H. Alignment of remuneration with delivery for customers

Executive pay

59. Our executive pay policy for 2025-30 is provided in Appendix SES065

60. This executive pay policy has taken into account the feedback from Ofwat's February 2022 and December 2022 letters to the Chairs of Remuneration Committees and will ensure that a clear executive pay policy remains in place ensuring that poor performance overall is not rewarded and allows for transparent reporting of the application of the policy each year in our APRs.

61. Our executive pay policy continues to ensure that the Company's Remuneration Committee can exercise discretion and judgement by reference to overall performance delivery for customers, communities and the environment and performance against specific metrics and stakeholder feedback.

Dividend policy

62. Our dividend policy for 2025-30 is provided in Appendix SES065.

63. The Board noted Ofwat's amendment of Condition P of the Company's licence effective from 17 May 2023 introducing specific requirements for declaring and paying appointed dividends. The Company's previous AMP7 dividend policy was considered by the Board to be overall consistent with these licence changes, but our updated dividend policy for 2025-30 makes explicit the alignment of our policy with such licence changes.

64. As noted on our dividend policy for 2025-30, the following items are built into the design of the policy and therefore considered when applied to potential dividend payments:
    - Performance in meeting our statutory and licence obligations;
    - Commitment to our customers;
    - Performance against regulatory measures;
    - Employee interests and – if necessary in the future – pension obligations;
    - Actual capital structure; and
    - Overall financial resilience.

65. We will continue to be transparent in our future APRs about application of this dividend policy, explaining how dividends declared or paid have been determine and justify any deviations from the policy.

66. Our dividend policy leads to the following level of payable dividends from the appointed business for 2025 to 2030.

Table 7: Appointed dividends payable

£ outturn	2025/26	2026/27	2027/28	2028/29	2029/30
Appointed dividend payable in the year	5.1	6.0	5.9	5.8	5.7

Source: SES analysis

67. These represent a return on regulatory equity averaging 6.5% and an average dividend yield of 4.22% over the period. In line with our dividend policy, these amounts will be assessed in terms of customer delivery and performance at each period and adjusted as deemed necessary.

68. Dividends are paid in June (a final dividend for the previous year, after approval of annual accounts) and December (an interim dividend for the current year, after the interim results announcement). Payments are made to shareholders via Group holding companies and the SESW Holding Company, which was established at the time our index-linked bond was issued in order to provide additional ring-fencing protection for the appointed

business. Release of the dividend from the SESW Holding Company requires the approval of the independent directors established for this purpose.

Voluntary sharing of outperformance

69. Given the comprehensive executive pay policy provided in Appendix SES065, and the Remuneration Committee's view of the effective use of this policy in the past, no voluntary sharing schemes for outperformance are proposed.