Affinity Water: PR24 Business Plan Submission - Commentary

RR1: Revenue cost recovery inputs

The Wholesale WACC component inputs of Equity (RR1.1-RR1.6), Cost of Debt (RR1.7-RR1.12) and Gearing (RR1.13-RR1.18) have been populated in line with Ofwat's 'Early View' published alongside the PR24 Final Methodology. They are also consistent with the inputs in tables RR26 that have been suitably adjusted for retail the retail margin deduction as per the methodology.

PAYG base rates have been set by price control using the approach outlined in the PR24 Final Methodology. This uses the sum of net opex + capitalised IRE as a percentage of total net totex for each year and price control. This is done utilising data from table CW1. No adjustment has been made to the base rate so Total PAYG rate is the same as Base.

Base RCV Run-off Rate has been set for both pre 2025 RCV and post 2025 investment RCV using average historical fixed asset depreciation data by price control taken from published APR tables going back to 2016. Where the calculated rate exceeds the rate cap stated in the PR24 Final Methodology of 4.5%, which is the case for the rate for Water Resource price control at 5.40%, then the cap rate of 4.5% is used; the Water Network price control calculated rate is 4.21% that is within the methodology cap. Future expenditure is expected to be of the same profile as existing assets so we have applied the same rate across pre 2025 RCV and post 2025 investment RCV. No adjustment has been made to the base rate so Total RCV Run-off Rate is the same as Base.

RR2: Totex (cross referenced to cost assessments)

All lines in this table are derived from tables elsewhere in the pack.

RR3: RCV opening balances

The RCV opening balances by price control have been populated in accordance with the guidance by using the populated PR24 RCV Adjustments Feeder Model v2.0 made available by Ofwat through their website. The model takes inputs from data tables PD1 and PD11 calculates opening RCV balances with outputs set to mirror the data table requirements.

RR4: Financing financial model inputs

The notional target gearing percentage in lines RR4.1-4.6 has been set as 55% across the price controls to reflect the notional capital structure assumed within the Early View WACC in the PR24 Final Methodology.

The percentage of debt (line RR4.7-4.8) assumed to be index linked is 33%, as well as RPI linkage (94%) within that, is consistent with the PR24 Final Methodology (Creating tomorrow, together: Our final methodology for PR24 Appendix 10 – Aligning risk and return, Section 6.3.2, page 43).

The interest rates assumed for all the various debt types (lines RR4.39-4.40 and RR4.51-4.52) are based on the allowed cost of debt assumed in the buildup to the allowed cost of debt in the Early View WACC. The rate assumed for index linked debt applies the fisher equation to the nominal allowed cost of debt (using 2% for CPI and 3% RPI inflation amounts). The fixed rate debt uses the nominal allowed cost of debt unadjusted. The rate applied for each year is determined by the mix of new and embedded debt laid out in the PR24 Final Methodology (Appendix 11 – Allowed return on capital, Table 4.8, page 82).

The equity dividends paid (lines RR4.63-4.66) represent the assumptions applied to the actual capital structure modelling. The equity dividends paid for the actual structure company is calculated using the allowed return on capital and then adjusts for any post-financeability true-ups and then deducts the actual nominal debt interest charge which considers debt accretion also. The ordinary shares issued input assumes that fresh equity is injected to prevent an increase in gearing from March 2025 in the case of real increasing RCV and not require a reduction in dividends paid. The injection is assumed to be in year 2 of the AMP as an efficient way to facilitate the requirement for the AMP that also coincides with a significant refinancing of embedded debt.

The Dividend yield percentage (RR4.79) is applied to the notional capital structure to derive notional distributions. We have used a 2% yield input that is half the 4% yield stated in the PR24 Final Methodology (Creating tomorrow, together: Our final methodology for PR24 Appendix 10 – Aligning risk and return, Section 9.4, page 63). Due to the size of the investment program causing material amounts of growth in RCV, we have applied reduction from 4% to 2% in order to finance this investment driven growth. We have maintained the yield floor of 2% (half of the base 4% yield) as we agree with Ofwat's assertion that some distributions are needed to maintain a healthy investor relationship and support financial resilience. The reduction in notional distribution however does not fully fund the RCV investment growth, resulting in notional gearing increasing, so we have assumed notional equity income through the issuance of ordinary shares (RR4.64 – RR4.66) to maintain the notional gearing at 55% in line with the notional structure used in the Early View allowed WACC.

Opening debt, cash and equity balances for April 2025 are forecast using current actual balance sheet data applied through the internal AWL PR24 financial model to project future balances in April 2025.

RR5: Tax inputs

RR5.1-19: Tax opening balances

These are linked from the internal AWL PR24 financial model.

RR5.20-25: Capital allowances

We claim Research & Development Allowance (RDA) for capital expenditure on qualifying Research & Development. It is not possible at this stage to forecast the amount of AMP7 capital expenditure that will qualify for RDA

RR5.26-27: Capital allowances - opening balances

We have forecast the balance of the main Plant & Machinery pool (assets with an expected useful life of less than 25 years) at 31 March 2025 by rolling forward the actual pool balance as at 31 March 2022. We have apportioned the brought forward balance between Water Resources and Water Network Plus on the basis of the RCV split.

We have not disclaimed any capital allowances in previous periods.

RR5.32-33: Tax opening balances,

We have forecast the balance of the main long life asset pool (assets with an expected useful life of 25 years or more) at 31 March 2025 by rolling forward the actual pool balance as at 31 March 2022. We have apportioned the brought forward balance between Water Resources and Water Network Plus on the basis of the RCV split.

We have not disclaimed any capital allowances in previous periods.

RR5.38-39: Tax opening balances

We have forecast the balance of the structure and buildings pool (assets with an expected useful life of 25 years or more) at 31 March 2025 by rolling forward the actual pool balance as at 31 March 2022. We have apportioned the brought forward balance between Water Resources and Water Network Plus on the basis of the RCV split.

We have not disclaimed any capital allowances in previous periods.

RR5.44-46: Capital allowance rates

The following capital allowance rates have been used for the different pools throughout the AMP period.

Main pool at 18%, Special rate pool at 6% and Structure and buildings allowance at 3%.

RR5.47-48: First year allowance rates

Full expensing on qualifying additions to main pool at 100% and 50% on special pool is used for 2025-26 only. As the enhanced deduction is only enacted until 2025-26, we have assumed these will not be available for rest of the AMP periods.

RR5.50-51, 56-57, 62-63, 68-69, 74-75, 80-81, 86-87, 92-93: Capital allowances,

We calculated the percentage allocations for the above lines by analysing gross (i.e. before deducting contributions) new capital expenditure on a project-by-project basis. We analysed the projects in-house, and engaged Chandler KBS, our capital allowances adviser, to review our assessment of the tax treatment of large and/or complex projects.

RR5.98-99: Other tax inputs

We have estimated disallowable expenditure, which is mainly business entertaining, car lease rental restriction and legal fees related to capital transactions.

RR5:104-105: Other tax inputs

There are no other adjustments to taxable profits

RR5:110-111: Other tax inputs

We have no forecast general provisions at 31 March 2025.

RR5: 116-117: Other tax inputs

This includes charge on assets held under finance leases and includes any allowable expenditure relating to leases that were previously accounted for as an operating lease.

RR5: 122-123: Other tax inputs

All P&L expenditure relating to renewals is allowable as a deduction from taxable trading profit.

RR5.128-129: Other tax inputs

No commentary as lines are nil.

RR5.134-135: Other tax inputs

This is the main corporation tax rate of 25% with effect from 1 April 2023 and nominal tax loss allowance of £5m to be utilised against current year losses without any restriction.

RR5.142-143: Other tax inputs

The retail amounts not included in RR9 are included in this table.

RR5.148-149: Other tax inputs

We account for contributions to mains extensions and diversions as deferred revenue, however for tax purposes we treat these contributions as capital items. Contributions are deducted from the long-life asset pool when received, thereby reducing the capital allowances claimed. Amortisation of the deferred revenue is treated as non-taxable income, in order to avoid taxing the contributions twice.

RR5.154-155: Other tax inputs

The tax treatment of all grants and contributions that are taxed on receipt follows the accounting treatment, therefore we do not make any adjustments in the tax computation in respect of these grants and contributions.

RR5.160-161: Other tax inputs

This includes the allowable depreciation on capitalised revenue.

Additional Comments:

We would like to note that in our submitted populated PR24 financial model v21a, published by Ofwat through their website, there is a single error flagged relating to 'Control level tax due check overall' for the amount of (0.130)m. We have investigated this and have discovered that there is an error within the model regarding the check calculation in the Tax tab row 59 relating to tax loss utilisation. The formula does not correctly consider loss amounts below the set tax loss allowance (in this case (4.222)m compared to (5.000)m allowance) and creates an error flag in row 107 when there is not one.

RR6: Post financeability inputs

The inputs for this table are derived from the outputs from the Revenue Adjustment Feeder model. We have operated this model using the default tax switches as pre-populated in that model, and we have selected option 3 to spread the necessary adjustments over the 5 years 2025 – 2030 in present value neutral terms. We chose this option as we considered it likely to lead to the greater stability in customer bill evolution.

RR7: Residential retail inputs

All lines in this table are derived from tables elsewhere in the pack and from our internal AWL PR24 financial model.

RR8: Business retail

As confirmed by Ofwat in their query response ID 403, we have populated the lines for measured and unmeasured charges, based on our forecast of Business Customer numbers and usage.

RR9: Miscellaneous finance model inputs

RR9.130-171: Direct procurement for customers

DPC estimated cost has been taken from consultants working on projects going through DCO and fed this into Gate 5 estimate, with thoughts applied similarly to the DPC need.

Please note that cost 1 is for Minworth project, cost 2 for GUC and cost 3 for SESRO. Due to late start of T2AT project, this project has not been considered, no DPC cost has been reported.

RR9.178-225: Other Income

We include our forecast income in respect of third party damage to our network (line 9.197) and in respect of non price control bulk supplies (line 9.209). These match the costs noted in table CW11. We do not forecast any other income in the period.

Note

There is no commentary for any other lines in this table.

RR10: Allowed revenue

This data table is taken directly from preset outputs within the populated PR24 financial model v21a, made available by Ofwat through their website, following the methodology and guidance.

RR11: PAYG and run-off outputs

This data table is taken directly from preset outputs within the populated PR24 financial model v21a, made available by Ofwat through their website, following the methodology and guidance.

RR12: RCV by control

This data table is taken directly from preset outputs within the populated PR24 financial model v21a, made available by Ofwat through their website, following the methodology and guidance.

RR13: Annual RCV

This data table is taken directly from preset outputs within the populated PR24 financial model v21a, made available by Ofwat through their website, following the methodology and guidance.

RR14: Bill profile

The average customer bill reported in RR14.1 for 2023-24 and 2024-25 are derived from the published PR19 FD average bill amounts indexed to 2022-23 CPIH year average. Bills for years 2025-26 to 2029-30 are outputs of the PR24 Financial Model.

The optional inputs in RR14.2 and RR14.3 have not been utilised and have been left blank.

RR15: Retail margins

This data table is taken directly from preset outputs within the populated PR24 financial model v21a, made available by Ofwat through their website, following the methodology and guidance.

RR16: Financial ratios

We have provided commentary on the lines noted below. For completeness there is no commentary for the other lines in the table.

RR16.37-41: Additional financial ratios provided

In our analysis of actual structure financial metrics we consider the WBS covenants in place. We have included the 3 key metrics of AICR at Class A (includes only Class A debt interest) and Senior (all debt interest) level as well as gearing calculated in an alternative way to regulatory calculations. We have also included our analysis of Moody's AICR and S&P's FFO/Net Debt ratios consistent with our actual rating reporting. These ratios have been prepared in line with our actual structure modelling and consider non-appointed cash flows that sit outside the scope of the Price Review but are relevant to WBS and actual company assessment.

Company proposed ratio A - Actual capital structure – AWL Debt Covenant Class A Conformed AICR – FFO adjusted for RCV depreciation/run-off, working capital, capitalised IRE and capitalised grants and contributions divided by total Class A cash interest and fees less any interest income.

Company proposed ratio B - Actual capital structure – AWL Debt Covenant Senior Conformed AICR - FFO adjusted for RCV depreciation/run-off, working capital,

capitalised IRE and capitalised grants and contributions divided by total cash interest and fees less any interest income.

Company proposed ratio C - Actual capital structure – AWL Debt Covenant Senior RAR (Gearing) – The sum of total outstanding debt balances, including accretion balances on facilities and derivatives, and any interest actual outstanding net of cash and cash-equivalent balances as a percentage of determined RCV indexed to March year end.

Company proposed ratio D - Actual capital structure – AWL calculated Moody's AICR – FFO adjusted for RCV depreciation/run-off and excess fast money divided by total cash interest and fees less any interest income.

Company proposed ratio E - Actual capital structure – AWL calculated S&P's FFO/Net Debt ratio – FFO after net debt interest and accretion of index linked debt divided by the sum of total outstanding debt balances, including accretion balances on facilities and derivatives, and any interest actual outstanding net of cash and cash-equivalent balances.

RR16.56: Further Adjustments to FFO

Adjustments to FFO are mainly for a difference in tax charge applied through the notional structure and the actual structure modelling as a result of differing debt interest amounts applied to profit for tax. The actual debt interest modelled assumptions are built up facility by facility and forecast out across the period and differ to those used in the PR24 Financial Model (Ofwat) based on some notional adjustments to debt levels and mix of fixed and Index linked debt.

RR16.59: Adjustments to RCV run-off

There are no adjustments to notional RCV run-off for the actual structure ratio calculations.

RR16.62: Changes in financing costs due to equity issuance

This is a nil input.

RR16.63: Further adjustments to interest

The Interest Income/(Expense) line fed into this section from RR24 includes accretion on index link debt whereas ratio calculations require cash interest excluding debt accretion. The input adjustment removes the index linked debt brought across from RR24 along with some rounding amendments to 2 or more decimal places.

RR16.66: Adjustments to excess fast money

There are no adjustments to notional excess fast money for the actual structure ratio calculations.

RR16.69: Further adjustments to net debt

Affinity Water's actual structure contains more debt than the notional structure. The adjustment input here reverts the notional structure debt level from the PR24 Financial Model (Ofwat) to the modelled actual debt structure.

RR16.72: Adjustments to RCV balances

No adjustments have been made to RCV balances.

RR16.75: Adjustments to indexation of index linked loans

Affinity Water's actual debt structure contains more index linked debt then the 33% assumed within the notional structure modelling. An adjustment is required to represent the modelled amount of index linked debt based on our actual facilities modelled individually.

RR16.78: Dividends

The Dividends input represents the assumption applied to the actual capital structure. The equity dividends paid is calculated using the allowed return on capital and then adjusts for any post-financeability true-ups and then deducts the actual nominal debt interest charge that considers debt accretion. What remains is free cash flows made available for the actual structure appointee to distribute with the consideration for funding RCV growth dealt with through equity share issuance.

Additional comments

We would like to note that, in our submitted populated PR24 financial model v21a published by Ofwat through their website and is used to populate table RR16, there is an inconsistency within the pre-set calculations in the Output RR16 tab row RR16.11 between the annually calculated ratio and the AMP average calculation. We have investigated this and note that the annual calculated ratios correctly reflect the dividend yield calculation applied to cash flows within the model whereas the AMP average re-calculates a different value for regulated equity to then divide the dividend cash flows by. This different basis of calculation creates this inconsistency that we have left unedited from the published model.

RR17: Financial metrics by scenario

Table RR17 lays out the key financial metrics for the modelled actual company structure with financial stress test scenarios applied as a deviation from the actual structure base case metrics shown in table RR16. The base case assumes allowed revenues as per the notional structure model post financeablity adjustments and expenditure is in line with allowed wholesale totex and retail cost to serve. The company's actual debt structure has been modelled in detail and applied to give accurate annual cash flows for the actual structure company. This has been achieved through producing a detailed actual structure internal AWL PR24 financial model that applies the PR24 Final Methodology and runs in combination with the

PR24 Data Tables and PR24 Financial Model. The internal AWL PR24 financial model contains within it all calculations needed to produce forecasted actual structure financial statements by price control and analysis for financial metrics for the base case (see table RR16) along with the functionality to run scenario overlays to all outputs to allow for stress testing, which is where the inputs to RR17 are derived. The internal AWL PR24 financial model's build, structure and operation is subject to external testing and assurance by KPMG along with the PR24 Financial Model and associated tables. The financeability and financial resilience analysis that forms the basis of external assurance is also rooted in these models.

The basis of calculation of the financial metrics input into RR17 and consistent with those of the base case entered into table RR16 and includes the same voluntary input ratios relating to the actual WBS covenants (Class A AICR, Senior AICR and gearing) in place as well as Moody's AICR and S&P's FFO/Net Debt in line with analysis within our rating reports. In applying the scenarios, the model produces adjusted financial metrics by manipulating the base case financial statements that feed the ratio analysis. The impact of the chosen scenario is enacted in the relevant place within the statements (e.g. an opex downside scenario would increase operating expenditure within the income statement or an ODI penalty would reduce revenues within the income statement both reducing net profit and associated cash flows) to accurately reflect the impact of the scenarios on the calculated financial metrics.

We have decided that our focus of this assessment is look at the financial metrics in line with how rating agencies approach the assessment of credit worthiness. We will be using the benchmarks established within agency assessment criteria for maintaining invest grade rating and this requires a rating of at least Baa3/BBB- to comply. We have deemed it necessary that this minimum level of assessment is attainable after stress has been applied to the company so headroom within the base case is required. The level of headroom we have deemed necessary for the base case is in line with our current credit rating of Baa1/BBB+ that gives 3 notches of surplus headroom within the financial assessment before failure of the minimum investment grading threshold. The Affinity Water actual structure benefits from a rating assessment uplift that reflects the WBS in place and this is in line with how agency currently assess the company. The base case target ratios are 1.30x for a Baa1 AICR and 6.0% for a BBB+ FFO/Net Debt along with gearing levels below 80%. In reality, the entire Affinity Water company (including non-appointed and non-price control cash flows) is what is assessed by agencies, and we have considered this in our voluntary input ratios consistent with base case entries into table RR16. The target metrics are below those of the notional structure would be expected to achieve as it does not benefit from the credit positive assessment of a WBS that are equivalent to a notch up in rating (1.50x AICR, 9% FFO/Net Debt and 72% gearing).

When the stress tests are applied, we expect the company to maintain at least an investment grade rating as a proxy for credit worthiness to access the markets and continue to finance its activities. The benchmark metrics for the actual structure company to achieve Baa3/BBB- are an AICR above 0.9x and FFO/Net Debt above

5% with gearing below 80%. The assessment is conducted across the entire AMP so a perceived failure would require a sustained period of failure to reach benchmarks rather than a single year. We have also considered current evidence that agencies will consider the context of the performance, such as S&P's FFO/Net Debt metric that is currently under pressure from high inflation but not seen as credit negative due to the nature of the regulated inflation hedging on RCV and revenue growth.

The scenarios have been run assuming no management intervention or mitigation. It is reasonable to expect management to react to financial pressures faced by the business as well as utilising projected dividend cash flows to mitigate excess cash downsides and maintaining gearing levels. The scenarios that apply changes to cost of debt and ODI penalties will be considered by our modelled dividend calculation, reducing distributions to counteract the increased costs but all other scenarios impact cash flows unmitigated. In scenarios that model increased costs consistently across the AMP, it is reasonable to assume management have it within their power to partly on wholly mitigate through strategic decision making and business efficiency to handle short term pressures.

Base Case ratios

The base case represents the vanilla business plan submission assuming the actual capital structure post financeability adjustments. These ratios are presented in table RR16 also.

Ratio Outcomes:

		2026	2027	2028	2029	2030
Gearing	%	70.7%	72.6%	74.3%	75.6%	76.4%
Adjusted cash interest cover	ratio	2.39	2.55	1.88	1.76	1.69
Adjusted cash interest cover (alternative calculation)	ratio	2.30	2.45	1.82	1.71	1.63
FFO/Net Debt	ratio	8.7%	8.4%	7.8%	7.5%	7.4%
FFO/Net Debt (alternative calculation)	ratio	8.4%	7.4%	6.2%	5.9%	5.8%
Headroom for reverse stress test to Baa1/BBB+	£m	32	34	27	25	24
Covenant Class A AICR	ratio	2.93	3.61	2.33	2.08	1.99
Covenant Senior AICR	ratio	2.41	2.97	2.05	1.85	1.78
Covenant Combined RAR	%	70.5%	72.4%	74.2%	75.6%	76.5%
Moody's AICR	ratio	2.54	2.51	1.86	1.76	1.70
S&P FFO/Net Debt	%	9.1%	8.1%	6.6%	6.4%	6.2%

Assessment:

The Base Case comfortably achieves the benchmark ratios for Baa1/BBB+. AICR ratios are consistently above 1.30x across the AMP for all iterations of the calculation with £m headroom of £32m to £24m in each year. The headroom for reverse stress

testing in the Base Case and all scenarios has focused on the AICR calculation as the single clearest indicator of financial performance. FFO/Net Debt remains consistently above the 6% benchmark while gearing stays below 80%. We project AMP7 March 2025 closing gearing to be 77.9% with fresh equity to fund AMP8 investment all coming in 2026 resulting in a de-gearing to below 71% to prepare for the AMP's investment programme and increase financial resilience which then increase back up to March 2025 levels after midnight adjustments.

There is a noticeable deterioration of metrics through the AMP, this is due to the large amount of more expensive new debt that is required to fund the investment growth of the AMP above the fresh equity injected. This is compounded by a significant amount of refinancing in AMP8 meaning that the new debt required would make 54.6% of Affinity Water's debt raised in AMP8 by March 2030. With the high cost of debt we are currently seeing, this puts increasing pressure from the AMP's starting position although target ratio head room is maintained. This is also an issue created by the significant deviation from the new debt share of 16.7% assumed in setting the allowed cost of debt in the Early View WACC applied in the business plan.

Scenario assessment summary:

Scenario	WBS Covenants	AICR >0.90x (Moody's)	FFO/Net Debt >5% (S&P)	Gearing <80%	Overall
+10% Totex underperformance each year	PASS	PASS	PASS WITH MITIGATION	PASS WITH MITIGATION	PASS
ODI underperformance 3% RoRE each year applied with a 2-year delay	PASS	PASS	PASS WITH MITIGATION	PASS	PASS
Inflation reduced -2% each year	PASS	PASS	PASS	PASS	PASS
Deflation of -1% years 1-2 then base case	PASS	PASS	PASS	PASS	PASS
10% spike in inflation year 1 along with +2% in CPIH/RPI wedge, then 5% increase for 2 years with +1% in wedge	PASS	PASS	PASS AFTER CONSIDERING INFLATION	PASS	PASS
+20% Increase in bad debt each year	PASS	PASS	PASS	PASS	PASS
New debt cost increased by 2%	PASS	PASS	PASS	PASS	PASS
Financial penalty of 6% of revenue each year applied with a 2-year delay	PASS	PASS	PASS WITH MITIGATION	PASS	PASS
Combination 1 – Sustained poor performance in each year of Inflation -1%, Totex +2%, ODIs 0.5% RoRE and bad debt +10%	PASS	PASS	PASS	PASS	PASS
Combination 2 – Recovery from a massive asset failure & penalties capex +£60m and opex +£20m year 1 then opex +£10m year 2 and +£5m year 3	PASS	PASS	PASS	PASS	PASS

Scenario	WBS Covenants	AICR >0.90x (Moody's)	FFO/Net Debt >5% (S&P)	Gearing <80%	Overall
Combination 3 – recreation of AMP7 covid and cost price pressures by inflation-2% and opex +5% in years 1-2 and inflation +8%, opex +10% and capex +4% years 3-5	PASS	PASS	PASS AFTER CONSIDERING INFLATION	PASS	PASS

The modelled scenarios show a resilient position through the metrics maintaining at least a Baa3/BBB- after identified mitigations and considering agency approach to interpreting ratios in high inflation scenarios. WBS covenants are also compliant in all scenarios so would not restrict the actual company's ability to access new financing in the markets.

Reverse stress testing target and limit calculations are focused on the AICR with a threshold level set at 1.20x for a Baa3/BBB- level. We have assessed that this is the single strongest indicator of operating cash flows within the context of the financial liabilities of the business within each scenario. The ratio features strongly in agency assessments as well as within WBS covenants.

The modelled scenarios are:

1. Totex underperformance of 10% for each year of the AMP applied to both opex and capex

In this scenario we have increased the amount of both operating and capital expenditure by 10% increasing the costs in the income statement, reducing net profit, and cash flow statement, reducing net cash generated, while maintaining revenue allowances at base case levels. The scenario compounds through the AMP as less cash is generated and more new debt is required increasing gearing as well as applying pressure to AICR and FFO/Net Debt. The changes to expenditure also have an impact on the tax for profit calculation and therefore tax payable as well as working capital calculations.

The majority of the risks to the business that we have identified are captured within this scenario. Operational risk from internal and external factors materialise as increase in expenditure to accommodate and maintain service. Weather events, such as freeze-thaw and prolonged dry periods, result in opex underperformance exposure well within the 10% test range. In order to achieve a 10% totex underperformance we believe it would require several severe events to occur simultaneously without mitigating action.

Ratio outcomes:

		2026	2027	2028	2029	2030
Gearing	%	72.1%	75.9%	79.3%	82.1%	84.2%
Adjusted cash interest cover	ratio	1.60	1.62	1.25	1.16	1.11

		2026	2027	2028	2029	2030
Adjusted cash interest cover (alternative calculation)	ratio	1.60	1.62	1.25	1.16	1.11
FFO/Net Debt	ratio	7.0%	6.6%	5.9%	5.6%	5.4%
FFO/Net Debt (alternative calculation)	ratio	6.7%	5.6%	4.4%	4.0%	3.8%
Variance to Base (+/(-)):						
Gearing	%	+1.3%	+3.2%	+5.0%	+6.5%	+7.8%
Adjusted cash interest cover	ratio	(0.79)	(0.93)	(0.64)	(0.60)	(0.58)
Adjusted cash interest cover (alternative calculation)	ratio	(0.70)	(0.83)	(0.57)	(0.55)	(0.53)
FFO/Net Debt	ratio	(1.7)%	(1.8)%	(1.9)%	(1.9)%	(2.0)%
FFO/Net Debt (alternative calculation)	ratio	(1.7)%	(1.8)%	(1.8)%	(1.9)%	(1.9)%
Headroom for reverse stress test to Baa1/BBB+	£m	11	11	2	(2)	(5)
Extent of stretch required to reach limit	%	15.0%	14.8%	10.8%	9.4%	8.2%
Covenant Class A AICR	ratio	2.49	2.50	1.60	1.38	1.30
Covenant Senior AICR	ratio	2.05	2.08	1.42	1.24	1.18
Covenant Combined RAR	%	71.9%	75.7%	79.3%	82.2%	84.4%
Moody's AICR	ratio	1.82	1.71	1.29	1.21	1.15
S&P FFO/Net Debt	%	7.3%	6.2%	4.7%	4.4%	4.2%

Scenario assessment: PASS WITH MITIGATION

The impact of this scenario is a an increase in gearing +7.8% by March 2030, a reduction in AICR by (0.58) to (0.93) and reduction in FFO/Net Debt by (1.7)% to (2.0)% each year. The AMP average AICR is 1.35x well above the 0.90x Baa3 threshold. The AICR threshold to Baa1 is breached in two years with a gap of £(2)m and £(5)m which we deem to be manageable with mitigation to avoid a downgrade. The reverse stress test implies the ability to absorb an unmitigated scenario of 8.2% underperformance to 15.0% that would continue to be at Baa1 levels which implies a strong position. The AMP average FFO/Net Debt (alternative) of 4.9% is marginally below the 5% target and gearing is 84.2% above the upper threshold both due to the increased amount of expensive new debt taken on to cover the cash shortfall within the scenario.

The scenario assumes allowed distributions of £175m are made across the AMP which would likely be forfeited in mitigation to such a scenario reducing gearing by 7%. Incorporating this action would lower gearing well below the 80% threshold and increase FFO/Net Debt by c0.5% (before considering lower interest as a result) increasing well above the lower threshold for BBB-. In addition to this there is significant Non-appointed cash flows (c£8m p.a.) that could be used as a contingent equity support within the corporate entity. A sustained totex underperformance of 10% per year without management action can also been

perceived as overly severe and we would expect management to be able to offset this scenario at least partly.

When considering all factors, our assessment is that the actual structure would be able to maintain investment grade level with ample reserve in further mitigating actions.

2. ODI underperformance of 3% of RoRE for each year of the AMP applied to revenues with a 2-year delay

The impact of this scenario is a reduction in revenues in years 3-5 as penalties applied with a 2-year delay to when incurred. The actual model dividend calculation considers ODI performance so an increase in penalties reduces distributions made and offsets the shortfall in cash flows and reduces the impact to net debt and gearing. The scenario considers the impact on the profit for tax calculation as well as working capital changes driven by the scenario.

Ratio outcomes:

		2026	2027	2028	2029	2030
Gearing	%	70.73%	72.65%	74.19%	75.42%	76.20%
Adjusted cash interest cover	ratio	2.39	2.55	1.13	1.05	1.00
Adjusted cash interest cover (alternative calculation)	ratio	2.30	2.45	1.07	1.00	0.95
FFO/Net Debt	ratio	8.70%	8.41%	5.99%	5.77%	5.64%
FFO/Net Debt (alternative calculation)	ratio	8.37%	7.36%	4.40%	4.14%	4.03%
Variance to Base (+/(-)):						
Gearing	%	-	-	(0.2)%	(0.2)%	(0.2)%
Adjusted cash interest cover	ratio	-	-	(0.75)	(0.71)	(0.68)
Adjusted cash interest cover (alternative calculation)	ratio	-	-	(0.75)	(0.71)	(0.68)
FFO/Net Debt	ratio	-	-	(1.8)%	(1.8)%	(1.7)%
FFO/Net Debt (alternative calculation)	ratio	-	-	(1.8)%	(1.8)%	(1.7)%
Headroom for reverse stress test to Baa1/BBB+	£m	32	34	(3)	(7)	(10)
Extent of stretch required to reach limit	%	3.3%	3.5%	2.7%	2.4%	2.1%
Covenant Class A AICR	ratio	2.93	3.61	1.67	1.37	1.31
Covenant Senior AICR	ratio	2.41	2.97	1.47	1.22	1.17
Covenant Combined RAR	%	70.5%	72.4%	74.1%	75.4%	76.2%
Moody's AICR	ratio	2.54	2.51	1.19	1.12	1.08
S&P FFO/Net Debt	%	9.1%	8.1%	4.9%	4.6%	4.5%

Scenario assessment: PASS WITH MITIGATION

The outcome of the scenario continues to satisfy Baa3/BBB- criteria with minimal AICR and gearing headroom remaining in all 5 years. FFO/Net Debt is pushed below

the threshold but could be mitigated through retaining the remaining forecast £95m of distributions to reduce net debt and improve the ratio above the threshold. The reverse stress testing implies penalties in the range of 2.1% to 2.7% of RoRE would be required to remain within the Baa1/BBB+ AICR rating with further headroom to investment grade thresholds.

3. Inflation 2% below the base case each year of the price review

Inflation is a key driver throughout the price review modelling. Revenues, costs, dividends, debt and RCV are all linked to the underlying inflation assumption and move with it. The inflation sensitivity is an overlay to the single base case assumption so when applying the movement flows throughout the model without impacting assumed allowed determined outcomes (such as allowed revenue). The nature of inflation compounds through time and the scenario overlay considers this with each year's lower inflation in addition to the previous periods.

Ratio outcomes:

		2026	2027	2028	2029	2030
Gearing	%	71.08%	73.51%	75.74%	77.56%	79.04%
Adjusted cash interest cover	ratio	2.38	2.39	1.76	1.62	1.49
Adjusted cash interest cover (alternative calculation)	ratio	2.29	2.30	1.69	1.56	1.44
FFO/Net Debt	ratio	8.65%	8.08%	7.38%	7.05%	6.71%
FFO/Net Debt (alternative calculation)	ratio	10.18%	8.48%	7.12%	6.76%	6.46%
Variance to Base (+/(-)):						
Gearing	%	+0.4%	+0.9%	+1.4%	+1.9%	+2.6%
Adjusted cash interest cover	ratio	(0.01)	(0.16)	(0.13)	(0.15)	(0.20)
Adjusted cash interest cover (alternative calculation)	ratio	(0.01)	(0.16)	(0.13)	(0.14)	(0.20)
FFO/Net Debt	ratio	(0.1)%	(0.3)%	(0.4)%	(0.5)%	(0.7)%
FFO/Net Debt (alternative calculation)	ratio	+1.8%	+1.1%	+1.0%	+0.9%	+0.7%
Headroom for reverse stress test to Baa1/BBB+	£m	31	29	21	18	14
Extent of stretch required to reach limit	%	-83.2%	-14.4%	-9.5%	-7.0%	-4.6%
Covenant Class A AICR	ratio	2.84	3.35	2.15	1.89	1.75
Covenant Senior AICR	ratio	2.33	2.76	1.90	1.69	1.57
Covenant Combined RAR	%	70.9%	73.3%	75.6%	77.5%	79.1%
Moody's AICR	ratio	2.52	2.37	1.75	1.64	1.52
S&P FFO/Net Debt	%	10.9%	9.2%	7.6%	7.3%	7.0%

Scenario assessment: PASS

The outcome of the scenario continues to satisfy Baa1/BBB+ criteria with AICR headroom remaining in all 5 years so more than satisfies the Baa3/BBB- threshold

criteria. The reverse stress testing implies a significant reduction in inflation would be needed to impact AICR and eliminate all available headroom.

Gearing shows the largest impact over the 5 years, increasing by +2.6%, but is not enough to cause concern within the rating assessment with plenty of potential mitigation from potential distributions or targeted operational efficiencies. The actual capital structure is well protected from inflation in the short term, with much of the debt held attached to an inflation index, but through time more fixed rate debt is introduced with re-financing in 2026 and RCV growth funding creating more exposure towards the back of the AMP.

4. Deflation of -1% for 2 years, followed by a return to the base case assumption

The Base Case inflation assumption, that applies OBR inflation forecasts, is not too dissimilar to this sensitivity. Following the current inflation volatility, a period of low/negative inflation is projected to take place. The further downward pressure is captured within the scenario.

Ratio outcomes:

		2026	2027	2028	2029	2030
Gearing	%	70.84%	73.10%	74.77%	75.99%	76.78%
Adjusted cash interest cover	ratio	2.38	2.45	1.86	1.75	1.68
Adjusted cash interest cover (alternative calculation)	ratio	2.29	2.36	1.80	1.69	1.63
FFO/Net Debt	ratio	8.69%	8.21%	7.69%	7.47%	7.34%
FFO/Net Debt (alternative calculation)	ratio	9.18%	8.09%	6.11%	5.85%	5.74%
Variance to Base (+/(-)):						
Gearing	%	+0.1%	+0.5%	+0.4%	+0.4%	+0.4%
Adjusted cash interest cover	ratio	(0.00)	(0.10)	(0.02)	(0.02)	(0.01)
Adjusted cash interest cover (alternative calculation)	ratio	(0.00)	(0.10)	(0.02)	(0.02)	(0.01)
FFO/Net Debt	ratio	(0.0)%	(0.2)%	(0.1)%	(0.1)%	(0.0)%
FFO/Net Debt (alternative calculation)	ratio	+0.8%	+0.7%	(0.1)%	(0.1)%	(0.0)%
Headroom for reverse stress test to Baa1/BBB+	£m	32	31	26	24	23
Extent of stretch required to reach limit	%	-91.2%	-11.6%	-9.1%	-8.6%	-8.1%
Covenant Class A AICR	ratio	2.89	3.45	2.31	2.06	1.98
Covenant Senior AICR	ratio	2.38	2.84	2.03	1.84	1.77
Covenant Combined RAR	%	70.6%	72.9%	74.7%	76.0%	76.8%
Moody's AICR	ratio	2.53	2.43	1.84	1.75	1.69
S&P FFO/Net Debt	%	9.9%	8.8%	6.6%	6.3%	6.2%

Scenario assessment: PASS

As the Base Case assumptions for inflation are not too dissimilar to this sensitivity, the scenario does not have a material impact on metrics. The outcome maintains Baa1/BBB+ levels with headroom, staying well clear of Baa3/BBB- threshold levels.

5. Inflation spike of 10% in year 1 with an increase in the CPIH/RPI wedge by 2%, then years 2 and 3 have higher inflation by 5% with a 1% increase in CPIH/RPI wedge

An extremely sever high inflation scenario showing the effect on the price review outcomes of sustained high impact. Inflation compounds through time and impacts cash flows across the price review modelling so is a material variable.

Ratio outcomes:

		2026	2027	2028	2029	2030
Gearing	%	69.13%	70.11%	71.09%	72.59%	73.54%
Adjusted cash interest cover	ratio	2.41	3.05	2.06	1.85	1.77
Adjusted cash interest cover (alternative calculation)	ratio	2.32	2.94	1.99	1.79	1.71
FFO/Net Debt	ratio	8.92%	9.16%	8.33%	7.90%	7.74%
FFO/Net Debt (alternative calculation)	ratio	-0.95%	4.20%	3.12%	6.20%	6.06%
Variance to Base (+/(-)):						
Gearing	%	(1.6)%	(2.5)%	(3.3)%	(3.0)%	(2.9)%
Adjusted cash interest cover	ratio	+0.02	+0.50	+0.17	+0.09	+0.08
Adjusted cash interest cover (alternative calculation)	ratio	+0.02	+0.49	+0.17	+0.08	+0.08
FFO/Net Debt	ratio	+0.2%	+0.7%	+0.6%	+0.4%	+0.4%
FFO/Net Debt (alternative calculation)	ratio	(9.3)%	(3.2)%	(3.0)%	+0.3%	+0.3%
Headroom for reverse stress test to Baa1/BBB+	£m	36	48	37	33	31
Extent of stretch required to reach limit	%	-90.6%	-12.6%	-12.7%	-12.0%	-11.3%
Covenant Class A AICR	ratio	3.31	4.14	2.68	2.20	2.10
Covenant Senior AICR	ratio	2.69	3.34	2.31	1.93	1.85
Covenant Combined RAR	%	68.9%	70.0%	71.1%	72.7%	73.7%
Moody's AICR	ratio	2.56	2.73	2.00	1.83	1.76
S&P FFO/Net Debt	%	-0.3%	4.7%	3.5%	6.6%	6.4%

Scenario assessment: PASS AFTER CONSIDERING INFLATION

Higher inflation has a largely positive impact on financial metrics for actual capital structure. Gearing is reduced by (2.9)% and AICR ratios are improved. FFO/Net Debt (alternative) ratios are negatively impacted significantly in years 1-3 as additional debt accretion impacts both numerator and denominator within the calculation that ignores the systemic relationship to inflation for the company and industry (i.e. nominal RCV inflation). S&P, who rely on the alternative FFO/Net Debt ratio, have

shown precedent in looking through extreme inflation impact in the current position. Our assessment would not consider this to change and when combined with the recovery of the metric when inflation subsides along with improved leverage and AICR metrics, do not believe it would impact the credit assessment.

The reverse stress testing against the AICR ratio implies a sever downward movement in inflation would be required and the structure is well protected against and benefits from upward inflation.

6. Increase in bad debt by 20% each year over current levels

The Retail price control typically incurs roughly £11m per annum in bad debt charges. This scenario looks at the impact of increased costs relating to increased failed customer debt recovery across the test period of £2.2m. The increase in costs is modelled to impact profit for tax and working capital also to gauge a fuller picture of the impact of cash flows.

Ratio outcomes:

		2026	2027	2028	2029	2030
Gearing	%	70.79%	72.81%	74.60%	75.92%	76.77%
Adjusted cash interest cover	ratio	2.31	2.46	1.82	1.71	1.64
Adjusted cash interest cover (alternative calculation)	ratio	2.30	2.45	1.82	1.70	1.63
FFO/Net Debt	ratio	8.54%	8.24%	7.60%	7.37%	7.23%
FFO/Net Debt (alternative calculation)	ratio	8.21%	7.20%	6.01%	5.75%	5.63%
Variance to Base (+/(-)):						
Gearing	%	+0.1%	+0.2%	+0.3%	+0.3%	+0.3%
Adjusted cash interest cover	ratio	(0.08)	(0.09)	(0.06)	(0.05)	(0.05)
Adjusted cash interest cover (alternative calculation)	ratio	+0.00	(0.00)	(0.00)	(0.01)	(0.01)
FFO/Net Debt	ratio	(0.2)%	(0.2)%	(0.2)%	(0.2)%	(0.2)%
FFO/Net Debt (alternative calculation)	ratio	(0.2)%	(0.2)%	(0.2)%	(0.2)%	(0.2)%
Headroom for reverse stress test to Baa1/BBB+	£m	30	32	25	23	22
Extent of stretch required to reach limit	%	297.0%	309.5%	236.1%	214.1%	200.2%
Covenant Class A AICR	ratio	2.87	3.51	2.26	2.02	1.93
Covenant Senior AICR	ratio	2.36	2.88	1.99	1.80	1.73
Covenant Combined RAR	%	70.6%	72.6%	74.5%	75.9%	76.8%
Moody's AICR	ratio	2.53	2.50	1.85	1.75	1.69
S&P FFO/Net Debt	%	8.9%	7.9%	6.5%	6.2%	6.1%

Scenario assessment: PASS

This scenario falls well short of the most severe +10% totex scenario above that impacts ratios in much the same way but to a greater extent. This lower level of

increased costs does not have a significant impact to credit metrics, maintaining Baa1/BBB+ ratings well above the Baa3/BBB- resilience threshold.

The reverse stress testing against AICR targets implies a significant increase in bad debt is required, +200% to +310%, for this risk to create an issue in isolation.

7. Increase cost of new debt as it is refinanced and projected additional debt in projections

The base case assumes any maturing debt is refinanced in the period of maturity assuming rates implied by the allowed cost of debt used in the WACC and current market conditions. The risk to Affinity Water from this sensitivity has increased into AMP8 due to the significant amount of debt projected to be needed to fund investment driving RCV real growth. By the end of the AMP, projections show that new debt will make up 54.6% of the debt held by the company. This is significant given the current cost of debt in the markets when compared to embedded debt allowances that makes up 83% of the total cost of debt allowance.

Ratio outcomes:

		2026	2027	2028	2029	2030
Gearing	%	70.73%	72.63%	74.36%	75.62%	76.39%
Adjusted cash interest cover	ratio	2.39	2.46	1.54	1.40	1.33
Adjusted cash interest cover (alternative calculation)	ratio	2.30	2.37	1.49	1.36	1.28
FFO/Net Debt	ratio	8.70%	8.36%	7.24%	6.89%	6.68%
FFO/Net Debt (alternative calculation)	ratio	8.37%	7.32%	5.65%	5.27%	5.08%
Variance to Base (+/(-)):						
Gearing	%	+0.0%	(0.0)%	+0.0%	(0.0)%	(0.0)%
Adjusted cash interest cover	ratio	(0.00)	(0.09)	(0.34)	(0.36)	(0.36)
Adjusted cash interest cover (alternative calculation)	ratio	(0.00)	(0.09)	(0.33)	(0.35)	(0.35)
FFO/Net Debt	ratio	(0.0)%	(0.0)%	(0.5)%	(0.6)%	(0.7)%
FFO/Net Debt (alternative calculation)	ratio	(0.0)%	(0.0)%	(0.5)%	(0.6)%	(0.7)%
Headroom for reverse stress test to Baa1/BBB+	£m	32	33	17	12	8
Extent of stretch required to reach limit	%	69.7%	72.1%	5.2%	3.7%	3.0%
Covenant Class A AICR	ratio	2.92	3.34	1.84	1.62	1.54
Covenant Senior AICR	ratio	2.40	2.78	1.66	1.47	1.41
Covenant Combined RAR	%	70.5%	72.4%	74.4%	75.8%	76.6%
Moody's AICR	ratio	2.53	2.36	1.51	1.41	1.34
S&P FFO/Net Debt	%	9.1%	8.0%	6.0%	5.6%	5.5%

Scenario assessment: PASS

This scenario shows a worsening position worsening as the AMP progresses, this is due to the nature of the test that takes effect as new debt is issued. The large re-financing in the AMP occurs midway though year 2 and investment growth funding compounds into the final 3 years of the AMP. Distributions are reduced to offset increased servicing of actual debt interest so net cash impact to gearing and net debt levels is mitigated.

Gearing and AICR metrics stay comfortably above Baa3/BBB- resilience thresholds but the alternative FFO/Net Debt ratio comes under pressure as new debt compounds, although stays above threshold. There is potential to mitigate by replacing cash flows from new debt with retained projected distributions, £156m included in scenario, that would both reduce net debt and increase FFO that is net of debt interest.

8. Financial penalties equal to 6% of Appointee turnover each year applied with a 2-year delay

Similar to the ODI penalty scenario, this sensitivity reduces revenues by 6% of pre-sensitivity Appointee turnover applied with a 2-year delay from when the penalty is incurred. The modelled scenario applies the penalty to years 3-5 that are assumed to be incurred in years 1-3. The reduction in revenue is modelled to impact profit for tax and working capital to gauge the full extent of cash flows and timing.

Ratio outcomes:

		2026	2027	2028	2029	2030
Gearing	%	70.73%	72.65%	74.77%	76.75%	78.25%
Adjusted cash interest cover	ratio	2.39	2.55	1.40	1.33	1.28
Adjusted cash interest cover (alternative calculation)	ratio	2.30	2.45	1.34	1.27	1.22
FFO/Net Debt	ratio	8.70%	8.41%	6.65%	6.49%	6.39%
FFO/Net Debt (alternative calculation)	ratio	8.37%	7.36%	5.05%	4.86%	4.78%
Variance to Base (+/(-)):						
Gearing	%	-	-	(0.4)%	(0.7)%	(0.9)%
Adjusted cash interest cover	ratio	-	-	(0.48)	(0.44)	(0.41)
Adjusted cash interest cover (alternative calculation)	ratio	-	-	(0.48)	(0.44)	(0.41)
FFO/Net Debt	ratio	-	-	(1.1)%	(1.0)%	(1.0)%
FFO/Net Debt (alternative calculation)	ratio	-	-	(1.1)%	(1.0)%	(1.0)%
Headroom for reverse stress test to Baa1/BBB+	£m	32	34	8	6	4
Extent of stretch required to reach limit	%	10.1%	10.8%	8.5%	7.7%	7.1%
Covenant Class A AICR	ratio	2.93	3.61	1.92	1.65	1.58
Covenant Senior AICR	ratio	2.41	2.97	1.69	1.46	1.41
Covenant Combined RAR	%	70.5%	72.4%	73.8%	74.9%	75.5%

		2026	2027	2028	2029	2030
Moody's AICR	ratio	2.54	2.51	1.43	1.37	1.32
S&P FFO/Net Debt	%	9.1%	8.1%	5.5%	5.3%	5.2%

Scenario assessment: PASS WITH MITIGATION

The penalties incurred apply pressure to AICR but they remain above Baa3 levels while gearing remains below the 80% threshold. The alternative FFO/Net Debt ratio is lowered below the BBB- threshold as debt increases and FFO is reduced by the penalties. There is potential to mitigate this by restricting distributions within the AMP (c£112m available) to reduce net debt and increase FFO.

9. Combination 1 – 5 years of sustained poor performance (totex +2%, ODI penalty 0.5% RoRE & bad debt +10%) with inflation pressure -1% each year

This scenario represents our assessment of a reasonable downside scenario with a combination of reasonable operationally driven cost pressures (totex +2% & ODI penalty 0.5% RoRE) and reasonable levels of macro-economic pressures (inflation -1% & bad debt +10%). We believe it is essential to test this severe but plausible downside scenario with a combination of variables to gauge the resilience of the actual company structure.

Ratio outcomes:

		2026	2027	2028	2029	2030
Gearing	%	71.13%	73.69%	76.01%	77.83%	79.17%
Adjusted cash interest cover	ratio	2.02	2.09	1.56	1.45	1.38
Adjusted cash interest cover (alternative calculation)	ratio	2.02	2.09	1.56	1.45	1.38
FFO/Net Debt	ratio	7.95%	7.55%	6.88%	6.61%	6.41%
FFO/Net Debt (alternative calculation)	ratio	8.54%	7.23%	5.96%	5.66%	5.50%
Variance to Base (+/(-)):						
Gearing	%	+0.4%	+1.0%	+1.7%	+2.2%	+2.7%
Adjusted cash interest cover	ratio	(0.36)	(0.46)	(0.32)	(0.31)	(0.31)
Adjusted cash interest cover (alternative calculation)	ratio	(0.27)	(0.37)	(0.26)	(0.25)	(0.25)
FFO/Net Debt	ratio	(0.8)%	(0.9)%	(0.9)%	(0.9)%	(1.0)%
FFO/Net Debt (alternative calculation)	ratio	+0.2%	(0.1)%	(0.2)%	(0.2)%	(0.3)%
Headroom for reverse stress test to Baa1/BBB+	£m	22	22	14	11	9
Extent of stretch required to reach limit	%	320.6%	289.7%	210.7%	182.0%	158.7%
Covenant Class A AICR	ratio	2.61	3.05	1.96	1.73	1.64
Covenant Senior AICR	ratio	2.15	2.52	1.73	1.55	1.48
Covenant Combined RAR	%	70.9%	73.5%	75.9%	77.8%	79.2%

		2026	2027	2028	2029	2030
Moody's AICR	ratio	2.26	2.18	1.62	1.53	1.46
S&P FFO/Net Debt	%	9.2%	7.9%	6.4%	6.1%	6.0%

Scenario assessment: PASS

AICR and FFO/Net Debt ratios remain resilient in the face of the combined sensitivities. Reverse stress testing of the AICR headroom implies no years drop below Baa1 levels with a combined scenario applied with the factor of 158.7% to 320.6% to breach the threshold. Gearing increases by +2.7% but remains within threshold levels with the further contingency of potentially withholding distributions if needed.

10. Combination 2 – Massive asset failure costs & penalties – Year 1 capex +£60m & opex +£20m, year 2 opex +£10m & year 3 opex +£5m

This scenario looks to replicate the financial risk associated with recovering from a massive asset failure. We project a significant year 1 cost to reestablish supply and build contingent assets as well as legacy opex in years 2 and 3 to cover operational adjustment and penalties. This scenario is different from combination 1 that looks at sustained reasonable pressure at looks at resilience through the lens of an isolated large event.

Ratio outcomes:

		2026	2027	2028	2029	2030
Gearing	%	73.81%	76.70%	78.45%	79.57%	80.19%
Adjusted cash interest cover	ratio	1.67	2.05	1.65	1.66	1.60
Adjusted cash interest cover (alternative calculation)	ratio	1.67	2.05	1.65	1.60	1.55
FFO/Net Debt	ratio	6.99%	7.27%	6.93%	7.00%	6.90%
FFO/Net Debt (alternative calculation)	ratio	6.67%	6.26%	5.37%	5.41%	5.33%
Variance to Base (+/(-)):						
Gearing	%	+3.1%	+4.0%	+4.1%	+4.0%	+3.8%
Adjusted cash interest cover	ratio	(0.71)	(0.50)	(0.23)	(0.11)	(0.09)
Adjusted cash interest cover (alternative calculation)	ratio	(0.62)	(0.40)	(0.17)	(0.10)	(0.09)
FFO/Net Debt	ratio	(1.7)%	(1.1)%	(0.8)%	(0.5)%	(0.5)%
FFO/Net Debt (alternative calculation)	ratio	(1.7)%	(1.1)%	(0.8)%	(0.5)%	(0.4)%
Headroom for reverse stress test to Baa1/BBB+	£m	13	23	19	22	21
Extent of stretch required to reach limit	%	164.7%	300.3%	336.5%	317.3%	299.7%
Covenant Class A AICR	ratio	2.74	2.30	1.96	1.86	1.85
Covenant Senior AICR	ratio	2.27	1.93	1.74	1.67	1.67
Covenant Combined RAR	%	73.7%	76.6%	78.4%	79.6%	80.3%

		2026	2027	2028	2029	2030
Moody's AICR	ratio	1.83	2.05	1.66	1.64	1.59
S&P FFO/Net Debt	%	7.2%	6.9%	5.8%	5.8%	5.8%

Scenario assessment: PASS

Metrics remain above threshold levels as the first 3 years impacted by the financial repercussions of the event and then the whole AMP as a result of additional debt taken on to cover the additional cash requirement. Gearing increase by +3.8% but levels remain within management levels.

Reverse stress testing of the AICR shows headroom against Baa1 levels with stetch to limit would require the scenario to take place with an increased factor of 165% to 337%.

11. Combination 3 – Repeat of AMP7 Covid and cost pressures -Years 1-2 inflation - 2% and opex +5% and years 3-5 inflation +8%, opex +10% and capex +4%

The 3rd combination scenario looks at recreating the pressures of AMP7, being a downside scenario that materialised in reality. The scenario looks at volatile inflation across the AMP along with cost pressures outside of management control.

Ratio outcomes:

		2026	2027	2028	2029	2030
Gearing	%	71.38%	74.34%	75.41%	76.18%	76.34%
Adjusted cash interest cover	ratio	1.98	1.94	1.33	1.31	1.30
Adjusted cash interest cover (alternative calculation)	ratio	1.98	1.94	1.33	1.31	1.30
FFO/Net Debt	ratio	7.85%	7.26%	6.35%	6.31%	6.33%
FFO/Net Debt (alternative calculation)	ratio	9.37%	7.65%	-0.04%	-0.19%	-0.31%
Variance to Base (+/(-)):						
Gearing	%	+0.6%	+1.7%	+1.1%	+0.6%	(0.1)%
Adjusted cash interest cover	ratio	(0.40)	(0.61)	(0.56)	(0.46)	(0.39)
Adjusted cash interest cover (alternative calculation)	ratio	(0.31)	(0.51)	(0.49)	(0.40)	(0.34)
FFO/Net Debt	ratio	(0.9)%	(1.1)%	(1.4)%	(1.2)%	(1.0)%
FFO/Net Debt (alternative calculation)	ratio	+1.0%	+0.3%	(6.2)%	(6.1)%	(6.1)%
Headroom for reverse stress test to Baa1/BBB+	£m	21	19	5	5	5
Extent of stretch required to reach limit	%	284.4%	218.1%	123.8%	125.3%	129.2%
Covenant Class A AICR	ratio	2.57	2.84	2.06	1.72	1.67
Covenant Senior AICR	ratio	2.12	2.35	1.81	1.53	1.49
Covenant Combined RAR	%	71.2%	74.1%	75.3%	76.2%	76.5%
Moody's AICR	ratio	2.22	2.04	1.38	1.34	1.32

		2026	2027	2028	2029	2030
S&P FFO/Net Debt	%	10.1%	8.4%	0.4%	0.2%	0.0%

Scenario assessment: PASS AFTER CONSIDERING INFLATION

AICR and gearing metrics remain compliant with the resilience Baa3/BBB- threshold. Alternative FFO/Net Debt in years 3-5 is heavily impact by the high inflation applied in the scenario. S&P who are focused on the alternative FFO/Net Debt (alternative) ratio have shown through current circumstances that they look through the inflation impact on the calculation as it ignores the systemic linkage to inflation within the regulatory mechanics in the industry. When considering this along with good AICR and gearing metrics we assess that the credit assessment would return an investment grade rating.

RR18: Income statement – actual company structure

Table RR18 shows the Income Statement for the actual structure appointee company consistent with historical reporting with the APR and financial statements. 2022-23 has been populated using the actual year's results from published APR data. The final 2 years of AMP7 have been forecast using the AMP7 data compiled to complete the PR24 table submissions (i.e. CW1 and PD5 for wholesale totex, revenues and RET1 and RET2 for Retail and PD1 for inflation). The opening balances from the 2022-23 APR along with the forecast table data is applied through the internal PR24 financial model built to forecast the financial statements for the remainder of AMP7 as well as the actual structure company forecast and analysis for AMP8.

The higher nature of AMP7 interest costs is due to the high inflation assumptions (PD1) drive a high amount of debt accretion. The inflation forecast subsides into AMP8 with much lower interest cost as a result when compared to AMP7.

Other income in the AMP8 forecast shows only the expensed grants and contributions income assumed within the submission tables but the AMP7 forecast also assumes cash generated from the projected land sales as well as non-price control and non-appointed profits that would be included within April 2025 opening cash balances. The 2022-23 APR appointee balance sheet apportions out an element of the cash balance associated with the non-appointed business, but this only applies to in year profits with the cash accumulating into the appointee balance sheet in future years and so therefore requires consideration here to forecast an accurate opening balance into AMP8. In AMP8 only the appointee business is considered for the purposes of the price review assessment and process.

Fair value gains/(losses) on financial instruments represents the revaluation done as part of the 2022-23 APR and financial statements whereas the forecast is the unwinding of the position through time to maturity of the financial instruments being

energy hedging to 2025 and inflation linked debt swaps maturing in 2026, 2030 and 2036.

Movements in deferred tax relate to the assumed disclaiming of capital allowances in AMP7 due to the lack of profits need to offset and to avoid creating carried forward tax losses as a result. This happens across 2023-24 to 2025-26 with the remaining 4 years assuming a more steady-state approach.

RR19: Statement of financial position – actual company structure

Table RR19 shows the Statement of Financial Position for the actual structure appointee company consistent with historical reporting with the APR and financial statements. 2022-23 is consistent with the appointee statements report within published APR data. Future balances are calculated using the internal AWL PR24 financial model built to forecast financial statements for the remainder of AMP7 as well as the actual structure company forecast and analysis for AMP8. The forecast statement is integrated to the forecasts for Income Statement (RR18) and Statement of Cash Flows (RR20) to compile and comprehensive set of forecast financial statements. Movements in Retained earnings & other reserves align to the Income Statement with changes in Cash & cash equivalents aligning to the Statement of Cash Flows with movements in component lines aligning across the statements.

A steady state approach on actual 2022-23 balances is taken on several lines within the statement they have irregular accounting movements and have no material impact to forecasting cashflows. Intangible assets, retirement benefit asset, current tax liability, current and non-current provisions as well as deferred income – grants & contributions.

In 2025-26 £250m of borrowings moves between non-current and current liabilities as it approaches maturity and repaid in 2026-27.

The retained earnings and other reserves balance in actual 2022-23 reported numbers is negative at £(132.019)m and our actual company AMP7 forecasts shows this deteriorating further by 2025. As the AMP8 forecast shows, we plan to carry out accounting adjustments, through a capital reduction and asset revaluation, that will rectify this situation. The adjustments increase balances in retained earnings and other reserves in 2025-26 by reducing called up share capital (£30.506m in 2022-23 increasing by £150m in 2025-26 relating to planned fresh equity injection) and increasing fixed assets NBV.

RR20: Statement of cash flows – actual company structure

Table RR20 shows the Statement of Cash Flows for the actual structure appointee company consistent with historical reporting with the APR and financial statements. 2022-23 has been populated using the actual year's results from published APR data. The final 2 years of AMP7 have been forecast using the AMP7 data compiled to complete the PR24 table submissions (i.e. CW1 for wholesale capex). The opening balances from the 2022-23 APR along with the forecast table data is applied through the internal AWL PR24 financial model built to forecast the financial statements for the remainder of AMP7 as well as the actual structure company forecast and analysis for AMP8.

Working capital uses a steady state days approach to forecasting future movements leaning on actual 2022-23 APR data. The fluctuations in calculated £m movements are a result of moving driver forecasts with changes in revenues or expenditure creating the year-on-year changes.

Tax paid is based on tax calculations carried out within the internal AWL PR24 financial model for the financial results of the actual appointee company. This differs from the calculations within Ofwat's PR24 Notional Financial Model that have the purpose of establishing tax wedge element of allowed revenue.

Distributions are forecast to be reestablished from 2025-26 aligning with allowed returns adjusted for performance and actual debt interest.

£150m of fresh equity has been forecast in 2025-26 in order to de-gear the actual appointee company below 71% by March 2026 to prepare for the significant investment programme and enhance financial resilience.

Net loans received are forecast to maintain at least £100m of cash balances and is a significant number due to the size of the investment program and resulting RCV growth. The £100m of cash liquidity, on top of £150m of undrawn RCF facility, is the product of our assessment of the suitable level of liquidity required to support the significant investment program. Across AMP8, surplus net cash of £56m is generated in order to increase cash balances to £100m.

RR21: Net debt analysis (appointed activities)

Table RR21 summarises the financial instruments within Affinity Water Limited's capital structure and corresponds to the historic reporting of the APR and financial statements. RR22 provides more granular data of the RR21 and therefore both tables reconcile. As table RR21 shows the financial instruments within the company's structure, it should reconcile with the financial instruments line in RR19. However, there is an observed difference of c.£30m. This difference arises from the firstly, the categorisations of current leases, which is included in RR21 but included in a

separate line in RR19. Included in the difference is the inclusion of amortised debt costs in RR19, which the RAG guidance requires to be stripped out of RR21.

RR22: Analysis of debt

Table RR22 shows all financial instruments that are embedded in Affinity Water Limited's capital structure. This table corresponds with the historic reporting of the APR and financial statement. This table also acts to provide granularity of RR21 and thus the totals should correspond to the values of RR21. There are no discrepancies between table RR21 and RR22.

RR23: Financial derivatives

Table RR23 shows all financial derivatives as well as their market values as at 31 March 2023. This mirrors the historic reporting in the APR and annual financial statements. There are no derivatives that Affinity Water Limited has transacted that are not represented in this table.

RR24: Debt balances and interest costs

The calculations used to populate table RR24 are derived from the internal AWL PR24 financial model designed to forecast financial statements and data for the actual appointee company from 2022-23 actuals out to 2030 to complete the PR24 submission. The model calculates each actual debt facility and inflation linked swap using actual terms and rates to obtain a forecast as accurate as possible for the existing debt portfolio.

In calculating levels of accretion for our RPI and CPI linked debt we have taken the March year end forecast index used to complete table PD1. The year end spot rate is a more accurate than a year average rate to the actual mechanism applied to accounting for debt accretion in our annual financial statements and accounts. To obtain a March year end CPI rate to apply to our CPI linked debt we have applied a CPIH to CPI wedge to the PD1 report assumptions based on historical averages of the wedge taken from ONS data.

The assumptions applied to the modelling are as follows:

	2024	2025	2026	2027	2028	2029	2030
RPI	5.88%	1.39%	0.69%	1.85%	2.83%	3.03%	2.99%
CPI	2.98 %	0.57 %	(0.10%)	1.06 %	2.04 %	2.03 %	1.99 %

The fixed debt balances, repayments and issuances are taken from the financial modelling used to generate the financial statements. Existing debt is repaid on

maturity and new debt is issued with a 50/50 mix of fixed and index linked bonds. The pricing for the cost of new debt draws on the allowed cost of new debt used in the Early View WACC published in Ofwat's Final Methodology.

The percentage rates used to populate the Interest rates and financing costs section of RR24 are derived from the financial model to achieve the modelled outcome in the Interest for financial metrics section. The £m interest amounts within the Interest for financial metrics section apply a 50% weighting to new debt and a full period charge to maturing debt, so the percentage inputs apply this logic to exactly calculated amounts to achieve the desired £m outcome. This alignment in £m outcome is key as table RR16 that shows financial metrics draws from table RR24 and needs to be aligned to our modelled analysis.

RR25: Allowed return on capital for the appointee

We have used the Ofwat assumptions to populate this table. As such we have no specific commentary.

RR26: Allowed return on capital by wholesale price control

The data used to populate RR25 and RR26 is the same and consistent with the final methodology. However, it should be noted that RR25 includes retail margin adjustment so the cost of equity in RR25 is different to the cost of equity in RR26. One needs to change the Equity risk premium to make CoE in RR26 equal 4%.

The TMR is simply equity risk premium plus risk free rate so by changing equity risk premium and keeping risk free rate the same you also change TMR which is why it's different to RR25.

RR27: Revenue analysis & wholesale control reconciliation

This data table feeds from the populated PR24 financial model v21a, made available by Ofwat through their website, following the methodology and guidance.

RR27a: Revenue analysis

This data table feeds from the populated PR24 financial model v21a, made available by Ofwat through their website, following the methodology and guidance.

RR28: Historic cost analysis of tangible fixed assets

The amounts shown in table RR28 relate to the actual company reported fixed assets (as shown in tables RR18 and RR19) that include a £200m asset revaluation in 2025-26 increasing the NBV of assets as well as increasing retained earnings and other reserves on the Statement of Financial Position. As the PR24 Financial Model v21a does not have the functionality to include the revaluation it has not been included on the notional company outputs generated by the model and is the reconciling difference between actual company and notional company outputs for fixed assets.

RR29: Asset lives

Asset life forecasts have been calculated using historical data within each price control from published APR data and then taking a view on the impact of future expenditure on historical levels. The historical asset life calculation used takes the depreciation charge in year for each price control and divides it by the average NBV using data from 2016 to 2023 and averaging across the years.

With the significant amount of investment in the final years of AMP7 that steps up into AMP8, we have assessed that a view must be taken in setting future asset life depreciation rates. The nature of our significant investment program would indicate that there will be a shift towards longer life assets then currently held on the fixed asset register driving historical rates of depreciation. We have taken the view that blended asset life within each price control in 2025 will be 25% higher than calculated historical averages to 2022-23 and increase by a further 5% each year into AMP8. The table below shows the assumptions made by price control and the overall movement in fixed asset balances. Fixed asset balances increase significantly with the proposed investment program, and even more so when considering that historical assets reduce in value each year and newer, longer life assets become more prominent.

	Calculated Historical Average to 2022-23	**2024-25 +25%**	**2025-26 +5%**	**2026-27 +5%**	**2027-28 +5%**	**2028-29 +5%**	**2029-30 +5%**
Fixed Asset Balance WR £m	*133*	148 +11%	160 +9%	172 +7%	190 +10%	196 +3%	196 +0%
Average asset lives for all fixed assets WR	*19*	24	25	26	27	28	29
Fixed Asset Balance WN £m	*1,258*	1,360 +8%	1,434 +5%	1,538 +7%	1,654 +8%	1,759 +6%	1,838 +5%

	Calculated Historical Average to 2022-23	2024-25 +25%	2025-26 +5%	2026-27 +5%	2027-28 +5%	2028-29 +5%	2029-30 +5%
Average asset lives for all fixed assets WN	24	30	32	34	36	38	40

RR30: RoRE analysis

Summary

A detailed pack explaining our approach to quantifying RoRE ranges has been provided in Appendix X. The appendix contains the following:

- Our assessment of RoRE ranges for the notionally efficient company
- Our assessment of actual RoRE ranges under notional company structure
- Our assessment of actual RoRE ranges under actual company structure

The data used to populate RR30 is our assessment of actual RoRE ranges under notional company structure. We did consider if our assessment of RoRE risk ranges for the notionally efficient company should be used to populate RR30 but felt the actual RoRE ranges under the notional company structure was the most appropriate lens to view the risk. This being said, the overall outcomes under both lenses is similar.

We have modelled the following key areas of risk in our analysis:

(i) totex;
(ii) retail costs;
(iii) revenue incentive mechanisms;
(iv) financing (inflation and new debt issuance);
(v) ODIs;
(vi) Measures of Experience (MeX); and
(vii) Price Control Deliverables (PCDs).

PCDs are a new financial incentive at PR24, and we have captured the RoRE risk created by PCDs in addition to the six RoRE ranges Ofwat expect.

Our analysis shows that the conditions specified in the Final Methodology lead to downside asymmetry and higher absolute levels of downside risk in terms of RoRE risk ranges.

We have articulated some of the reasons for this here and in our Business Plan and in line with the expectations of the Final Methodology we have outlined ways to correct this downside skew by mitigating risk at source.

How each of the low and high scenarios have been calculated for each of the contributing areas of RoRE.

Our approach to conducting RoRE risk analysis has been carefully developed with Ofwat's guidance in mind. That is to say, our approach draws on historical data to identify the range of out/under-performance achieved in the past; and uses this to make inferences regarding future risk.

For the 'actual' company-specific risk analysis, we have analysed the past performance of Affinity alone. This is because we consider Affinity's own past performance to be the most likely indicator of its future performance, with the performance of other companies that have different characteristics to Affinity unlikely to be as informative. For this analysis, we have also been able to supplement historical data with internal expert judgment, in instances where the historical data is:

(i) incomplete; and/or
(ii) expected to be a less good predictor of future performance.

To address each in turn:

(i)Totex and (ii) retail costs

To model totex and retail cost risk, we undertake a historical analysis of under/over-performance against totex and retail cost allowances for Affinity. Specifically, we model the historical percentage variation between outturn expenditure and allowances, calculated on a price control basis. We then use the P10 and P90 historical variance, along with projections of PR24 allowances, to estimate the range of possible performance over PR24, as a percentage of regulatory equity.

(iii) revenue incentive mechanisms

To model the risk imposed by revenue incentive mechanisms at PR24, we collected historical data on allowed and recovered revenues for Affinity. This allowed us to establish the P10 and P90 revenue forecast error observed historically.

By combining this data with relevant information on the penalty threshold and penalty rate (published by Ofwat for PR24), alongside projections of allowed wholesale revenues at PR24, we are able to estimate the range of possible financial penalties that could be received over PR24.

(iv) financing (inflation and new debt issuance)

We calculate both the: (i) inflationary risk on embedded debt; and (ii) cost of new debt risk, as per Ofwat's guidance. To calculate inflationary risk, we follow Ofwat's methodology, but flex the inflation assumption (+/-1% variance around a 2% central case). We construct an inflation distribution using the last 10 years of data from the OBR. We also use Affinity's actual % of index-linked debt in the calculations.

To calculate the cost of new debt risk, we remove Ofwat's 15 bps adjustment to the iBoxx index, as we consider the index itself reflects the likely performance for firms.

(v) ODIs and (vi) Measures of Experience (MeX)

To model ODI and MeX risk, we gather data on the historical performance of Affinity against targets. We calculate the annual variance between outturn performance and the target, before taking the P10 and P90 of this historical variance to inform our risk range.

By applying the P10 and P90 variance to projections of PR24 performance targets, we are able to predict the possible range of performance around our targets at PR24. We then use the PR24 indicative ODI rates published by Ofwat to calculate the implied financial impact for Affinity. We also use information published by Ofwat regarding how caps, collars, and enhanced incentives will be used at PR24.

For ODIs where there is little or no historical data, we supplement this data with the internal expert judgment to calculate our 'actual' company-specific risk ranges.

(vii) Price Control Deliverables (PCDs)

To calculate PCD risk, we constructed probability distributions of the length of delays for capital and enhancement projects, based on historical evidence of delays to UK construction projects provided by Cornerstone. Combining these delay length distributions with our PCD proposals enabled us to obtain a range of possible financial impacts of PCDs over PR24 (in the form of PCD penalty payments and time delivery incentive payments), and thus construct our risk ranges:

Any variations from our approach taken in chapter 2 of Appendix 10 – aligning risk and return.

None

What mitigating factors have been considered as part of the RoRE analysis.

The risk ranges presented in table RR30 show the 'gross' risk, i.e. we have not included the de-risking impact of any potential regulatory mitigations including those we have discussed below and in Chapter 9.

In essence, the table and risk analysis show the current downside asymmetry based on the conditions specified in the Final Methodology, we have made various suggestions for how this can be corrected but we have not embedded these corrections into our risk ranges.

Where the detail for bespoke uncertainty mechanisms or notified items is located within their business plan.

We do not include any bespoke uncertainty mechanisms or notified items in our plan.

How the four ODI components have been aggregated to take account of interactions between individual performance commitments.

Broadly speaking, risk ranges are calculated for each performance commitment individually, before being aggregated into an overall risk range for ODIs and MeX as a whole, using a Monte Carlo simulation.

There are two key reasons for using a Monte Carlo simulation to aggregate the results:

- Firstly, this method reflects the fact that it is highly unlikely that a company will experience the extreme ends of all risks simultaneously, i.e. they are unlikely to perform at the P10 on each risk area at the same time. A Monte Carlo model therefore builds in a more realistic range of possibilities.
- Secondly, the output of the Monte Carlo simulation is not simply a range of two numbers, but a distribution of possible values of an aggregated outcome. This allows us to gather more information about expected RoRE (e.g. most likely value, P10, P90), than we could gain from a simple aggregation approach.