# The Ofwat Graduate Development Programme - Economics

February 2021



# Overview of today's session

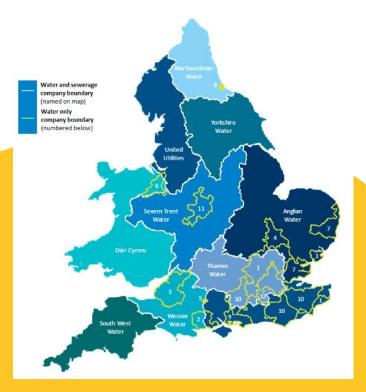
- What is Ofwat anyway?
- The economics graduate programme
- What do economists actually do in Ofwat?
  - Example 1 cost assessment
  - Example 2 customer engagement
- Reflections of an ex Warwick alumni
- How to apply



Section 1
What is Ofwat anyway?

### Who are we?

- Ofwat was established in 1989 when the water and sewerage industry was privatised. Water companies act as natural regional monopolies, a term you may be familiar with from your economics modules.
- We regulate 6 water-only companies (WOCs) and 11 water and sewerage companies (WASCs) in England and Wales, covering around 50 million households.



Source: discoverwater.co.uk

It is our duty to:

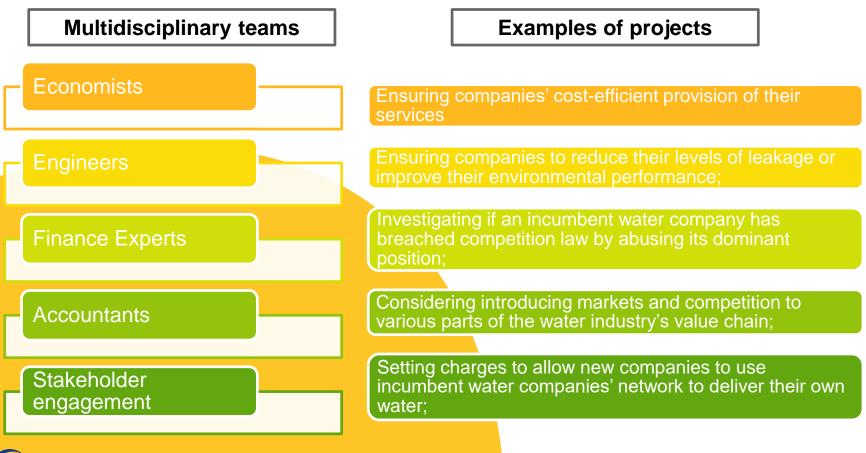
- To protect the interests of consumers;
- b) ensure water companies can finance the carrying out of their functions; and
- further the resilience objective to secure the longterm resilience of water companies' water supply and wastewater systems.

Our 3 strategic goals for the sector are to transform water companies' performance, drive water companies to meet long term challenges and for companies to provide greater public value for customers and the environment. You can read our strategy here.



### How do we work?

- Ofwat is an organisation place where you can apply the principles of industrial organisation and microeconomics to real-life issues.
- We work in multidisciplinary and teams: some projects are listed below.





Section 2
The economics graduate programme

### Programme overview

- You'll be employed on a 2 year fixed term contract starting salary £28,000 (more details of benefits online).
- This is a 2 year programme, covering 4 X 6 month rotations. The aim is to give you range of experiences, so you can develop as a well rounded regulatory economist.
- The scheme is open to both undergraduate and postgraduate students.
- We have offices in Birmingham and London (you'll be able to express a preference for which) with remote working available.
- The start date for the scheme is 6 September 2021 (but can be flexed depending on when finish studies).

Example project – cost assessment

### We regulate the water and sewerage industry!

 As there are regional monopolies operating in England and Wales, we need to intervene through economic regulation. One mechanism to do so (amongst others) is our price review which enables, incentivises and encourages water companies to achieve:

Great service for customers

That water and wastewater services to be resilient to both short-term shocks and long-term challenges such as population growth and climate change.

That such services to be affordable for all, including those struggling to pay.

- We set price five-year price controls where we set the allowed revenue companies can have from customers. PR19 will set price controls for the period 2020/21 to 2024/25.
- There are three broad areas of the price control:
  - Risk and return (ensure services are viable in financially and consumers are not harmed at the same time)
  - Outcomes: companies' focus on delivering what matters to customers and society, while giving them greater flexibility in how they deliver them
  - Cost assessment: We set a total expenditure allowance for companies for the period 2020-25.

### Cost Assessment within PR19



Cost assessment is the setting of an efficient total expenditure (totex) allowance for each company for the price control period.

Building block	Costs included	Assessment approach
Modelled base costs	Routine costs that can be compared between companies	Econometric models using historical data
Other costs	•Costs that are routine but they are not comparable across time or •One off investments, lumpy data	Various methods as appropriate
Adjustments	Cost adjustment claims submitted by companies	Gates approach (deep dive)

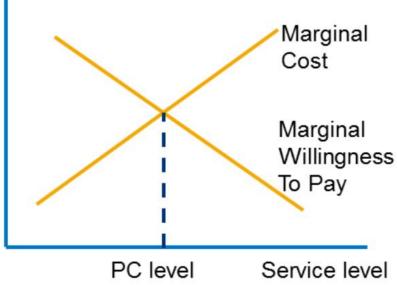
We use econometric models to benchmark costs and set efficient allowances for the regulated companies (see <u>Econometrics Technical Appendix</u>)

- Ensure data is of high quality
- Using econometrics to test economic hypothesis (panel data estimation methods)
- Developing transparent models
- Testing different models' specifications

Example project – customer engagement

### How we understand customer preferences

- In a competitive market, understanding customers' preferences is essential: companies that listen and respond to the needs of their customers thrive, while those that don't struggle.
- But... monopoly companies in the water sector do not face the same kind of competitive pressure. So how do we:
  - Work out what customers want? (e.g. do they want more investment to reduce supply interruptions or more investment to increase flood resilience?)
  - 2. Incentivise them to deliver this?
  - In recent price reviews, we have asked companies to undertake willingness to pay surveys: customers are asked how much they are prepared to pay for different service improvements, and we use this information to:
    - Set service levels for each company; and,
    - Set incentive rates for each area of service.





# Challenges with this approach

- One challenge at the last price review (PR19) was the pretty massive difference in incentive rates proposed by the different companies. For example, based on the rates proposed by companies, households were willing to pay:
  - between 10p and £4.20 on their annual water bill for a unit reduction in supply interruptions; and,
  - between £1.50 and £17 on their annual water bill for an equivalent reduction in internal sewer flooding incidents.

Which raises a question... how do we deal with this?

One option is to centralise the research.

- This should eliminate variation in results based on differences in research techniques/different companies carrying out the work.
- The downside is that this might stifle innovation in company research techniques.

But more generally... do consumers actually think in terms of willingness to pay?

- We know consumers are subject to cognitive biases which means they can struggle to engage with some forms of research.
- If so, maybe we need to consider alternative forms of research... Maybe citizen's assemblies?

If you're interested, you can read more about this work here.



Reflections of an ex Warwick alumni

### Takeaways from Warwick and the job find process

- Make use of the Warwick Career Centre
- Have some mock interviews
- Get a LinkedIn profile
- Think like an economist show you can think through issues
- Finding a job can be challenging don't give up and keep learning



# Being a Graduate in Ofwat



Site visit to Thames Tideway



Canadian Thanksgiving



Overnight stay

Site visit to United Utilities

# How to apply

# How to apply

You can apply on our website <u>here</u>. The process is:



The closing date for applications is 23.59 on Sunday 28 February 2021, so don't missout!

# Any questions?

If you have any queries, you can get in touch at:

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