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Dear Sir

Consultation: RIIO-2 Sector Specific Methodology

Omexom is the VINCI Energies brand dedicated to providing full engineering, procurement and construction services to electricity utility companies. VINCI Energies is part of VINCI SA, a global organisation with extensive experience in financing, building, owning and operating major infrastructure assets in the UK and internationally.

It is encouraging to see that Ofgem's objective is to ensure that RIIO-2 delivers a fair deal to all stakeholders; today's consumers, tomorrow's consumers, the environment, and for investors.

However, in reviewing the RIIO-2 Sector Specific Methodology, we note the structural reduction that Ofgem proposes to make to baseline allowed cost of equity return coupled with the proposal to retain full indexation as the methodology for setting cost of debt allowances.

We believe the magnitude of the proposed reduction to cost of equity return will adversely impact the ability of licence holders to finance their businesses from both a debt and equity perspective.

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The proposed structural reduction to cost of equity return will:

i/ Create an uncertain environment less attractive to equity investment,

ii/ Adversely impact financial covenant strengths including cashflow available for debt servicing and post maintenance income cover ratios,

iii/ Adversely impact the credit ratings of licence holders should gearing levels attempt to be maintained or increased if equity investment is not available,

iv/ With adversely affected credit ratings, the cost of bond debt available to the licence holders will rise. This will further adversely impact covenant strength due to:

(a) the proposal to retain full indexation as the methodology for cost of debt allowances coupled with;

(b) the resulting disconnection between indices and what rates are achievable in the market by the licence holders for what will be an indeterminate period.

As such, given this adverse impact on the ability of licence holders to finance their businesses due to a general deterioration in the investment environment for the sector, cashflows available to licence holders for OPEX, REPEX and CAPEX will be more unpredictable and uncertain in both their timing and quantum.

We believe because of this adverse impact on cashflows, licence holders will inevitably be forced to adopt a more risk adverse approach which may include unjust and unfair risk being transferred to contractors and other procurement and supply chain partners. Further, it may also force licence holders to defer project delivery or simply reduce absolute investment in the network.

Contractors faced with this environment will incur reductions in manpower productivity, reductions in work scheduling efficiency, increased financing costs, increased unit material and sub contract costs, and an absolute reduction in workload.

Ultimately, many if not all contractors would need to review their own business model assumptions to ascertain the viability of committing further investment into the sector, jeopardizing the employment prospects of a highly skilled engineering workforce, and may result in a dysfunctional and disorderly procurement and supply chain remaining in the sector.

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In conclusion, we believe the impact of the proposed structural reduction to the cost of equity return coupled with the proposed methodology for setting cost of debt allowances will result in long term detriment to consumers due to:

i/ Licence holders being less able to finance their businesses with the future cost of bond debt available to the sector eventually converging with the full indexation cost of debt protocol, resulting in additional cost for the consumer to absorb within RIIO-3 and price controls thereafter, and

ii/ Increased unit costs embedded within the procurement and supply chain having to be addressed in RIIO-3 and price controls thereafter.

We are eager to engage should Ofgem wish to discuss or seek clarification on any of the points raised in the comments above.

Yours sincerely

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