COST EFFICIENCY STRATEGY 2025-30

DELIVERING VALUE-FOR-MONEY FOR CUSTOMERS

Executive Summary

Hunter Water provides safe, reliable, high-quality drinking water to more than 600,000 people in homes and businesses across the Lower Hunter. We also provide wastewater, stormwater, trade wastewater, recycled water, and raw water services.

For over 130 years, we have worked with and for our communities to help deliver their aspirations, innovating to meet the changing needs of our growing region while protecting its health for future generations.

Originally established as Hunter District Water Supply and Sewerage Board in 1892, we separated from our public sector traditions and the organisation became Hunter Water Corporation on 1 January 1992. As a State-Owned Corporation, we are required to operate efficiently and to maximise the value of the State's investment.

Our prices have been subject to economic regulation for more than 30 years. This regulation has and continues to create incentives for Hunter Water to operate and invest efficiently. We currently have one of the lowest operating costs per property for water and sewerage services of any major utility in Australia.

While we are already an efficient business, there are always opportunities to improve. This Cost Efficiency Strategy is our plan to identify, deliver, monitor, and measure cost-efficiency initiatives throughout the business.

This Strategy serves to demonstrate to our community that we are challenging ourselves to become even more efficient over time; we have a credible plan to achieve the Strategy; and will be accountable if we don't.

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Introduction

Background

For our customers, community, and business, recent times have been challenging, from extended and severe drought, fires, floods, and the COVID-19 pandemic. Throughout these challenges, our customers and community have remained at the heart of what we do. Being guided by what is valued by our community continues to build trust and confidence in Hunter Water, particularly in times of uncertainty.

Hunter Water, as a monopoly essential service provider and the custodian of our customers' funds, is responsible for ensuring customers pay no more than they need to for the products and services they require.

While recent years have been characterised by flat or falling water bills (in real terms), the need to replace ageing assets, cater for population growth, manage risks such as climate change, and meet changing community expectations, are placing pressure on our water resources and infrastructure, necessitating new investment. The water industry is not insulated from economy-wide inflation and the costs to deliver our investments, and to operate and maintain the business, are materially increasing.

Meeting these challenges while ensuring our customer bills remain affordable, particularly given current cost-of-living pressures, remains our priority.

This has placed even greater focus on ensuring we're providing our services as efficiently as possible and demonstrating this – to ourselves, our customers, our Shareholders, and to IPART.

Why we've developed this Strategy

This Cost Efficiency Strategy (Strategy) is our plan to identify, deliver, monitor, and measure cost-efficiency initiatives throughout the business.

We've developed the Strategy to:

- Meet the expectations of our customers and community to continuously improve value for money in providing the services they want.
- Set a clear and ambitious efficiency target for the business and identify the initiatives and supporting measures that make us accountable.
- Demonstrate our plan to achieve cost efficiencies and an appropriate return on capital invested to our shareholders.
- Meet and exceed IPART's requirement that Hunter Water has a management-approved and externally published cost efficiency strategy (summarised in **Box 1**).

Box 1: Requirements for a cost-efficiency strategy

IPART's Water Regulation Handbook indicates that the Cost Efficiency Strategy should include:

- an annual 'efficiency factor' across operating and capital expenditure that represents a realistic yet challenging target
- details of productivity improvements achieved and proposed, which highlight that (Hunter Water) is adopting innovations
- details of how Hunter Water has performed against current period targets.

Source: IPART, Water Regulation Handbook

Intended audience

Given the different motivations for the Strategy, this document has multiple audiences. It serves as a detailed account of our Strategy for external stakeholders, including IPART, NSW Treasury, and other parts of government. It is also an internal tool and roadmap for our business.

We will publish a separate public-facing version of this strategy, on our website, that is targeted at our customers and community.

Cost-efficiency at Hunter Water

Hunter Water has strong internal and external processes and controls to ensure our expenditure is efficient and provides value-for-money for our customers. As a State-Owned Corporation, we regularly report to our Shareholder, NSW Treasury, on our performance and the efficiency and effectiveness of our business.

This section summaries these processes, our recent expenditure performance, and achievements and presents external benchmarking of the efficiency of our business compared to other water utilities.

This section also provides evidence that supports our view that Hunter Water is broadly at the cost-efficiency frontier. It sets the context for our cost efficiency target for the 2025-30 pricing period and why this is a realistic and challenging target for our circumstances.

Keeping control over costs

Our focus on delivering safe, reliable, and efficient water services is recognised from our Corporate Strategy down to our individual business cases and funding requests.

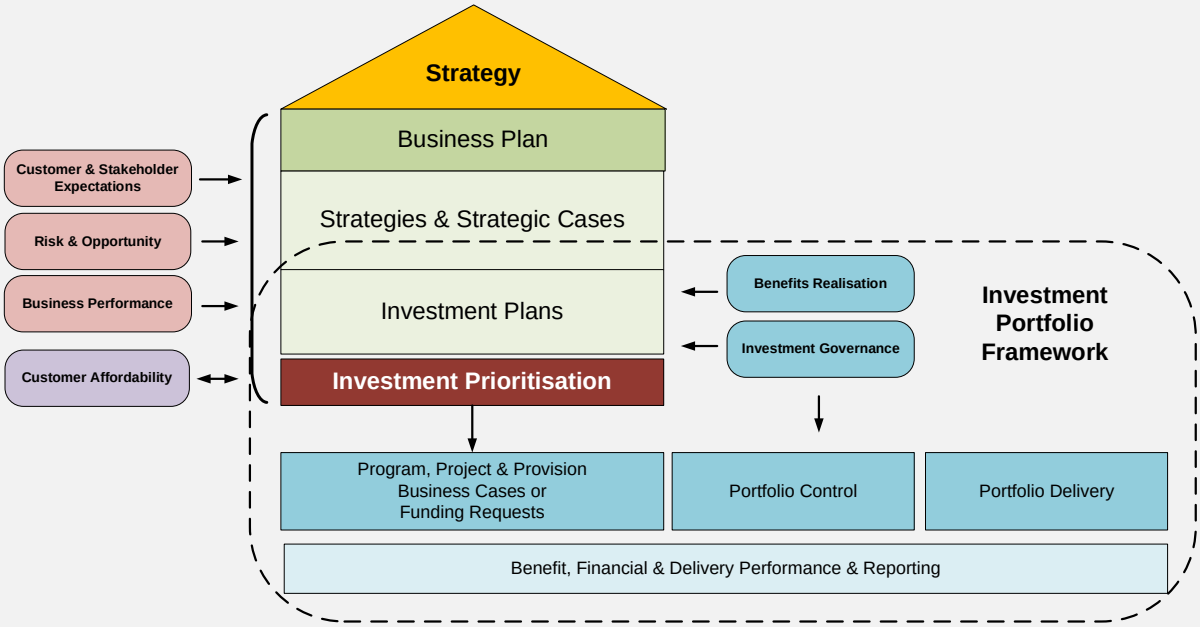
Some of the ways we focus on cost-efficiency and value for money include:

- **Detailed bottom-up budget builds:** This involves assessing regulatory requirements, needs, and drivers at the most granular level and building models to develop operating budgets based on the product (i.e., water), sub-product (i.e., water treatment), location, and expense type (cost category).
- **Our budgeting approach:** Our P50 approach to budgeting means that our proposed expenditure represents the most likely cost outcome with a 50% chance of our actual costs being either under or over the budgeted amount. This approach helps us keep costs down for customers by not including unnecessary contingency costs.
- **Robust top-down reviews by decision-makers**: Our Executive Managers, Management Investment Committee, Board Investment Committee, and Board of Directors challenge and prioritise our expenditure. This ensures our proposed expenditure is efficient and represents value for money for customers. (**Box 2** summarises our Investment Prioritisation framework).
- **Robust competitive procurement and market-testing:** We are continuously enhancing our capability in supply chain risk management and procurement. Most of our expenditure is market-tested through robust competitive procurement processes. Our contracts are actively managed in accordance with a detailed contract management framework to ensure we receive value for money.

We also actively identify opportunities to improve our efficiency. We regularly engage with the Water Services Association of Australia (WSAA) on its annual cost benchmarking study for the water sector. The WSAA's report identifies areas of our business where further work could lead to cost savings. Our efficiency target described later in this Strategy incorporates savings from work programs we anticipate putting in place based on WSAA's most recent benchmarking results.

Box 2: Hunter Water's Investment Prioritisation Framework

Our Investment Prioritisation Framework summarised in the figure below supports our Corporate Strategy by identifying those investment programs/projects which provide the highest Value to our customers and community.



Our five principles for investment prioritisation are:

- **Maximising customer value.** Our framework aims to maximise the customer value of the overall investment portfolio through the selection and timing of individual investment projects and programs.
- **Strategic alignment.** Investment portfolio outcomes should be aligned to Strategic Objectives and Risk Appetites.
- **Outcome-based investment initiatives.** Investments considered for inclusion in the portfolio should have all costs and benefits quantified using the Benefits Management Framework.
- **Engaged customers.** Prioritisation aims to balance affordability for customers with investments that address the long-term interest of customers. The approach is assessed and refined based on customer engagement and stakeholder feedback.
- **Investment Trade-offs.** Investment prioritisation should consider balancing trade-offs.

Source: Hunter Water

Engaging with our shareholder

Hunter Water is subject to a range of NSW Government policies that aim to replicate the disciplines and incentives that lead private sector businesses towards efficient commercial practices. We regularly report to our shareholder, NSW Treasury, including in relation to:

- **Agreed efficiency targets** that are included in our annual *Statement of Corporate Intent* and *Business Plan*. We need to demonstrate past efficiency performance and forecast efficiency targets, including the measures of efficiency and methods for assessing efficiency improvements.
- **External efficiency reviews,** where we must engage an appropriately qualified expert to undertake an efficiency review at least every five years or as otherwise agreed with Treasury. Once the results of the external review are available, we determine the actions needed improve efficiency and analyse the financial and operational impacts while ensuring that this will not adversely impact our quality of service to customers.
- **Our capital structure,** to ensure it is aligned with the strongest performers among our industry peers. We work with Treasury to identify adjustments needed to our capital structure that more efficiently allocates the Government's capital.

In addition to being a driver for our ongoing efficiency, these policies and Shareholder expectations also aim to enhance the transparency and accountability for our financial performance.

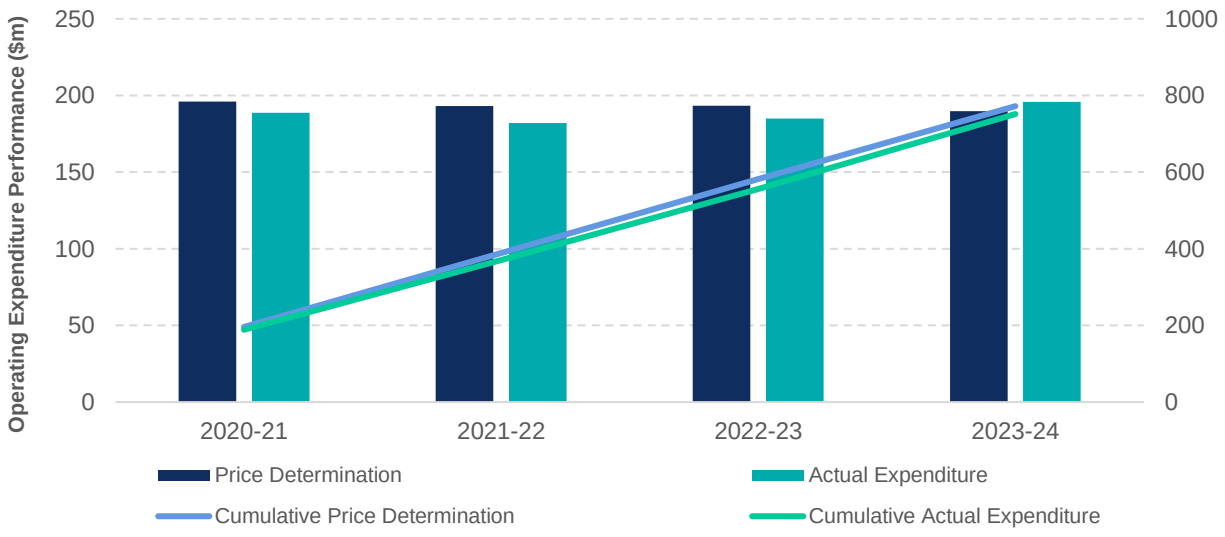
Our recent performance and achievements

Actual expenditure compared to IPART's allowance

Our robust controls around spending mean we effectively manage our actual expenditure within the allowances set by IPART. In the current regulatory period to date, we've:

- underspent the operating expenditure allowance by around 2.6% or $20.4 million between 2020-21 and 2023-24 (**Figure 1**).
- overspent the capital expenditure allowance by 1.7% or $14 million between 2020-21 and 2023-24 (**Figure 2**).

Figure 1: Actual operating expenditure compared to IPART allowance ($millions, $2024-25)



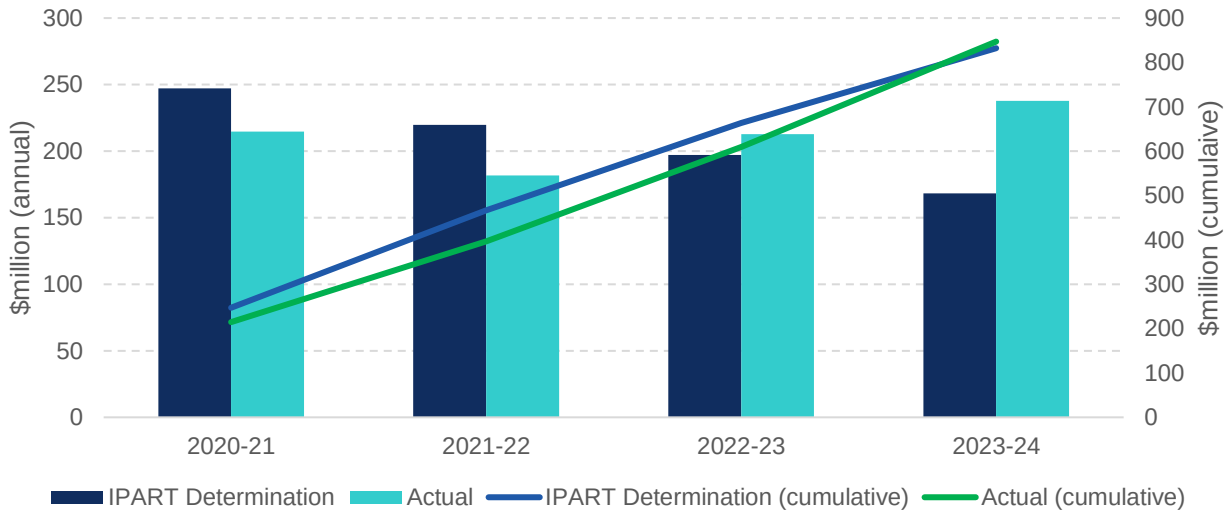
Source: *Hunter Water*

Our operating expenditure allowance in the current regulatory period was determined by IPART to be prudent and efficient. IPART's decision included a 0.8% continuing efficiency factor.

Figure 2 shows that overall, actual capital expenditure between 2020-21 and 2023-24 was similar to IPART's allowance. We underspent the allowance in 2020-21 and 2021-22 due to the COVID-19 pandemic, supply chain constraints, wet weather, and construction market conditions. As these external factors eased, our expenditure exceeded the allowance in 2022-23 and 2023-24.

All our investments go through a robust gateway approval, asset creation, procurement and prioritisation process to ensure they are well tested and deliver value for money.

Figure 2: Actual capital expenditure compared to IPART allowance ($ m, $2024-25)



Source: Hunter Water

While largely managing within IPART's expenditure allowances over the 2020 determination period, Hunter Water has also delivered the required performance outcomes to customers and achieved high levels of compliance against our operating licence. This is demonstrated in the annual audits of our Operating Licence and our annual Compliance and Performance Report. For example, IPART's most recent report to the Minister on Hunter Water's compliance with our Operating Licence states that we demonstrate a "strong culture and commitment to compliance" and a high overall level of compliance with the licence.[1]

Achievements and current initiatives

During the current regulatory period, some of the cost savings initiatives that have been implemented include:

- **Energy (renewables):** We've installed around 6,000 solar panels across 12 of our sites. As outlined later in this Strategy, we're also commissioning our largest installation ever at Balickera which will double our renewable energy generation capacity and supply renewable energy to our Water Treatment Plant at Grahamstown. Renewable energy is forecast to save our customers $9 million across the next five years.
- **Energy (consumption):** We've implemented Smart Integrated Pump Schedule (SIPS) to optimise the operation of pumps and valves to reduce energy consumption across the water network. The SIPS system utilises real-time operational data to forecast water demand throughout the network for up to 48 hours in advance. Once this demand is known, a pump and valve operation schedule will deliver a least cost solution with consideration to physical constraints around supply reliability and operational limits within the water network.

[1] IPART, Hunter Water 2023 Compliance Audit, Report to the Minister, March 2024, p 4.

- **Spoil management**: An increased focus on maximising spoil reuse and minimising spoil going to waste. Additional safety requirements have increased costs of spoil disposal and re-use. Our improved spoil management practices are optimising the cost per tonne of disposal.
- **Project delivery**: We've identified project-specific efficiencies achieved through project delivery. This includes greater consolidation of contract works and forming supplier panel arrangements to improve supply chain resilience and drive lower rates through greater competitive tension. Examples include:
    - Farley wastewater treatment plant upgrade, where $5.9 million in savings were achieved through collaborative negotiations and scheduling opportunities and
    - Seaham weir modifications, where $5.6 million in savings were achieved through detailed planning (specific fishway analysis) and negotiations with the contractor.
- **Digital innovations:** This includes the adoption of new technology as part of the Belmont WWT hub upgrade and the progressive rollout of the Field Service Model (FSM) to replace our end-of-life workforce management system; these are further summarised in **Box 3**.

Box 3: Digital innovation delivering cost savings

Belmont Wastewater Treatment Plant Hubgrade. We commissioned a Hubgrade Performance Plant (HPP) at the Belmont Wastewater Treatment Works in 2023. HPP is an innovative digital solution that improves the performance of existing infrastructure, and the installation at Belmont is the first in the Asia Pacific region.

Adoption of this new technology has resulted in immediate energy savings and has delayed capital investment of $10 million for 10-years. Due to the success of HPP at Belmont, we are exploring opportunities to adopt a similar solution to increase capacity at both Edgeworth and Morpeth treatment plants without the need for significant capital investment.

Field Service Model. The FSM is a significant digital transformation program for our maintenance workforce replacing our end-of-life workforce management system. FSM was implemented in our Electrical Mechanical Maintenance (EMM) division in August 2023, and to date, we have since seen the following:

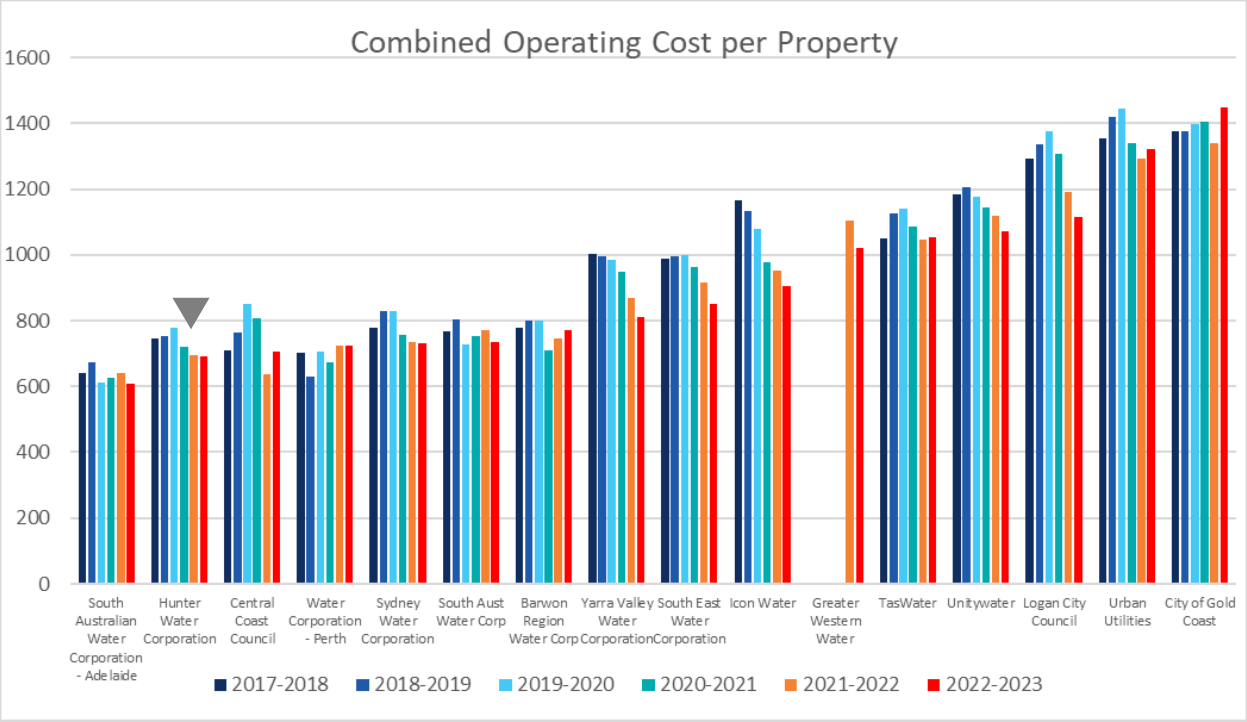
- Improvement in preventative maintenance KPIs to 100% compliance for all preventative maintenance since January 2024.
- A 30% reduction in overdue backlog corrective maintenance.
- A 10% decrease in the cost of preventative maintenance.
- A 25% decrease in total calls between EMM and the Control Centre (reduced by 1500 per month). This is equivalent to over 2,000 hours per year across EMM and the Control Centre.

Source: Hunter Water

Our expenditure compared to other water utilities

The National Performance Report (NPR) published by the Bureau of Meteorology benchmarks Australian water utilities' pricing, expenditure, and service quality. Indicators include water resource supply and usage, financial operations, bills and pricing, assets, water quality compliance, and customer performance. The most recent data from 2022-23 shows that our water and wastewater operating costs per property are among the lowest of 16 major water utilities (**Figure 3**).

Figure 3: Combined operating cost per property for water utilities ($/property)



Source: National Performance Report, December 2023

WSAA undertakes its benchmarking analysis which includes 'normalising' the NPR data to maximise comparability between water utilities. Normalising does not eliminate the impact of factors specific to a participant's regulatory, geographic, or operational environment.

The most recent WSAA benchmarking results from 2021-22 differ from the NPR findings. However, Hunter Water remained in the top three for the lowest operating costs per property.

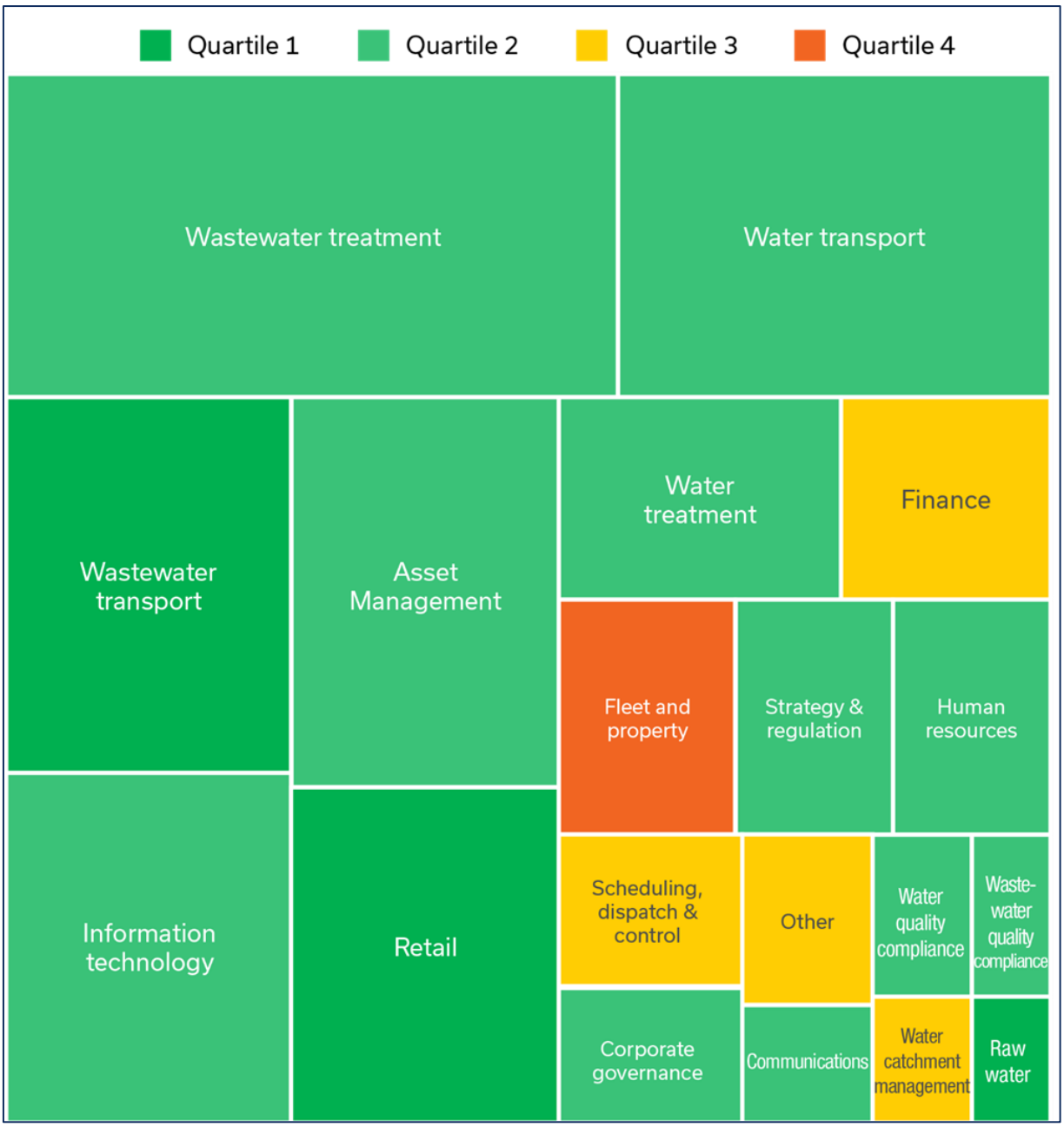
The tree-map in

Figure 4 shows our comparative performance across all 19 operating expenditure categories.

In Figure 4, the size of the box indicates the relative size by operating expenditure value. Quartile 1 (represented in darker green) means our costs for that category are in the lowest quartile among our peers. Quartile 2 (represented in lighter green) means our costs for that category are in the second lowest quartile among our peers. Quartile 3 (represented in yellow) and Quartile 4 (represented in orange) provide opportunities for further exploration and improvement.

The results show we perform strongly in most of the higher value operating expenditure categories, and the areas we perform poorest typically represent a lower proportion of our total costs.

Figure 4: WSAA benchmarking performance of Hunter Water



Source: WSAA Cost Benchmarking 2021-22

WSAA's expenditure benchmarking study also enables a comparison across operating and capital expenditure (total expenditure). **Table 1** provides a summary of the most recent study in 2021-22 for Hunter Water's total expenditure (totex) by category, in comparison to the industry median. Our totex is below or at the median for most categories in 2021-22, and on average over the past 5-years (as represented in green and orange). Those cost categories where Hunter Water's totex is above the industry median are represented in red.

Table I: WSAA's benchmarking of Hunter Water total expenditure

Category	Hunter Water Totex compared to the industry median	
	2021-22	5 Year Average
Water	Under	Under
- Water Network	Under	Under
- Water Treatment	Under	Under
Wastewater	Median	Under
- Wastewater Network	Over	Under
- Wastewater Treatment	Under	Under
Information Technology	Under	Median
Fleet & Property	Median	Over
Other Renewals & Compliance	Over	Over

Source: WSAA Cost Benchmarking 2021-22

Hunter Water actively engages in WSAA's benchmarking study and uses the findings to focus our efficiency initiatives and opportunities for improvement (as outlined below).

Our Cost efficiency target

Our efficiency target for 2025-30

We have set a cost efficiency target of 1% per annum of our forecast operating and capital expenditures over the 2025-30 pricing period. This equates to $77.6m in total cost savings over this period (**Table 2**). For reasons outlined below, we consider this represents a realistic, yet ambitious target.

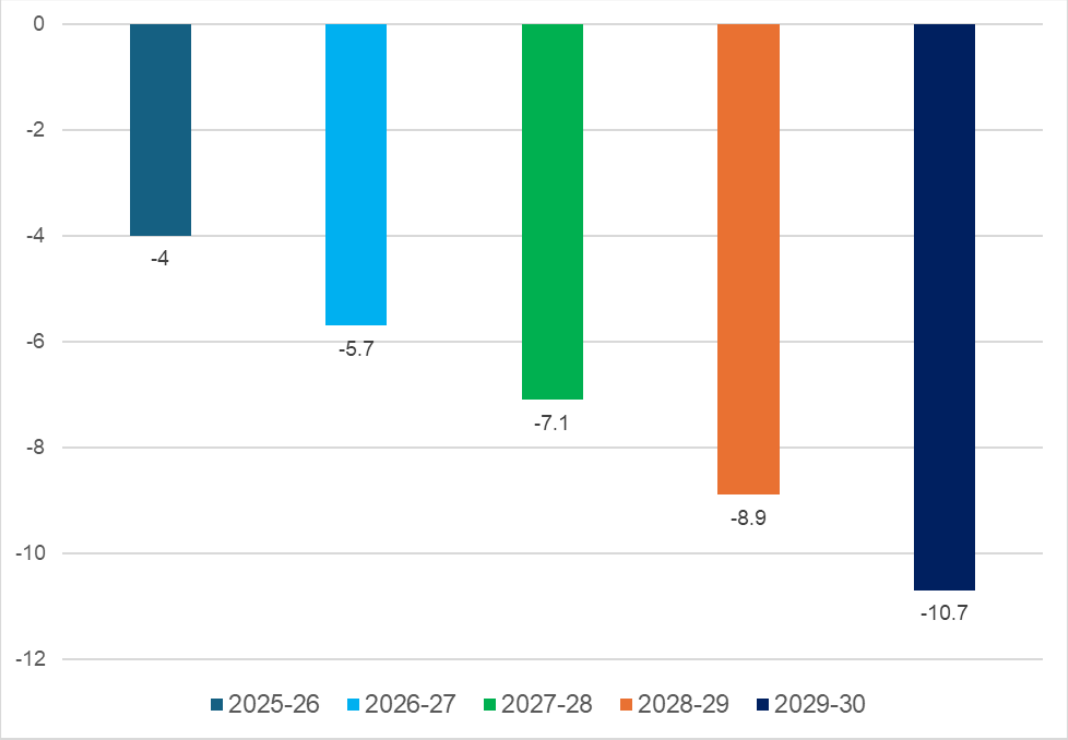
Table 2: Our 2025-30 cost efficiency target

2025-30 (5-year total)	Opex	Capex
1% efficiency target	$36.4 million	$41.2 million

Source: Hunter Water

Our 1% efficiency target compounds over time. This means we need to maintain cost savings year-on-year and identify new efficiency initiatives each year. **Figure 5** shows the 1% efficiency target on operating expenditure, equating to $36.4m in total operating expenditure savings over the regulatory period.

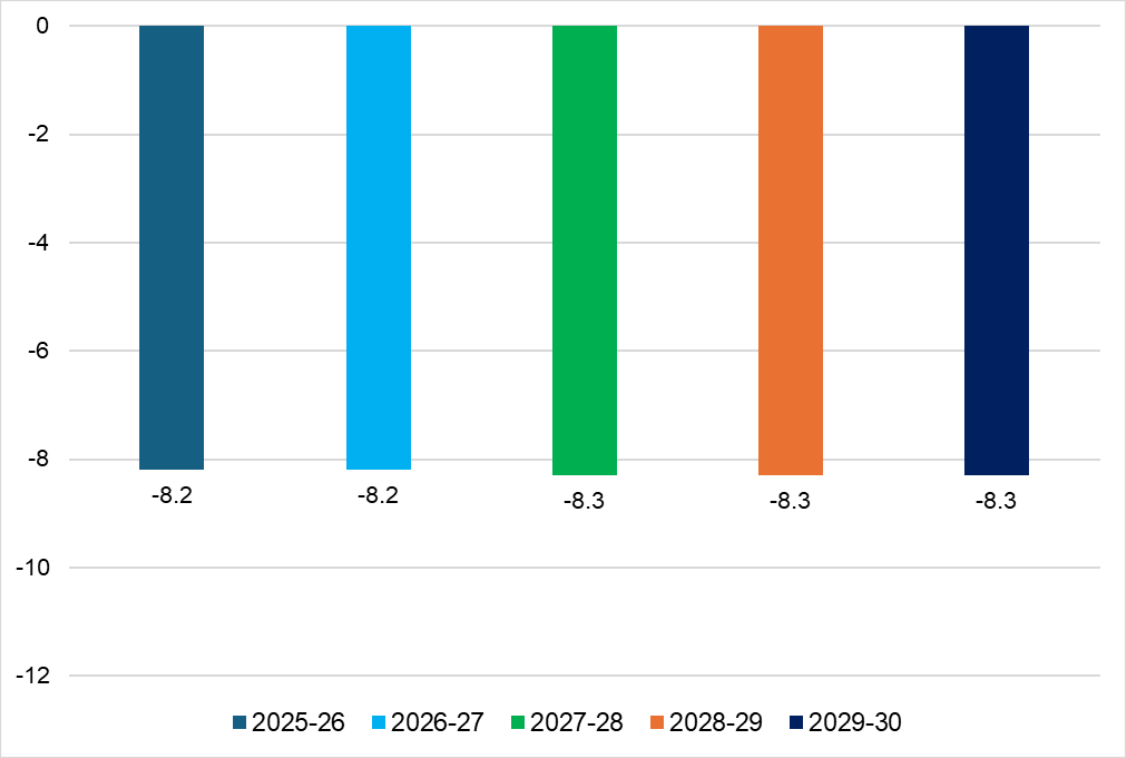
Figure 5: Operating expenditure efficiency target ($2024-25, $million)



Source: Hunter Water

Our capital expenditure savings target phases align with each product capital project delivery schedule. Applying a 1.0% per year compounding efficiency factor on capital expenditure is problematic given the 'lumpy' nature of capital works. The target of $41.2m capital expenditure efficiencies over the five-year period has been identified in alignment with the compounding efficiency. However, it has been spread proportional to each product's annual expenditure as shown in **Figure 6**.

Figure 6: Capital expenditure efficiency target ($2024-25, $million)



Source: Hunter Water

The sections below summarise our approach to determine our target and justification for why it is a realistic and challenging target for our business.

How we set our target

As summarised below, we considered a range of factors in setting our cost efficiency target. We also compared our target with historical productivity performance in the Australian economy and with the targets set by economic regulators.

Customer feedback

A key theme from engagement with our customers and community was concern about cost-of-living pressures. Right now, affordability is their number one priority. Many of our customers are already struggling to pay their bills, and some are experiencing vulnerability for the first time.

Our customers have motivated us to be ambitious with our efficiency target to help keep bills as affordable as possible.

Current performance

As noted in the previous section, we consider Hunter Water is broadly at the cost efficiency frontier. This is also consistent with our self-assessed grade under IPART's 3Cs framework. In setting the efficiency target we are mindful of our current performance and our position relative to the frontier.

Our efficiency target is a percentage (1% per annum) of our forecast expenditure, with this forecast expenditure reflecting the effect of a comprehensive range of efficiency measures implemented to date. That is, our efficiency target is applied to a 'base' level of expenditure (or current level of performance) that is already broadly efficient. Therefore, we have set the efficiency target at a level that primarily ensures Hunter Water continues to move with the efficiency frontier over time rather than having to 'catch-up' to this frontier (and then continue moving with it over time).

Internal assessment

We undertook a thorough internal (bottom-up) assessment of potential opex and capex cost saving initiatives and the estimated value of these opportunities. These initiatives are described in the following section. This assisted us in determining what is realistically achievable for our target.

While we've not yet identified all the initiatives needed to reach our efficiency target, we've established a framework to identify and implement opportunities throughout the 2025-30 pricing period. This framework is set out later in this Strategy.

Future operating challenges

We considered a range of operating challenges that may affect our ability to achieve efficiencies over the 2025-30 period and beyond, for example:

- Climate change, including the physical impacts of severe weather events, periods of drought, and high rainfall all have large impacts on our productivity
- The energy transition to lower emission technologies and how this affects our operating costs
- Demographic changes, including an ageing population and the impact of this on our labour productivity
- The outcomes of our investment in digital technologies, including cloud computing and improved customer experience, and how this translates into operating efficiencies.
- Increases in costs that are largely out of our control.

The risk from these challenges is difficult to quantify, and in some cases, we have limited ability to manage them. However, in setting our efficiency target we are mindful of these challenges and the risks they pose to the achievement of our target.

Comparing our target to other benchmarks

We have sense-checked our efficiency target with the following:

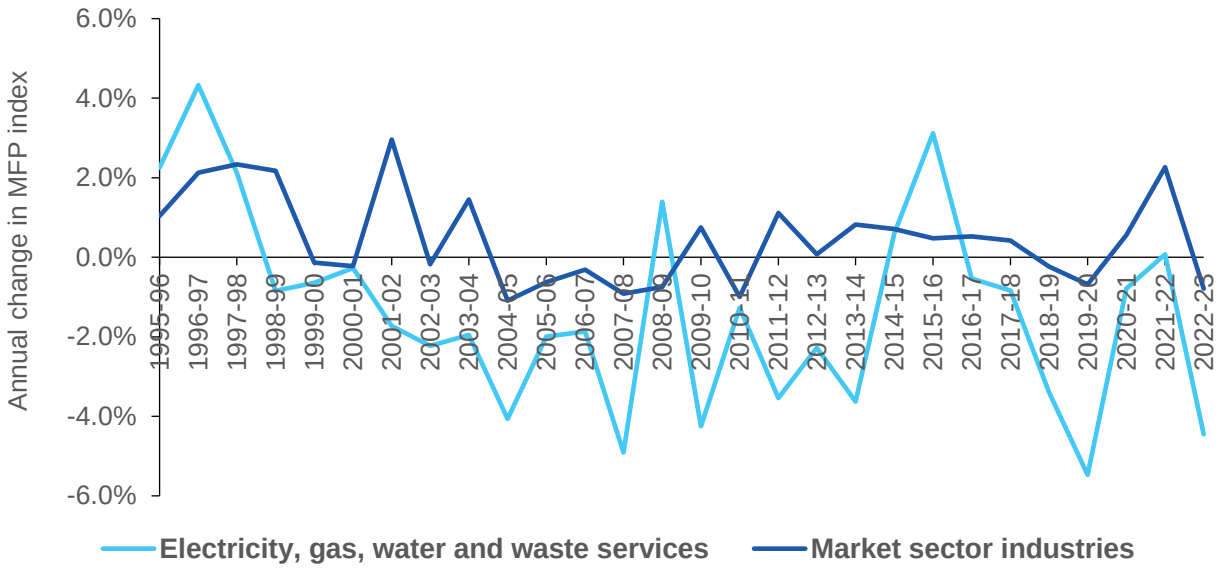
- historical productivity performance in the Australian economy, and
- decisions on efficiency targets set by a range of economic regulators (some of which also draw on historical productivity performance).

Historical productivity performance

Actual productivity performance in the economy can provide a guide as to what might reflect a reasonable efficiency target for Hunter Water. Using the same approach that IPART applied in its recent pricing decisions to calculate the continuing efficiency factor, we estimate the long-term average annual change in multi-factor productivity in the market sector of the economy is 0.8%.

As shown in Figure 7, over the past 20 years, the 'utility sector,' which includes 'water services' along with electricity, gas, and waste, has consistently lagged behind the broader market sector.

Figure 7: Multi-factor productivity in the Australian economy (% change)



Source: ABS, Cat 5260.0.55.002 Estimates of Industry Multifactor Productivity, Australia, Table 1 (Dec 2023)

The reasons for declining utility sector productivity are not clear. The Productivity Commission has suggested reasons, such as possible measurement issues[2], however 'unmeasured' impacts such as changes in regulations and standards which affect costs, may also be contributing factors.

Regulator decisions

Our target of 1% is compared with decisions from other regulators over the past couple of years in Table 3. These targets range from 0% up to 2% for some water businesses in Victoria.

Table 3: Recent regulator decisions on efficiency targets

Year	Regulator / business	Sector	Target p.a cumulative	Comment
2024	ESCOSA / SA Water	Water	0.8%	ESCOSA refers to this target as being in line with long-term multi-factor productivity growth outcomes for the market sector.
2024	ESC / Greater Western Water	Water	1.4%	The final decision refers to the expectations of Victorian water businesses
2023	ICRC / Icon Water	Water	1.2%	
2023	ESC / Yarra Valley Water	Water	1.7%	
2023	ESC / Barwon Water	Water	2.0%	
2023	ESC / South East Water	Water	2.0%	
2023	ESC/ East Gippsland Water	Water	1.0%	
2023	ESC / South Gippsland water	Water	1.4%	
2022	OTTER / TasWater	Water	1.5%	
2022	QCA / Seqwater	Water	0%	QCA noted that there was a credible efficiency program to reveal efficient costs over the regulatory period which it considered superior to an efficiency target.

Source: Hunter Water

[2] Productivity Commission, Productivity Insights, February 2020

A simple comparison of these targets is misleading because:

- Targets are generally specific to each business and include elements of both catch-up and continuing efficiency (Box 4) – therefore, differences can relate purely to where a business is relative to the cost efficiency frontier.
- Targets relate to other aspects of the regulatory framework in that jurisdiction – for example:
- Victorian water businesses who propose a 1.4% target to achieve a 'Standard' rating under PREMO can be compensated with a 0.4% increase in their return on equity relative to a proposal rated 'Basic' (and a lower efficiency target).
- Efficiency targets are sometimes only applied to 'controllable opex' as in Victoria, and thus may exclude bulk water costs, regulatory licence fees, etc.
- Regulatory decisions often refer to each other, meaning the decisions have a degree of circularity.

Bearing the above factors in mind, we consider a target of 1% to be appropriate for Hunter Water.

Box 4: Catch up and continuing efficiency

"Continuing efficiency" or "frontier shift" refers to the productivity improvements that the most efficient businesses achieve over time, for example, due to innovations and new technology.

Continuing efficiency differs from "catch-up efficiency," which refers to the efficiency gains needed for a business to reach the efficient cost frontier (see example below).

Figure 8: Catch-up and continuing (frontier shift) efficiency

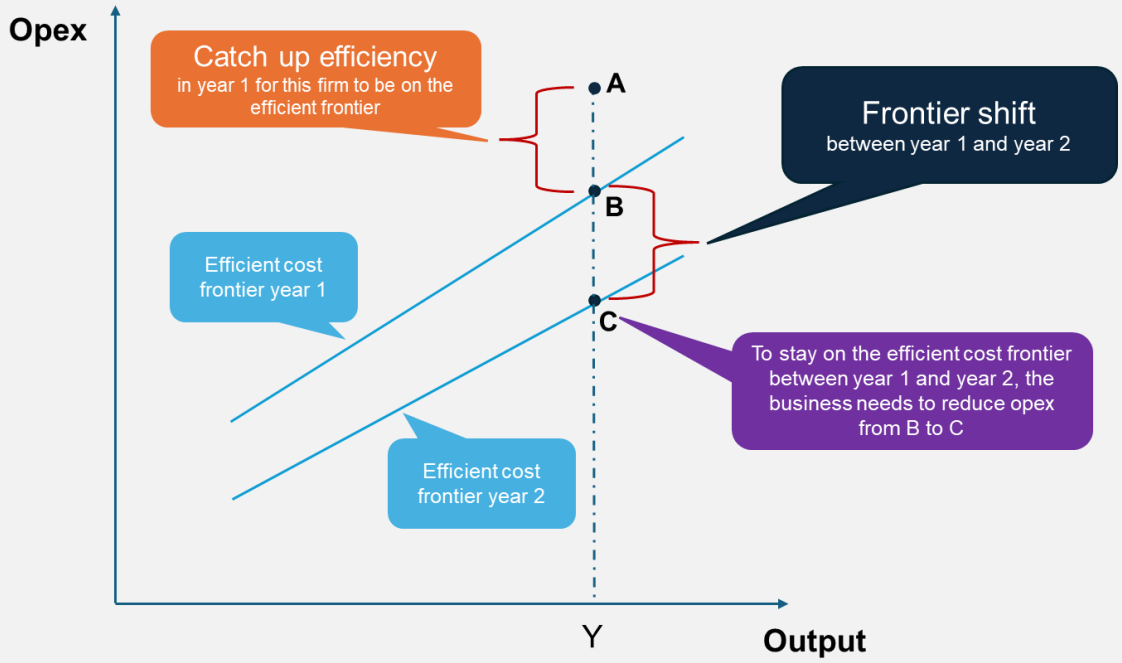


Figure 8 shows that:

- In year 1, one business produces Y units of output at cost B. This business is on the cost efficiency frontier in year 1. Another business is producing Y units of output at the higher cost of A. For this business (A-B) the catch-up efficiency needed to be on the cost efficiency frontier.
- In year 2, the most efficient businesses produce Y units of output at the lower cost of C. The difference between B and C is the "frontier shift" or "continuing efficiency" needed for a business to stay on the efficient cost frontier.

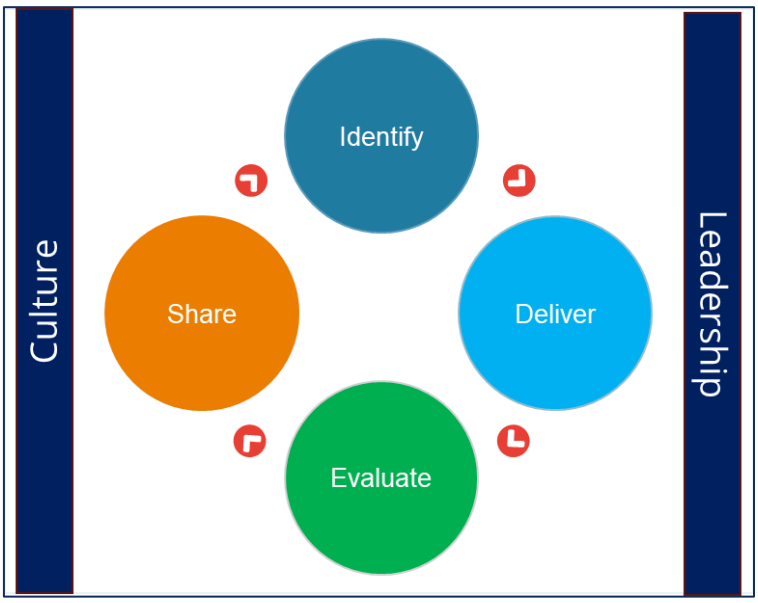
Our plan to meet the target

All parts of the business have a role to play in achieving our efficiency target. This section describes the framework and processes we've implemented to achieve our target. These are in addition to our current best practice expenditure management and review processes outlined earlier in the strategy.

Our cost efficiency framework

Our framework is an ongoing cycle summarised in **Figure 9** and discussed below. This framework recognises that an engaged and empowered workforce alongside appropriate resourcing, prioritisation, sponsorship, processes, and governance will be crucial in achieving our targets.

Figure 9: Our framework to deliver our efficiency target



Source: Hunter Water

Identify

We're putting in place structured processes to consider and identify opportunities for cost efficiencies across the business. These include:

- Recognition of all types of efficiencies in the context of customer value (**Box 5**)
- A dedicated Cost Efficiency and Continuous Improvement and Innovation (CI&I) team that is responsible for consistent practices and processes for ongoing identification, measurement, and reporting of efficiency initiatives
- Subject matter experts and cross-functional teams exploring efficiency opportunities in their respective areas of expertise, coordinated by the CI&I team.
- Periodic reviews of our business processes, systems, and frameworks to ensure leading cost efficiency practices are being implemented.
- Provisions to identify cost efficiencies in performance reviews, investment plans, and project development frameworks
- Encouraging individuals and teams to be innovative with solutions and provide a simplified process for these to be considered for implementation
- Utilising WSAA and other benchmarking/data analysis to identify areas of improvement and focus within our business.

Box 5: Types of efficiencies

We will consider cost efficiency through three lenses:

- Cost Reduction – a decrease in the costs previously incurred by the business. This is 'doing more or the same for less' with direct savings and impact on the bottom line. Examples include initiatives such as behind the meter solar to reduce our electricity spending.
- Avoided Costs – reducing a potential future expense or not incurring an expense due to a decision or action. Examples include undertaking preventative measures to avoid future outages or identifying a new or alternative solution with a lower future cost while delivering a similar outcome.
- Productivity Improvements – improving the level of customer service and/or employee satisfaction while maintaining the same cost base. This often refers to the effectiveness of processes, people, and technology in delivering services.

Source: Hunter Water

Deliver

We're developing a clear delivery methodology that:

- Establishes clear roles and responsibilities (i.e., who is responsible, accountable, consulted, and informed (RACI model))
- Includes management plans and timeframes for delivery of cost efficiency initiatives agreed to by key stakeholders
- Establishes protocols for reasonably estimating direct and indirect cost savings and benefits
- Provides support to those responsible for delivering efficiency incentives (i.e., tools to measure the performance of the initiative and financial analysis support)
- Ensures implementation stays on track through regular monitoring and support to remove any roadblocks.

Evaluate

The evaluation stage of the framework involves a regular review of the performance of efficiency initiatives. The aims are that this will ensure:

- savings or benefits of the efficiency initiative have or continue to be realised, and it is embedded in the day-to-day activities of the business
- progress against our efficiency target is regularly reviewed and reported, including through regular board and shareholder reporting via our corporate KPIs
- learnings from the initiatives are identified and shared across the business to inform future initiatives.

Share

Communicating the success and learnings from cost savings initiatives is critical to ensuring efficiency as part of our culture. We'll regularly share our achievements within the organisation to encourage future initiatives, build corporate knowledge, and continuously improve for the benefit of our customers and the Lower Hunter community - now and for future generations.

Initial efficiency opportunities

We've identified an initial set of cost efficiency initiatives to pursue over the 2025-30 pricing period. This is to:

- inform the suitability and achievability of our overall target
- provide initial focus areas for the business
- demonstrate our commitment to the Strategy.

These initial opportunities are summarised in **Table 4** and below. They represent efficiency savings (cost reduction lens) that could be realised over the 2025-30 period, subject to further investigation. In addition to these flagged initiatives, our cost efficiency framework will assist us to identify and deliver further initiatives throughout the 2025-30 pricing period to meet our 1% target. These 'further initiatives' are listed as 'yet to be identified' in **Table 4** below.

Table 4: Initial operating and capital efficiency initiatives over 2025-30 ($2024)

	OPEX	CAPEX
Initial opportunities identified		
Project Delivery		$16m – $20m
Planning & Decision Making		$8m - $10m
Digital (including FSM)	$6m - $7m	$3m - $6m
Opex savings from capital investment	$7m - $8m	
Rationalisation	$4m - $5m	
Enterprise Workforce Planning	$2m - $3m	
Workplace Facilities	$1m - $2m	
Maintenance (excluding FSM)	$0m - $1m	
Targeted actions from WSAA benchmarking	$6m - $7m	
Yet to be identified	Up to $7m	Up to $10m
Total	**$36.4m**	**$41.2m**

Project Delivery

Project delivery encompasses all project management activities from procurement to delivery, including value engineering, using lower-tier contractors, improved cost estimates, standardised drawings, and asset management. To date, Hunter Water has consistently implemented best practice project delivery practices.

Over the 2025-30 pricing period, we will investigate the scope to achieve further project delivery efficiencies through, for example:

- Bundled and consolidated packages of work across the delivery of design, engineering, infrastructure, and maintenance services. Through the bundling and consolidation of works, there may be opportunities to improve resilience in supply chains and delivery, optimise co-location efficiencies, retain contracted resources, consolidate corporate overheads, and enhance supplier competition.
- Continued Early Contractor Involvement and Early Tenderer Involvement to drive further efficiencies in the construction and operation phases.
- Greater use of performance-based contract models, with key performance indicators, to improve value for money.
- Leveraging NSW Government contracts, as with Hunter Water's recent change to the NSW Government Banking and Financial Services Agreement.

Our estimated cost savings in 2025-30 are based on actual project delivery savings achieved through the current pricing period.

Planning and Decision Making

Planning and decision-making efficiencies are achieved through the planning and business case preparation process. Actual system performance is collected and validated, changes in investment drivers are reviewed (regulatory, weather, climate), growth in new development is validated against available capacity, historical solutions are challenged, and innovative/targeted solutions are explored. Planning and decision-making efficiencies have been quantified at $8m.

Digital

Building our digital capabilities to transform the way we work will benefit our customers and our people, enabled by data-driven decision making and innovation at speed and scale. Digital transformation is the key to driving the long-term efficiency improvements necessary to keep our customer bills low and to meet the market in our service delivery. In recognition of the cost of digital investment and the impact on customer bills we are seeking to invest in a limited set of projects and programs that offer clear benefits:

- **Customer Experience** is expected to achieve efficiencies of $0.7m by providing customers with easier-to-use digital services and channels, reducing incoming calls, and replacing letterbox drops with SMS notifications.
- **Modern Utility** is expected to return CAPEX efficiencies of $6m through the application of Smart Systems, which incorporates installing monitoring or controlling devices or automation instrumentation which can either maximise the available capacity and allow increased growth without upgrades or can get early awareness of asset leaks and enable earlier maintenance to prevent larger and expensive replacements. OPEX efficiencies of $4.0m have been identified based on expected internal labour savings from improved work practices and optimised decision-making for overhaul and renewal frequency.
- **Digital Foundations** is expected to return efficiencies of $0.4m to be achieved through reducing non-conformance in compliance audits through better data and better real time data driven decision making.

Actions from WSAA benchmarking

To better understand the efficiency opportunities that could be derived from benchmarking, we have worked closely with WSAA since the 2021-22 benchmarking study. This collaboration produced a standardised and quantified benchmarking dataset of specific utilities considered most comparable to Hunter Water, which identified up to 20 functions (of a possible 130 total functions captured in the WSAA study) representing possible efficiency opportunities for Hunter Water.

For example, we plan to undertake a comprehensive review of our fleet management arrangements as this is an area we compare less favourably against our peers (see **Table 1** and

Figure 4).

In recognition of Hunter Water's unique circumstances and to avoid duplication of other identified efficiency initiatives, we have set an efficiency target of $6.4m in total or $1.1m on average per year from these targeted actions.

Operating Expenditure savings from capital investment

We're planning capital projects that will reduce our ongoing operating costs, including:

- An expansion of renewable energy ($6.2m), with a key contributor being the Balickera installation, will come online in July 2024.
- Energy efficiency strategies ($0.4m), including optimising WWTW nutrient analysers, mixers, and diffusers, reservoir level management, and valve automation.
- Roofing over the Spoil Bay at North Lambton depot ($0.4m), which will keep spoil stockpiles dry, resulting in less weight for disposal.
- Chichester Trunk Gravity Main replacement ($0.1m), which reduces welding costs upon replacing the final section from Brookfield to Burmi Creek.

Cost rationalisation

We're exploring opportunities to further reduce input costs through strategic reviews, including but not limited to our fleet, non-operational land holdings, biodiversity management, and rationalisation across our digital systems architecture. We've estimated this could deliver savings of:

- $4.3m from our fleet, software licenses, subscriptions and memberships, rates, land tax, property maintenance, and
- $0.5m from adopting government contracts in telecommunications and hardware.

We plan to conduct routine reviews of specific cost categories to ensure we have the right goods, services, and equipment to meet the business's changing needs and identify opportunities to reduce these input costs through better allocation or management.

Enterprise Workforce Planning

Enterprise workforce planning is underway to understand our desired workforce model with a long-term strategic focus (external/internal resources and distribution of work), to improve diversity (in response to the war for talent through workforce makeup and types of roles), and to optimise growth in the workforce. Through this process, we can reduce the cost of our design, engineering partner, and external labour through improved resource allocation, resource retention, and re-aligning resource types (internal versus external).

An efficiency target of $1.8m has been quantified based on a 5% reduction in overall labour spend.

We will also continue to manage employee leave provisions consciously. The greatest benefit of doing this is for the health and well-being of our employees, with a subsequent financial benefit. The annual leave provision was valued at $4.2m in February 2024, and efficiencies to sustainably reduce the provision over time have been quantified at $0.8m over the next pricing period.

Workplace Facilities

As part of our Workplace Masterplan, we're investigating a range of cost saving opportunities in our workplace facilities. These include:

- Security: $0.6 m in estimated savings (through remote unlocking and reduced theft),
- Vehicle updates: $0.1 m in estimated savings (using electronic vehicles with greater safety features) and
- Rationalisation of Tomago workspaces: $0.1 m in estimated savings (savings from energy, waste disposal, and cleaning).

Maintenance

Since 2014, Hunter Water has pursued a Maintenance Services Productivity Strategy focusing on demonstrating continuous improvement and targeting best quartile productivity benchmarking performance. An extensive transformation has occurred through changes to work practices, training, fleet, and equipment purchases. Cost efficiencies have been realised with maintenance operating expenditure reducing and being maintained well below inflation. Current conditions are challenging with an aging workforce, a tight labour market, and rising input costs.

Although significant efficiencies have been achieved, we still plan to identify new opportunities to drive and support productivity across the next pricing period. We estimate we will be able to absorb $1m in growth or 50% of overall growth estimates.

Accountability for this Strategy

We're putting in place internal and external processes to ensure we remain accountable for delivering on efficiency commitments in this Strategy.

External accountability

It's important that our customers and the community know what they're paying for and that they're getting good value for money. We're demonstrating this through:

- publishing a public version of this Strategy on our website
- reporting progress annually to our Community Committee (see Chapter 1 of our pricing proposal)
- communicating our efficiency performance to our broader customer base via existing channels.

In addition to regularly reporting our performance to IPART, we'll also report quarterly and annually to NSW Treasury, including our 'Efficiency Return' in the annual *Business Plan* and *Statement of Corporate Intent*.

Internal accountability

Within our business, we're putting in place a range of systems and reporting processes, including:

- Proactive and intentional management accountability through the Executive Management Team, Management Investment Committee and Board Investment Committee, to deliver the cost-efficiency strategy.
- Executive Management and organisational accountability for achieving cost efficiency targets via the Corporate Scorecard, cost efficiency, and profitability metrics.
- Monthly performance reporting to the Board via the Business Performance Report and Quarterly Report.

As noted above, an essential component of our cost efficiency framework is an engaged and empowered workforce along with appropriate resourcing, leadership, and governance.