

13th August 2019

Dan Rock
Head of Policy
Economic Regulation
Civil Aviation Authority
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Dear Dan,

Working paper summarising affordability and financeability modelling for capacity expansion at Heathrow airport (CAP1812)

I am writing to you in response to the CAA's assessment of affordability and financeability for capacity expansion at Heathrow. I appreciate the CAA's openness and constructive approach in developing this assessment.

This collaborative joint problem solving and analysis is in our view a far more efficient, effective and accurate way to conduct such assessments than isolated data requests and arms-length reviews. We would strongly urge a continuation of this approach in the future. Given the positive engagement between the CAA and Heathrow in the process we have limited additional comments on the working paper itself.

We note that the focus of the analysis is informing the CAA's response to the Department for Transport's (DfT)'s January 2019 request for an assessment of Heathrow expansion. The DfT sought the CAA's view on whether there are "credible scenarios" in which Heathrow can deliver its proposed masterplan in line with the Secretary of State's ambition on airport charges remaining close to 2016 levels in real terms while ensuring the programme is privately funded. We also note that the working paper is not a policy consultation nor a decision on the H7 regulatory framework.

The CAA's assessment builds on the April 2018 consultation (CAP1658) methodology. In our view the assessment of affordability and financeability is thus too narrowly focused on the resulting average airport charge per passenger and existing set of key credit metrics emerging from the modelled scenarios. We believe this is both overly mechanical in approach and fails to capture any rigorous test of consumer affordability or understand fully the market dynamics of financing expansion. However, within the constraints of the CAA's methodology, we understand the modelling approach and outputs.

In the working paper the CAA also describes how the definition of the regulatory framework and policy regarding financeability for H7 is progressing. It states that going forward, the CAA's approach to affordability will be guided by its primary duty of protecting the interest of current and future consumers as set out in its statutory duties - this is an important point. For the CAA to effectively protect the real interest of consumers, it must understand the full consumer benefits of Heathrow expansion. This means analytically assessing affordability relative to the overall fare paid by passengers, not solely the resulting airport charge per passenger. It also means an analytical consideration of the implications of timing, quality and risk for consumers.

Notwithstanding both this fundamental conceptual issue and the inevitable preliminary and indicative nature of any assessment at this point in time, Heathrow is supportive of the CAA's finding that there are credible scenarios that can be delivered affordably and financeably.

Although we recognise that CAP1812 is not a regulatory policy consultation document, we would also like to highlight the policy areas that now need prompt resolution by the CAA:

- *Duration of H7 regulatory framework*
In CAP1812, the CAA outlines an expectation that the duration of H7 would be 5 years. This in turn has been superseded by CAP1819, where the CAA discusses the possibility of a longer price control. Heathrow believes that a longer price control could be materially in the interest of consumers by supporting both financeability and affordability. We will provide further evidence in our response to CAP1819. We urge the CAA to engage actively with us in the next few months to explore consumer focused ways to provide longevity to the regulatory framework.
- *Financeability*
Heathrow is encouraged by the positive steps recently taken by the CAA in relation to financeability, including the appointment of Centrus as an advisor, and progress in developing the price control model (PCM). We ask the CAA to keep an open dialogue with Heathrow on these topics. It is a complex and sensitive issue and it would be a valuable step to be able to provide meaningful insight on the CAA's approach to assessing financeability in the October 2019 consultation.
- *Affordability*
Going forward, the CAA needs to define affordability based on robust consumer analysis. Closely related to the notion of affordability, we would expect the CAA to quantify the benefit to consumers of expanding Heathrow to evidence its decisions on the regulatory framework for expansion.

If you have any queries or would like to discuss further, please do not hesitate to contact me.

Yours sincerely



Richard Hepburn
Regulatory Director