HEATHROWWEST

Your Choice For A New Terminal

Introduction

Heathrow West Ltd is pleased to provide a response to CAP1832, "Working paper on financial resilience and ring fencing".

Executive Summary

The CAA has made proposals to ensure that, given the likely costs of expansion, there are options for ensuring that HAL has sufficient resources as well as options for mitigating the impact of financial distress and providing information to the CAA.

Heathrow West does not have detailed comments to make about the CAA's proposals at this stage. We have however 2 general observations about the CAA's approach. First, the sharply rising costs of expansion are making financial distress <u>more</u> likely and therefore put the overall expansion project at risk. Second, diversification of capital expenditure will make financial distress <u>less</u> likely and therefore increases the chances that expansion can be delivered.

The costs of expansion are rising making financial distress more likely

Our view is that the costs of the expansion project are continuing to increase. This view is shared by IAG / BA and Heathrow Hub. Heathrow West's ongoing correspondence with the CAA is seeking to understand the scale of the cost increase. We have written separately to the CAA to seek to understand HAL's costs in more detail to allow a comparison to be made between an airport expansion carried out by HAL alone and airport expansion carried out by HAL and Heathrow West. At some point, the CAA will need to understand and assess this comparison.

We observe that the excessive costs being proposed by HAL would seem to make the possibility of financial distress more not less likely. The fact that the costs are increasing therefore makes it particularly important that extra checks are put in place to allow the CAA to mitigate the risk that HAL will face potential financial distress and manage this effectively as HAL's regulator Clearly, should HAL face financial distress, there is every chance of a delay to expansion, or at worst, expansion not being completed at all. The hospitals funded by Carillion remain part built. The same must not be allowed to happen at Heathrow.

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Diversification of capital expenditure should make financial distress less likely

As we have made clear, there is no requirement in the ANPS that HAL carries out all the expenditure associated with expansion. In fact, the CAA12 is explicit that terminal competition is envisaged, as recommended by the Competition Commission in 2009.

The scale of the capital expenditure being proposed represents multiples of Heathrow's Regulatory Asset Base, thereby creating a degree of financial risk. We note that the 2015 Airports Commission recommendations concluded that the project, as proposed by HAL, was financeable. The project currently being promoted by HAL is a very different scheme to that approved by the Airports Commission. We note from the CAP1812 consultation on affordability and financeability that the CAA considers that there are credible scenarios where the expansion project remains affordable and financeable. However, the CAA also concludes that there are scenarios that would threaten the financial ratios being modelled by the CAA.

Allowing the project to be split into two substantial capital expenditure programmes, one by HAL and one by Heathrow West, would reduce the financial exposure of the overall expansion programme. This would allow expansion to be delivered earlier, and in a more cost-efficient way, than HAL. As well as strengthening the financial resilience of the overall project, the project would bring the benefits of competition to Heathrow airport, which would, we contend be to the benefit of passengers and airlines.

We are happy for this submission to be published.

Heathrow West Ltd

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