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Heathrow

Funding An Expanded Heathrow

31 July 2025

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Santander
Corporate & Investment Banking

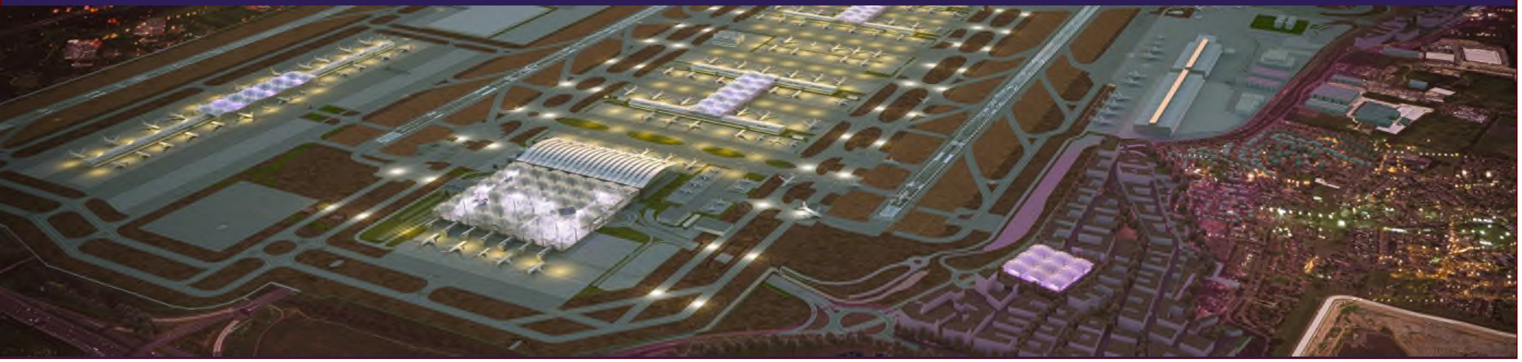
FRESHFIELDS

1 Introduction, Evaluation Process and Shortlisting Models

2 Assessment of Shortlisted Models

3 Conclusion and Recommendation

4 Disclaimer



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Introduction

Heathrow engaged **Santander** and **Freshfields** as advisers to review and evaluate potential **funding models** to **privately finance** the **expansion programme** at the **most efficient cost**

Project overview: The advisers carried out an initial survey of 8 funding models seen in UK and global infrastructure projects, assessed these models against the evaluation criteria set out on page 5 and shortlisted 4 options for detailed review

Objective: To evaluate potential funding models against the criteria set out on page 5 to compare their suitability. The task was not to determine what level airport charges should be set at or the WACC which should apply, but to identify a viable funding model to deliver private financing for the expansion programme from debt and equity investors at the most efficient cost possible

Contextualising risks: There are many fundamental risks that will be faced by Heathrow and its stakeholders through the expansion programme (see page 18) and it is essential that these risks be managed appropriately to deliver the programme most efficiently. The funding model can only help to manage some of the risks and many others will need to be considered and addressed further through the regulatory framework and other workstreams

Expansion context: The funding model should be able to be implemented within the timeline for overall delivery of an expanded Heathrow. It should also be able to facilitate additional revenue sources contributing to financing the expansion programme and helping reduce airport charges

Parameters: The advisers' review is based on the ratings thresholds as at the date of this report for investment grade ratings by Fitch and S&P (including an A- rating level in respect of Heathrow's Class A debt). The review was conducted using indicative modelling and modelled case assumptions provided by Heathrow on 23 July 2025 and does not consider any changes made to that modelling and assumptions after that date. Except as highlighted in relation to potential regulatory mechanisms for a single RAB, the report does not consider other regulatory changes which may be appropriate relating to capex governance, risk-sharing or incentive arrangements, nor any tax matters, project governance structures or wider procurement strategy

Initial Survey of Models

The advisers identified a range of funding models seen in major UK and global infrastructure projects (listed below) to survey

Model	Description
Regulatory Asset Based – Heathrow model	A Regulated Asset Base (RAB) model enables cost recovery and regulated returns on expansion and existing asset base investment through airport charges set by the CAA. Expansion programme's capex will be delivered within the current regulatory framework
Dual Regulatory Asset Based	Separates expansion RAB from existing operations, isolating expansion programme's capex, through the creation of an SPV financed separately with its own RAB but owned by existing Heathrow shareholders in a separate ring fence. Airport charges continue to be set by the CAA in respect of each RAB
Specified Infrastructure Project Regulations (SIPR) / TTT	This model is similar to a Dual RAB model and isolates expansion programme's capex, however the SPV is operated under its own distinct licence and owned and equity-funded by independent third-party shareholders outside of Heathrow's existing shareholder base and is non-recourse to Heathrow
Direct Procurement for Customers (DPC)	The DPC model enables competitively tendered, third-party financing and delivery of large infrastructure projects, transferring risk and driving efficiency in situations where it can deliver value for money for customers. No direct regulatory oversight of DPC counterparty
Project Finance SPV	This model structures infrastructure delivery through a standalone SPV that raises non-recourse debt, with repayment tied to project cash flows. This approach isolates risk, attracts private capital, and enables long-term investment through clearly allocated contractual responsibilities
Public Private Partnership (PPP)	Publicly awarded competitive tender to select a private party to design, build, operate, maintain and finance public infrastructure throughout a defined concession period. Cost recovery through airport charges during operation, with performance mechanisms to adjust revenue and allow reasonable returns that are guaranteed by the government
Large Airport Expansions (e.g., JFK, Riyadh)	An operator treats expansion programme and related assets as its own enterprise, recovering costs from commercial and aeronautical revenues outside of the existing regulatory revenue allowance, and supported in certain examples by public sector subsidies and risk sharing agreements
Cap/Floor	The model is common in the UK interconnector market and ensures bounded prices and returns for customers and investors. Revenues above the cap return to consumers through a reduction of future prices, and the difference when revenue is below the floor is compensated by the government or customers

Evaluation Process

Once identified, the advisers carried out the following evaluation process to evaluate and shortlist options

1. **Evaluation Criteria:** Advisers agreed a set of key criteria for the most suitable funding model to deliver the expansion programme from a financing and regulatory perspective:

Timely delivery for economic growth	Financeable for lenders	Value for Money for customers	Investable for equity investors	Financially independent from government	Efficient delivery of project and integration of operations
• Prioritises timely implementation • Works to timeline of DCO process completing by 2029	• Maintains a strong investment grade (IG) profile for Heathrow which includes a buffer appropriate to scale and nature of risks • Enables debt investors to lend at scale on competitive terms	• Delivers financing of the expansion programme at the most efficient cost possible	• Promotes investment from private capital • Facilitates competitive and predictable returns on equity compared to other global infrastructure projects	• Privately financed, market-led approach to minimise need for financial support from government	• Minimises business interruption and complexity of interface agreements

2. **Initial survey:** Advisers surveyed funding models used for major infrastructure projects in the UK and globally – see page 4

3. **Shortlist:** Advisers shortlisted four options for detailed review by discounting options which are inconsistent with the above evaluation criteria – see page 6

4. **Evaluation:** Advisers analysed each shortlisted option against the above evaluation criteria to assess its suitability to finance the project, based on ratings thresholds as at the date of this report, qualitative analysis and using modelled case assumptions provided by Heathrow on 23 July 2025 – see pages 9 to 14

Shortlisting potential options

The advisers identified 4 models to discount primarily due to their reliance on various forms of government support and shortlisted 4 options for further analysis

Model	Timely delivery for economic growth	Financeable for lenders	Value for Money for customers	Investable for equity investors	Financially independent from government	Efficient delivery for Heathrow operations
Project Finance SPV	Significant governance, regulatory and structuring complexity could cause delays	Only financeable with investment grade (IG) rating through **Heathrow guarantee and significant debt and equity pre-funding**	Significant pre-funding and/or sub-IG SPV results in higher cost of debt and overall funding cost	Returns depend on achieving a **bespoke regulatory regime incentivising efficiency** and strong **equity support**	Precedents include **bespoke government support / financial backing** for cheaper financing, likely given complexity & scale	Complex interface between existing regulated asset base and SPVs may reduce efficiency
Public Private Partnership (PPP)	Potentially slow procurement process and structuring complexity could cause delays	Financeable, if backed by robust government support and appropriate risk sharing	Value for Money is a key consideration for any PFI/PPP	Predictable returns but these are capped due to risk sharing and government support	**Significant financial support from government (e.g revenue and guarantees)** required for PPPs	Complex interface between existing regulated asset base and SPVs may reduce efficiency
Large Airport Expansions (e.g., JFK, Riyadh)	Risk of delays from stakeholder coordination and implementation of regulatory requirements	Would depend on final structure and level of risk retained	Would depend on final structure and level of risk retained	Would depend on market-based vs government backed support	**Financial support from government** likely required based on precedents	Complex interface between existing regulated asset base and SPVs may reduce efficiency
Cap/Floor	Not included in existing framework, requiring regulatory amendments	Hybrid treatment with some risk transferred outside of the project; appropriate price cap/floor levels key for financeability	Protects customers from price increases above the predetermined cap	Cap/Floor provides certainty on returns within a range but minimises incentives for outperformance	**Financial support from government** likely required to cover floor price breaches	Full Heathrow control retained, minimising risk of operational and interface inefficiencies

The following 4 models were shortlisted and analysed further in pages 9 to 14:

- **Dual Regulatory Asset Based**
- **Specified Infrastructure Project Regulations (SIPR) / TTT**
- **Direct Procurement for Customers (DPC) – for part / all of expansion programme**
- **Regulatory Asset Based – Heathrow model**

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Feasibility

Key reason for discounting

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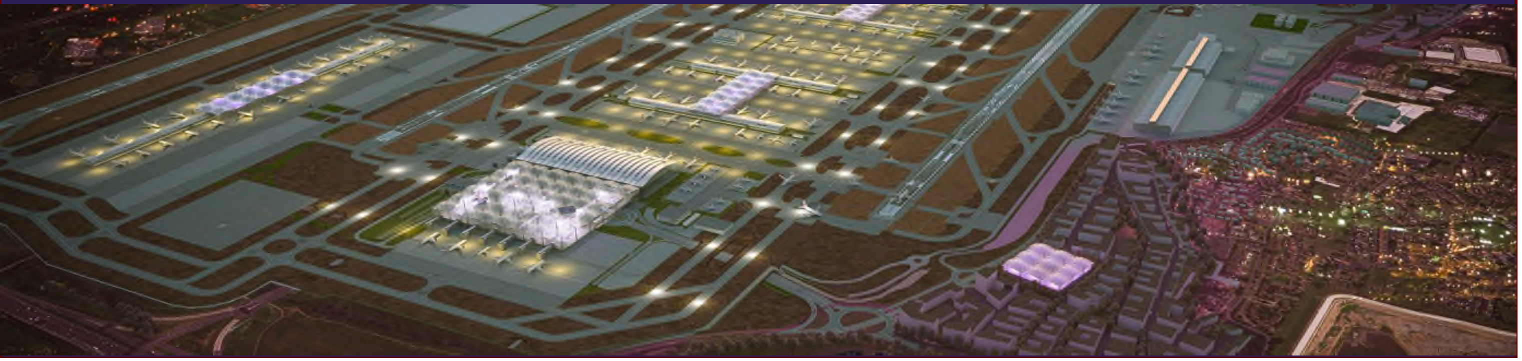

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Shortlisted Models explained

Advisers looked in detail at the following 4 shortlisted options

Dual RAB model

A separate sub-group & RAB in the wider Heathrow group

- Distinct development financing by a new sub-group within Heathrow corporate group, with a separate security package, distinct creditors and priority claim to revenue for construction
- Regulated by the CAA with its own RAB ascribed to its initial assets that would grow during the expansion programme
- Bespoke regulatory framework with new licence or HAL licence modifications

Specified Infrastructure Project Regulations

A RAB-based model (Thames Tideway Tunnel)

- An Infrastructure Partner (IP), using an SPV outside Heathrow's group, appointed in a competitive tender process to design, build and finance (and potentially operate and maintain) assets
- IP granted bespoke licence and directly regulated by CAA, with its own RAB ascribed to its initial assets (owned by IP) that would grow during the expansion programme
- Bespoke regulatory framework required with new licence for the IP
- IP raises own debt and equity, involving equity procurement process and distinct development financing of IP, with a separate security package, distinct creditors and priority claim to revenue for construction

Direct Procurement for Customers

A design-build-finance model with external contractor(s) for all/parts (DPC)

- DPC Partner(s), being one or more third parties outside Heathrow's group, would be contracted by Heathrow following a competitive tender process to deliver all or discrete, separable parts of the expansion programme
- DPC could be used to design, build and finance (and potentially operate and maintain) certain assets
- DPC Partner(s) would not be licensed nor directly regulated by the CAA nor have a separate RAB
- Bespoke regulatory framework required
- DPC Partner(s) raise distinct debt and equity
- DPC Partner(s) earn revenue paid by Heathrow as fees during contract period and an end of concession payment

Single RAB model

Existing Heathrow funding model

- Financing under HAL's existing secured ring-fenced financing platform
- New creditors would rank *pari passu* with existing HAL creditors and benefit from a combined covenant, guarantee and security package (over all HAL assets and revenue)
- Regulated by the CAA with HAL's existing RAB, which would grow during the expansion programme
- The existing regulatory model could be enhanced with potential regulatory mechanisms to increase cashflow predictability and smooth airport charges (see page 14 for further details)

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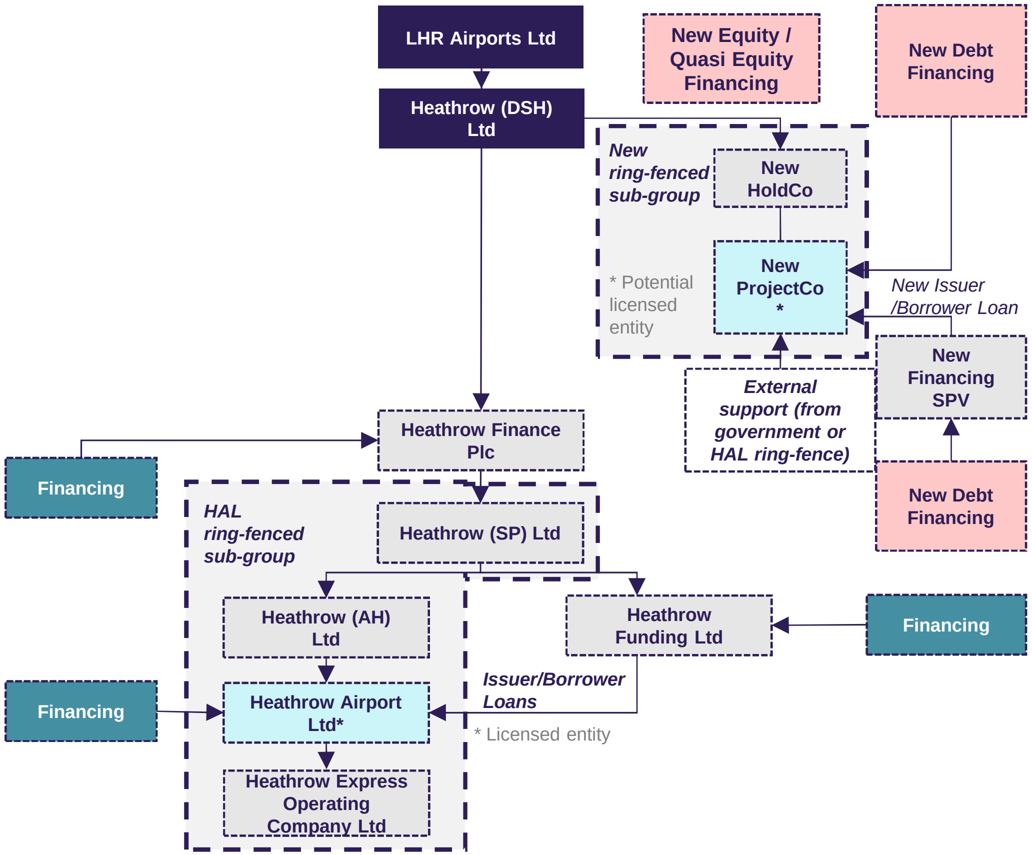
1. Assessing Dual RAB

A separate sub-group and RAB within the wider Heathrow group

Structure



Assessment

See Appendix for more detail

Less efficient financing

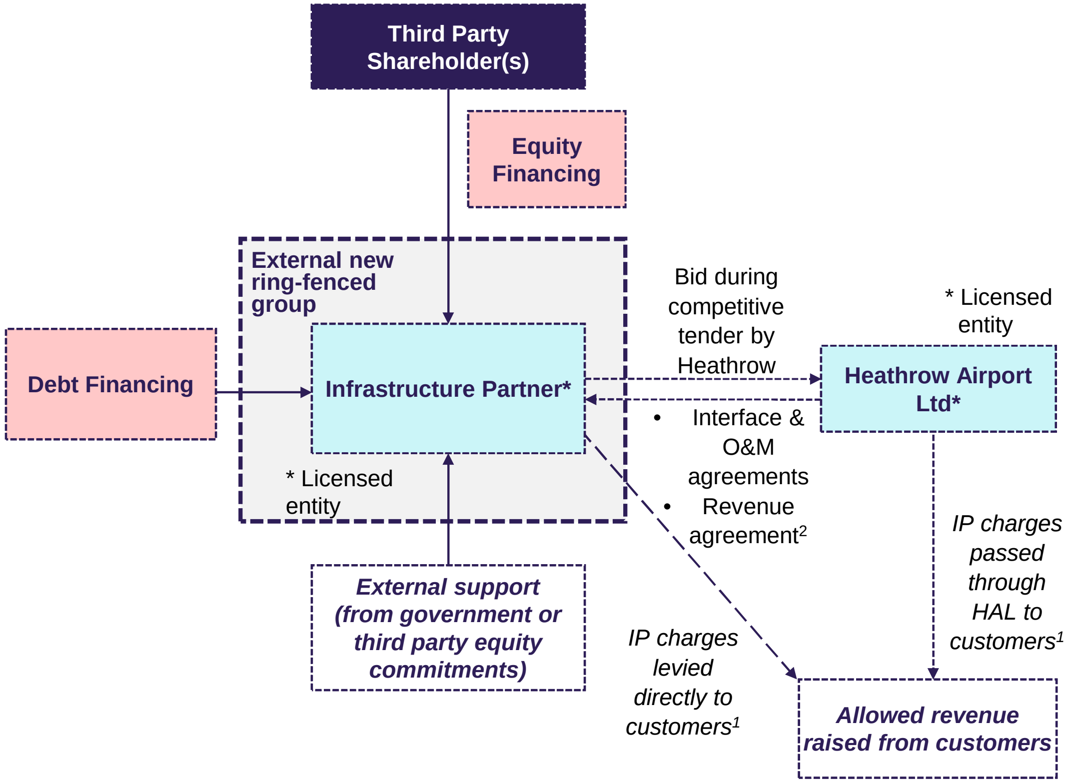
- ✗ To raise the amount of debt needed, an **investment grade rating** would be required by the market, which is likely to need:
  - Significant **committed funding upfront** from debt and equity investors (incurring funding costs earlier than when required), including a buffer for potential cost overruns; **and**
  - Material **financial support from government**; and/or
  - **Guarantees** from Heathrow Airport Limited (i.e. no ring-fencing of construction risk)
- ✗ With a sub-investment grade rating, the cost of debt would be **more expensive**
- ✗ Without support from HAL or government, would **increase airport charges** and **reduce equity returns**

- ✗ Risks **extra costs, potential delay and uncertainty** by:
  - Potential need for bespoke licence from CAA
  - Reorganisation of HAL assets
  - Obtaining any necessary consents from existing creditors

2. Assessing Specified Infrastructure Project Regulations (SIPR)

A RAB-based Thames Tideway Tunnel (TTT) style model

Structure



Note: This is the same structure as dual RAB but with third party ownership of the Infrastructure Partner

Note: (1) IP charges could be levied directly to airlines or passed through HAL, provided IP creditors have a priority claim in respect of the revenue stream; (2) Revenue agreement required if IP charges are passed through HAL to customers

Assessment

See Appendix for more detail

✓ Could **isolate construction risk** from Heathrow's existing business and remove the additional debt burden from Heathrow's balance sheet

Less efficient financing

✗ To raise the amount of debt needed, an **investment grade rating** would be required by the market, which is likely to need:
- Significant **committed funding upfront** from debt and equity investors (incurring funding costs earlier than when required), including a buffer for potential cost overruns; **and**
- Material **financial support from government**

✗ Without government support, would **increase airport charges** and **reduce equity returns**

✗ Risks **extra costs, potential delay and uncertainty** due to equity procurement process, need for bespoke licence from CAA & potential legislation, and reorganisation of HAL assets / creditor consents

Example: Unlike the expansion programme, the only SIPR project (TTT) and similar market examples (e.g. Sizewell C) have involved:
- A distinct and separable asset from existing operations
- Material financial support from government
- Regulatory and legislative change over ~1-3+ years followed by tender/licence approval processes over ~1-2.5+ years

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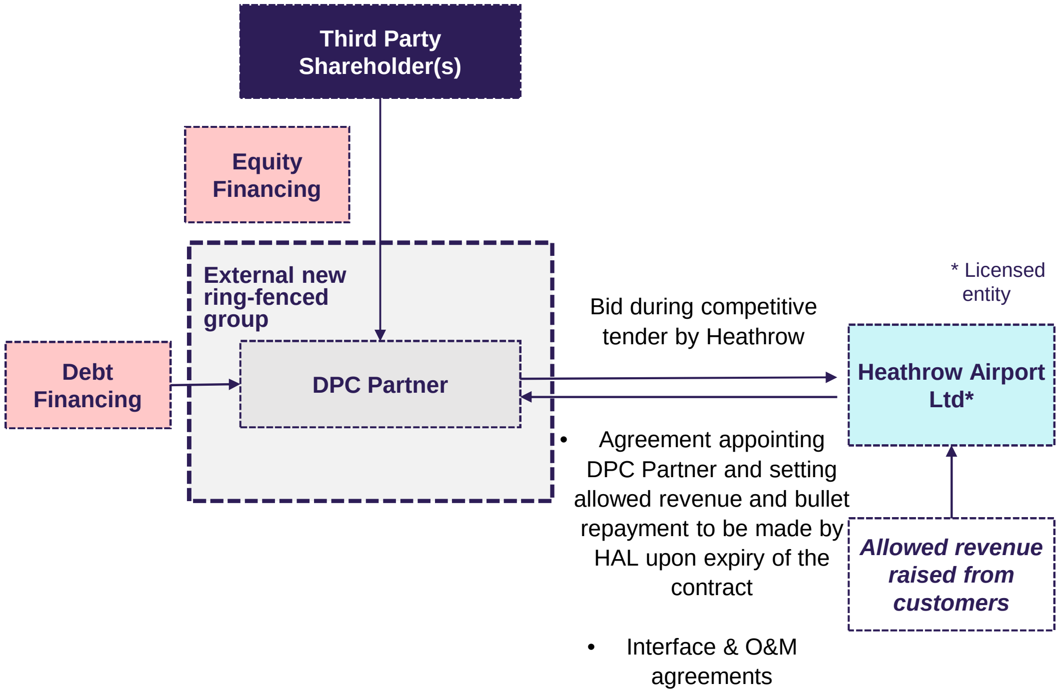
3A. Assessing Direct Procurement for Customers (DPC) for full programme

A design-build-finance model with external contractor(s) for **all** of the expansion programme

Structure



Note: This is the same structure as DPC for non-core parts of the programme as the difference depends on the assets to be developed by the DPC Partner

Assessment

See Appendix for more detail

Less efficient financing

- ✗ Requires significant **committed funding upfront** from debt and equity investors (incurring funding costs earlier than when required) including a buffer for cost overruns (which is likely required for an investment grade rating), causing significant **execution risk**
- ✗ Despite introducing competition, still risks **increasing airport charges** due to the scale of upfront funding required

- ✗ Requires a significant **end of concession payment** with a single DPC provider of an unprecedented and potentially unmanageable size, unless payment is staggered – causing significant **implementation risk**

- ✗ Likely requires **risk-sharing of potential liability for cost overruns** between Heathrow and one or more third party providers (i.e. ineffective risk transfer)

- ✗ Risks **extra costs, potential delay and uncertainty** due to set up time for tender process, external equity, discrete financing, new regulatory framework (and lack of direct regulation), and reorganisation of HAL assets / creditor consents
  - **Example**: the largest market example, HARP by United Utilities, took ~2.5 years between UU starting the tender process and announcing its preferred bidder (which is a smaller value and discrete project compared to an expanded Heathrow)

- ✗ Theoretically could involve multiple DPC counterparties to deliver an expanded Heathrow overall at a competitive cost, though in practice this would be **incompatible** with DPC principles of discreteness and lack of regulation, and could create **significant execution risk** (due to the size, strategic importance and integrated nature of an expanded Heathrow)

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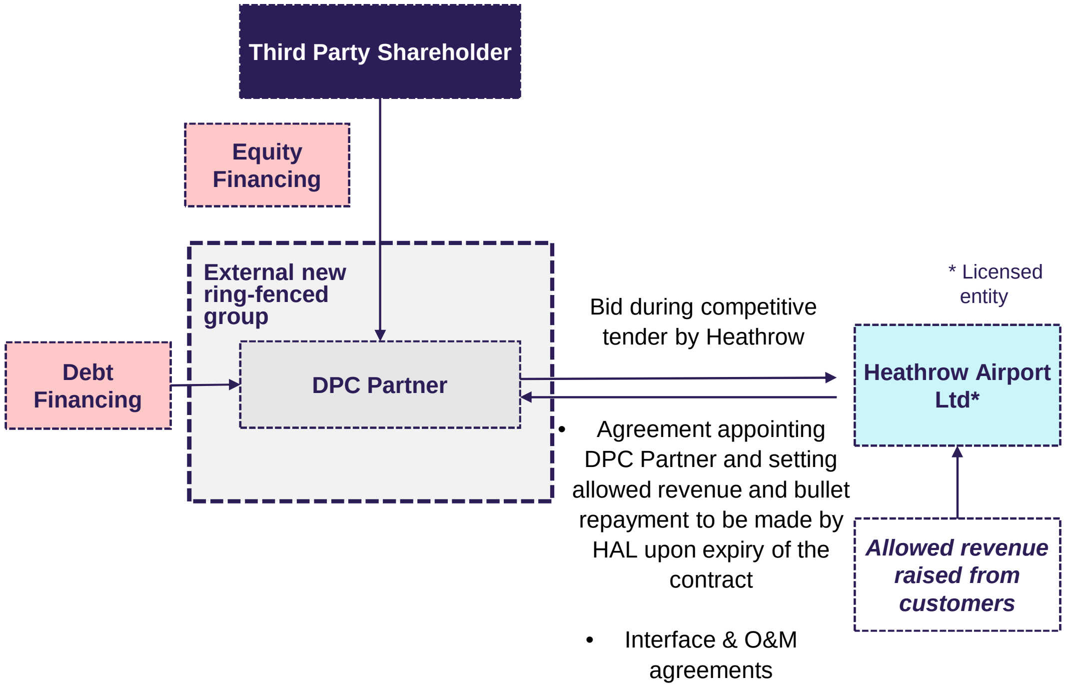
3B. Assessing Direct Procurement for Customers (DPC) for non-core parts

Design-build-finance model with external contractor(s) delivering **non-core discrete and separable parts** of the expansion programme

Structure



Note: This is the same structure as DPC for all of the programme as the difference depends on the assets to be developed by the DPC Partner

Assessment

See Appendix for more detail. Assessment will **vary** depending on which aspects are subject to the DPC contract

✓ Could **reduce overall cost** if:

? Any DPC consortium bids offer value for money with investor IRRs (Internal Rates of Return below ~15%) in line with market precedent (to reflect efficient delivery costs and appropriate risk transfer as below)

? The DPC package achieves **effective transfer** of construction and financing risks to DPC partner

✓ **Removes some of the additional debt burden** from Heathrow's balance sheet

✓ Allows **flexible allocation of responsibilities** for the design, build, financing, operation and maintenance of **non-core, separable and discrete** assets under the counterparty's appointment so that **efficiencies of integrated operations** at Heathrow can be maintained

✗ Risks **extra costs, potential delay and uncertainty** due to set-up time for tender process, external equity, discrete financing, new regulatory framework (and lack of direct regulation), and reorganisation of HAL assets / creditor consents

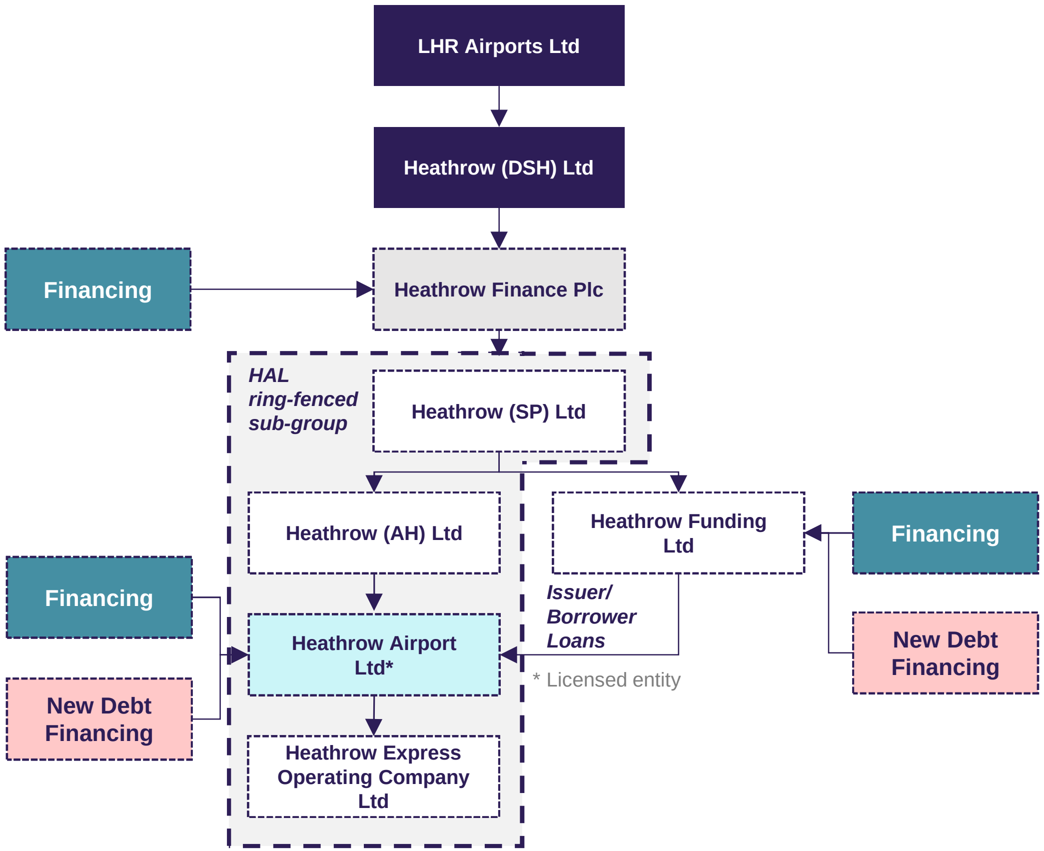
✗ Risks **regulatory delays** and issues regarding the **applicability of projects** proposed for delivery via DPC

- **Example:** two other DPC projects specified at PR19 by Ofwat have not proceeded as planned, with one now being delivered in-house owing to concerns that using the new DPC approach may delay the water company meeting its obligations
- **Example:** one PR24 specified DPC project by Ofwat will also be delivered in-house as potential bidders found the project was too integrated with the water company's existing facility

4. Assessing Existing Single RAB model

The existing Heathrow funding model

Structure



Assessment

See Appendix for more detail

Efficient financing

- ✓ Can **raise scale of debt** within HAL **investment grade rating thresholds** (including an A- rating level in respect of HAL's Class A debt), benefitting from **proven financing platform** and **efficient cost of debt**
- ✓ Enables **reinvestment of dividend capacity** by shareholders
- ✓ Capable of financing expansion programme in a **cost-efficient manner** within the **current regulatory framework**

- ✓ Can **reduce and/or smooth airport charges and increase cashflow predictability** during the implementation of the programme further through specific **regulatory mechanisms** (see page 14)

- ✓ **Avoids complexity and associated cost and risk of delays** of setting up separate regulatory regimes, potential reorganisation of assets / creditor consents and managing shared services, governance and arrangements with separate shareholders

- ✓ **Minimises likelihood** of needing **material financial support from government**
- ✓ Restricts potential support required to a limited and bespoke package to address exceptional, expansion-related risks

- ✗ Does not ring-fence Heathrow's existing business from **construction risk**

- ✓ Potential to **reduce airport charges longer term** via **a hybrid till model** e.g. for investments in peripheral commercial property assets

4. Regulatory Mechanisms to enhance the Single RAB model

The regulatory framework needs to provide **sufficient certainty** to encourage debt and equity investors to commit to finance the expansion programme - facilitating more efficient funding and thereby reducing airport charges. Therefore, certain regulatory mechanisms have been considered to increase certainty/cashflow predictability & reduce/smooth airport charges during the implementation of the programme. Other regulatory mechanisms should be explored further in case additional risks faced by the project can be mitigated (see page 18)

Levers for Cashflow Predictability

Adopt longer regulatory periods during the implementation of the programme

- **Reduces regulatory risk**
- **Improves cashflow visibility for debt sizing and investor confidence**
- **Allows certainty for fixed items (e.g. cost of capital) together with reopeners for other variables (e.g. traffic, operating costs, commercial revenues)**

Deferred revenue

Defer recovery of expansion programme capex and revenue into future years

- **Reduces peak airport charge through longer depreciation and WACC uplift periods**
- **Assures a net neutral return for shareholders over time**

Blended WACC/Dual WACC

Replace the single WACC for a blended WACC or Dual WACC pricing structure

- **Applies different rates to greenfield / brownfield assets to reflect greenfield project risk for the associated expansion programme's RAB during the implementation of the programme**
- **Delays increases to airport charges compared to a single WACC structure**

DPC for Discrete Projects

Explore a Direct Procurement for Customers model for discrete, separable, non-core projects within the expansion programme

Enables competitive market testing of developers and targeted risk transfer, which could reduce costs and airport charges and deliver project within proposed timetable if sufficiently early decisions are taken by the CAA to set up a new DPC framework

Hybrid Till Flexibility

A hybrid till proposal which involves removing certain revenues e.g. specific peripheral commercial property investments from the single till regulatory framework to facilitate investment

This regulatory lever could reduce costs longer term. The precise design is currently under consideration as part of the H8 price control process

Regulatory lever | Primary mechanisms | Complimentary mechanisms

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Evaluating the Shortlisted Options explained (1 of 2)

	Dual RAB A separate sub-group & RAB in wider Heathrow group	**Specified Infrastructure Project Regulations** RAB-based Thames Tideway Tunnel (TTT) style model	**Direct Procurement for Customers** Design-build finance model with external contractor(s) for full programme
Timely delivery for economic growth	× Potential bespoke CAA licence likely to be time-consuming and increase potential for delays × Higher likelihood of costly and lengthy creditor consent processes × Requires new sub-group and financing, with scope for considerable disagreement and uncertainty over reorganisation of HAL assets	× Risk of potential delay, extra costs and uncertainty due to equity procurement process, reorganisation of HAL assets to external SPV and creditor consent processes more likely × TTT precedent and similar projects (Sizewell C) required time-consuming set-up (regulatory and legislative change over ~1-3+ years followed by tender/licence approval processes over ~1-2.5+ years)	× Risk of potential delay, extra costs and uncertainty due to tender process, reorganisation of HAL assets to DPC and creditor consent processes more likely, particularly where multiple DPC counterparties involved × Regulatory change risks potential delays and extra cost × Largest market example (HARP by United Utilities) took ~2.5 years between UU starting the tender process and announcing its preferred bidder (which is a smaller value and discrete project compared to an expanded Heathrow)
Financeable for lenders	× Unlikely to obtain IG rating and raise scale of debt required without significant committed funding upfront from debt & equity investors (with gearing increasing over time as construction risk reduces) × HAL guarantees may be needed, undermining ring-fencing purpose	✓ Removes additional debt burden from HAL ✓ Isolates potential liability for cost overruns and construction risk from HAL (assuming guarantees are not provided) × Likely to require significant committed funding upfront from debt/equity investors to achieve IG rating and raise scale of debt required	× Requires significant committed equity/debt funding upfront (incurring funding costs earlier than when required), including cost overrun buffer – causing significant execution risk – and a significant end of concession payment for HAL unless staggered – causing significant implementation risk × Likely requires risk-sharing of potential liability for cost overruns between HAL and third party provider(s) negates risk transfer and neutrality for HAL
Value for Money for customers	✓ Separate RAB framework with an allowed rate of return commensurate with construction risk × Higher cost of upfront financing relative to single RAB could drive up airport charge (worse if sub-IG)	✓ Introduces competition into delivery of expansion programme × Without government support, higher cost of upfront financing relative to single RAB would drive up airport charge (worse if sub-IG)	× DPC for full programme with one or more partners is likely to be commercially and financially unworkable, as despite introducing competition and leveraging private sector expertise, it still risks increasing airport charge due to the scale of upfront funding required
Investable for equity investors	✓ Separate RAB framework with an allowed rate of return commensurate with construction risk × Without support from HAL or government, initial capitalisation need with higher cost of upfront financing relative to single RAB would harm equity returns × Could fail to ring-fence HAL	✓ Uses a RAB-based framework precedent, with the benefit of third party equity × Without government support, initial capitalisation need with higher cost of upfront financing relative to single RAB means third party shareholders would fund a significant share of capex, reducing investment merits	× Initial capitalisation need with higher cost of upfront financing relative to single RAB means third party shareholders would fund a significant share of capex, reducing investment merits
Financially independent from government	× Unlikely to obtain IG rating and raise scale of debt required without material financial support from government (and/or HAL guarantees plus upfront committed funding)	× Unlikely to obtain IG rating and raise scale of debt required without material financial support from government (plus upfront committed funding) – e.g. TTT	✓ Fully market-led approach, minimising the likelihood of needing material financial support from government × Requires some regulatory changes and modifications to HAL's licence
Efficient delivery of project and integration of operations	× Complex structure with likely governance, regulatory, legal and operational challenges (e.g. as a result of splitting integrated operations)	× Unlike similar market examples e.g. TTT, expanded Heathrow's assets are not distinct & separable from existing operations × Any risk of potential operational challenges/inefficiencies would need to be mitigated with shared services agreements and other contractual arrangements	× While in theory multiple DPC counterparties could be contracted to deliver at competitive cost, in practice size, strategic importance and integrated nature of an expanded Heathrow makes approach incompatible with DPC principles of discreteness and creates significant execution risk × Potential operational challenges/inefficiencies would need to be managed

Key reason for discounting

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Evaluating the Shortlisted Options explained (2 of 2)

	Single RAB **Existing Heathrow funding model**	**Direct Procurement for Customers** **Design-build-finance model with external contractor(s) for non-core parts**
Timely delivery for economic growth	✓ Avoids complexity, extra cost and risk of potential delays which could stem from (i) separate regulation, (ii) potential reorganisation of an expanded Heathrow's assets and (iii) managing shared services, governance & agreements with separate shareholders ★	✓ DPC packages for discrete/separable, lower value and non-core parts of expansion programme are less likely to require material reorganisation of HAL assets to external counterparties / costly creditor consent processes × Set-up time (tender process, external equity), regulatory change and potential implementation issues risk potential delays and extra cost × Largest market example (HARP by United Utilities) took ~2.5 years between UU starting the tender process and announcing its preferred bidder (which is a smaller value and discrete project compared to an expanded Heathrow)
Financeable for lenders	✓ With phasing of capex profile / scaling up debt over time, model can raise level of debt required (including USD liquidity) within IG rating & covenant thresholds (including A- for Class A debt), with equity contributions as needed ✓ Benefits from HAL's proven financing platform and efficient cost of debt ★	✓ Can protect HAL's IG rating and remove extra debt burden if DPC contract transfers construction & financing risk of asset to DPC partner effectively (more likely for discrete/separable, lower value and non-core/less strategic parts of the expansion programme) ★
Value for Money for customers	✓ Capable of financing expansion programme in a cost-efficient manner within current regulation ✓ Reduce and/or smooth airport charges and increase cashflow predictability during the implementation of the programme further through regulatory mechanisms ✓ Airport charges may be reduced further in the long term from hybrid till investments e.g. in specific commercial property assets	✓ A DPC model has potential to reduce airport charges by contracting skilled consortiums for delivery of discrete aspects of expansion programme ✓ Introduces competition into discrete parts of expansion, potentially lowering costs if DPC partner bids at competitive rates ★
Investable for equity investors	✓ Access to HAL's balance sheet for phased equity contributions, including reinvestment of dividends × Does not ring-fence Heathrow's existing business from construction risk. As with any model, agreement among stakeholders will need to be reached regarding potential cost overruns (above any agreed contingency amounts), procurement strategy and project governance to manage risk ★	✓ Discrete DPC projects could attract new equity investments while keeping the impact on Heathrow's shareholders to a minimum (if DPC partner bids at competitive rates) ★
Financially independent from government	✓ Structure minimises the likelihood of material financial support from government being needed ✓ Restricts potential support required to a limited and bespoke package to address exceptional, expansion-related risks	✓ Fully market-led approach, minimising the likelihood of material financial support from government being needed ✓ Regulatory precedents available e.g. from the water sector × Regulatory changes and modifications to HAL's licence will be required given lack of direct regulation
Efficient delivery of project and integration of operations	✓ Enables alignment of complex and integrated operational and delivery programmes to minimise cost and avoid additional integration workstreams	✓ Allows flexible allocation of responsibilities for design, build, financing, operation and maintenance of non-core, separable and discrete assets under DPC partner's appointment so efficiencies of integrated operations at Heathrow can be maintained

★ **Key benefit of the model**

Risk Areas for Future Stakeholder Engagement

An **indicative, non-exhaustive** list of risks associated with expanding Heathrow is set out below. Investors will be concerned with a broad range of risks of which the funding model can only seek to manage/mitigate some. All stakeholders will need to engage to seek to address the broader risk landscape through the regulatory framework and other means

Key Risks	Description
Cost	Inflated costs and overrun risks across projects e.g. arising in individual contract scopes and throughout supply chain
Delay / Termination	Delays to completing (e.g. as a result of planning) or termination of the project due to change in government policy or otherwise
Project-on-Project	Delays or issues with delivery of expansion programme because of interplay between different aspects and how they fit together
Construction	Increased costs or defects arising in individual contract scopes
Operational / Interface	Fragmentation of operations and managing interruptions from expansion programme alongside existing airport operations
Lender Cooperation	Lack of certainty around lender approvals
Regulatory & Compliance	Failing to ensure (i) certainty of regulation / legislation and timely buy-in; (ii) compliance with existing obligations; and (iii) flexibility over various market cycles
Financing	Increased financing costs if Heathrow's investment rating is not maintained
Capital Markets	Risks of volatility, cost of debt at scale, competing large scale project cannibalisation and FX risk linked to requirement of US liquidity vs GBP revenues and underlying swap constraints in bank market

Key Risks	Description
Airline Demand	Lower usage due to lack of demand and/or higher airport charges
Political	Shifting objectives of different governments and loss of political support
Long-Term Assets	Failing to preserve returns for investors during life of project in an evolving landscape
External Shocks	For example, the COVID-19 pandemic
Taxpayer	In case of significant overruns or disputes requiring bailout
Operational Ramp Up	Slower ramp up than expected
Market Capability and Capacity	Insufficient market-based capacity and capability to deliver on time and on budget (e.g. saturated domestic supply chains and impact of global commodity costs & fluctuations)
Environmental challenge	Challenges from sophisticated groups that may cause delays, harm market appeal and affect regulatory/political support
Social opposition (related to land acquisition)	Public opposition could impact effective project delivery

Only certain risks would be mitigated or managed more effectively by using the existing single RAB model and/or not pursuing an alternative funding model

Recommendation

The funding model which is **most suitable** to **privately finance** an expanded Heathrow at the **most efficient cost** is:

Single Regulatory Asset Base (RAB) model
+ With potential **regulatory mechanisms** which need approval / support of the CAA

Heathrow's single RAB model offers the best route to finance the expansion programme privately, in a timely and stable way, with efficient debt/equity investment and airport charges reduced and/or smoothed by certain proposed regulatory mechanisms

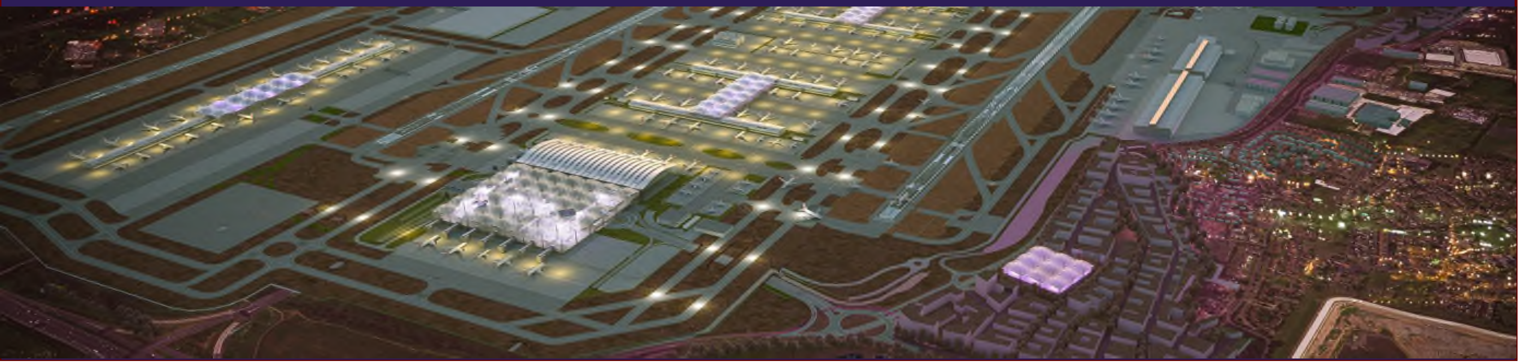
The model can mitigate or manage certain risks faced by the expansion programme more effectively (e.g. risks relating to financing, capital markets, regulatory and compliance, lender cooperation and operational arrangements) within the wider risk landscape

1 Introduction, Evaluation Process and Shortlisting Models

2 Assessment of Shortlisted Models

3 Conclusion and Recommendation

4 Disclaimer



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Thank You

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Simple Personal Fair

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Santander Credentials

Leading global infrastructure financing house with relevant experience in airports

Airports

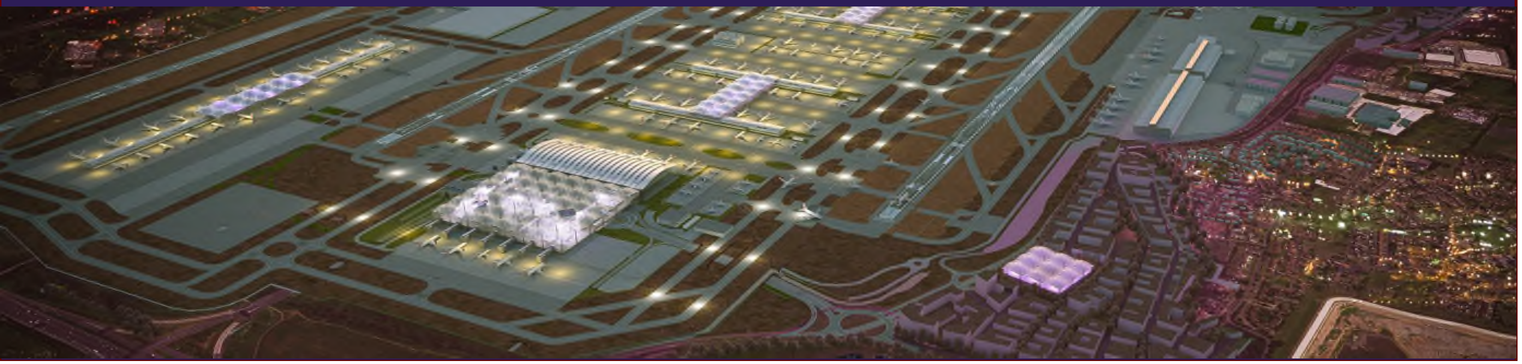
2025	London Gatwick – Refinancing	Arranger, lender
2024	Ardian (with PIF) acquired a 38% stake in Heathrow from Ferrovial	Financial advisor to Ardian & PIF
2024	Zurich Airport – Infrastructure Debenture I Aeroporto de São Gonçalo do Amarate	Financial advisor
2024	PSP Investments, Avialliance – Project Alphabet Acquisition of AGS	Acquisition Financial Advisor
2023	Zurich Airport – Auction I Aeroporto de São Gonçalo do Amarate	Financial advisor
2023	Refinancing – Edinburgh Airport, Global Infrastructure Partners	Lender
2022	Refinancing RCFs – Heathrow (Making every journey better)	BMLA, Coordinator, ESG Coordinator
2022	The New Terminal One (JFK International Airport) – JFK NTO Construction financing for JFK's New Terminal One	Senior Managing Agent & Lender
2022	Aéroports de Paris Management, Astaldi, Vinci Airports – Santiago Airport Refinancing	Structuring Agent & Lender
2021	Signature Aviation Leveraged buyout by Blackstone, GIP and Cascade Term Loan B	Joint Lead Arranger, Joint Bookrunner
2021	Fraport – BNB Bank Guarantee | Fraport Brasil S.A. Fortaleza Airport	Guarantor
2020	Fraport – BNB Bank Guarantee | Fraport Brasil S.A. Fortaleza Airport	Guarantor
2017	Zurich Airport – Florianopolis Airport Auction Financial Advisory	Auction Financial Advisor
2017	J.P.Morgan Asset Management, Partners Group – Billy Bishop, Billy Bishop Toronto City Airport	Lender

Other infra-assets

2024	Fjord1, DIF Capital Partners, KLP, EDF Invest – Acquisition of Ferry Operator (Floating Bridges)	Underwriter, MLA, DC Provider
2024	Fair Market Value Capital Partners, TD – Acquisition of a minority stake in PSA Italy	M&A & Debt Advisor, UW of Bridge Facility
2024	H2 green steel – "Boden" Greenfield hydrogen steel plant in Sweden	Mandated Lead Arranger and Hedging Provider
2024	Gruppo Fininc, Sacyr – **Project A21** Bridge Loan	Sole structuring agent, arranger, Global Coordinator, Bookrunner, Bridge MLA and LC Provide.
2023	GridServe, Infracapital, TPG – **Project Piazza** The largest debt raise by a privately-owned CPO globally	Sole Financial Advisor, MLA & Green Structuring Bank
2023	Unión Vial Río Pamplonita (Una Compañía de Sacyr Concesiones) – **Project PACU** Pamplona Cúcuta Refinancing	Financial Advisor & Lead Arranger & Social Bond Structuring Agent
2023	Envision AESC – **Project Envision** Financing of the 1st EV battery Gigafactory in France	MLA, Lender, BPIAE & Sinosure Facility Agent, Green Loan Coordinator and Hedge provider

Source: Public information, Infralogic

Appendix – Further Information to Main Report



Shortlisted Models – Analysis (1 of 2)

Advisers' further analysis of less viable models summarised

Dual RAB model

A separate sub-group & RAB in the wider Heathrow group

- ✗ To raise the amount of debt needed, an **investment grade rating** would be required by the market, which is likely to need:
  - Significant **committed funding upfront** from debt and equity investors (incurring funding costs earlier than when required), including a buffer for potential cost overruns; **and**
  - **Material financial support from government**, which is assumed not to be available; and/or
  - **Guarantees** from Heathrow Airport Limited, which would undermine any ring-fencing of the project's construction risk (a key benefit of using this structure)
- ✗ With a sub-investment grade rating, the cost of debt would be **more expensive**
- ✗ Without support from HAL or government, would **increase airport charges** and **reduce equity returns**
- ✗ Risks **extra costs, potential delay & uncertainty** by:
  - Potential need for bespoke licence from CAA and amendment to HAL regulatory regime
  - Reorganisation of HAL assets to the sub-group
  - Obtaining any necessary consents from existing creditors

Specified Infrastructure Project Regulations (SIPR)

A RAB-based Thames Tideway Tunnel (TTT) style model

- ✓ Could isolate construction risk from Heathrow's existing business and remove the additional debt burden from Heathrow's balance sheet
- ✗ To raise the amount of debt needed, an **IG rating** would be required by the market, which is likely to need:
  - Significant **committed funding upfront** from debt and equity investors (incurring funding costs earlier than when required), including a buffer for potential cost overruns; **and**
  - **Material financial support from government**, which is assumed not to be available
- ✗ Without government support, would **increase airport charges** and **reduce equity returns**
- ✗ Risks **extra costs, potential delay & uncertainty** due to:
  - Equity procurement process
  - Need for bespoke licence from CAA and new regulatory regime over the Infrastructure Provider
  - Potential legislative change
  - Reorganisation of HAL assets to external SPV and existing creditor consents
- ✗ **Example:** Unlike the expansion programme, the only SIPR project (TTT) and similar market examples (e.g. Sizewell C) have involved: a distinct & separable asset from existing operations; material financial support from government; and regulatory and legislative change over ~1-3+ years followed by tender/licence approval processes over ~1-2.5+ years

Direct Procurement for Customers (DPC) for Full Expansion Programme

A design-build-finance model with external contractor(s) for full programme

- ✗ Requires significant **committed funding upfront** from debt and equity investors (incurring funding costs earlier than when required), including a buffer for cost overruns (which is likely required by the market for an IG rating), causing significant **execution risk**
- ✗ Requires a significant **end of concession payment** with a single DPC provider of an unprecedented and potentially unmanageable size, unless payment is staggered – causing significant **implementation risk**
- ✗ Likely requires **risk-sharing of potential liability for cost overruns** between Heathrow and one or more third party providers, undermining the effective risk transfer to that third party and neutrality benefit for Heathrow
- ✗ Theoretically could involve multiple DPC counterparties to deliver an expanded Heathrow overall at a competitive cost, though in practice this would be **incompatible** with DPC principles of discreteness and lack of regulation, and could create **significant execution risk** (due to the size, strategic importance and integrated nature of an expanded Heathrow)
- ✗ Despite introducing competition, still risks **increasing airport charges** due to the scale of upfront funding required
- ✗ Risks **extra costs, potential delay and uncertainty** due to:
  - Set-up time for tender process, external equity, discrete financing, which is exacerbated in circumstances where DPC is used to deliver full expansion programme by one or more counterparties
  - Need for a new regulatory framework
  - Reorganisation of HAL assets to external counterparties and existing creditor consents
  - **Example**: the largest market example, HARP by United Utilities, took ~2.5 years between UU starting the tender process and announcing its preferred bidder (which is a smaller value and discrete project compared to an expanded Heathrow)

Shortlisted Models – Analysis (2 of 2)

Advisers' further analysis of viable models summarised

Single RAB model

Existing Heathrow funding model

✓ Can raise scale of debt needed within HAL's **investment grade rating thresholds** (including an A- rating level in respect of HAL's Class A debt), benefitting from HAL's **proven financing platform and efficient cost of debt** by:

— Phasing expansion programme capex profile and RAB growth

— Implementing a fundraising strategy which scales up debt required over time (including USD liquidity) in compliance with HAL's financial covenant limits and other conditions under its financing (e.g. liquidity reserve requirements, hedging thresholds, permitted types of debt)

— Enabling additional equity contributions, including recycling of dividend capacity

✓ Capable of financing expansion programme in a **cost-efficient manner** within the current regulatory framework

✓ Could further through specific regulatory mechanisms (see page 25 for more detail) **reduce and/or smooth airport charges and increase cashflow predictability** during the implementation of the programme

✓ May **reduce costs longer term** via **a hybrid till model** for investments in e.g. peripheral commercial property assets

✓ **Avoids complexity** and **associated cost and risk of delays** given no need for:

— Separate regulatory regimes;

— New companies involving potential reorganisation of expansion-related assets;

— Shared services, governance and arrangements with separate shareholders

→ assuming delivery can be managed efficiently in-house in line with HAL's business covenants

✓ **Minimises** likelihood of needing **material financial support from government –** restricts potential support required to a limited and bespoke package to address exceptional, expansion-related risks

✗ Does not ring-fence Heathrow's existing business from **construction risk**. As with any model, agreement among stakeholders will need to be reached regarding potential cost overruns (above any agreed contingency amounts), procurement strategy and project governance to manage risk

Direct Procurement for Customers

A design-build-finance model with external contractor(s) for non-core parts (DPC)

Assessment will **vary** depending on which aspects of the expansion programme are subject to the DPC contract

✓ **Reduces overall cost** assuming:

?Any DPC consortium bids at competitive rates;

?The DPC package achieves effective transfer of construction and financing risk of the development to the counterparty – this is more likely for discrete/separable, lower value and non-core/less strategic parts of the programme;

?External development of the relevant asset is permitted under HAL's existing regulatory and financing frameworks – i.e. minimal reorganisation of Heathrow assets required

✓ **Removes some of the additional debt burden** from HAL's balance sheet

✓ **Allows flexible allocation of responsibilities** for the design, build, financing, operation and maintenance of **non-core, separable and discrete** assets under the counterparty's appointment so that **efficiencies of integrated operations** at Heathrow can be maintained

✗ Risks **extra costs, potential delay and uncertainty** due to:

- Obtaining any necessary creditor consents
- Set-up time for tender process, external equity, discrete financing
- Need for a new regulatory framework (and lack of direct regulation)
- Reorganisation of HAL assets to external counterparties

✗ Risks **regulatory delays** and issues regarding the **applicability of projects** proposed for delivery via DPC:

- **Example:** two other DPC projects specified at PR19 by Ofwat have not proceeded as planned, with one now being delivered in-house owing to concerns that using the new DPC approach may delay the water company meeting its obligations
- **Example:** one PR24 specified DPC project by Ofwat will also be delivered in-house as potential bidders found the project was too integrated with the water company's existing facility

Regulatory Levers explained

Advisers considered the regulatory mechanisms summarised below

Regulatory periods

HAL operates under 5-year regulatory price control periods which are overseen by the CAA who determines the maximum airport charge levied on airlines. The current price control period (H7) will run until 31 Dec 2026.

Increasing the length of price control periods during the construction period (whereby certain components of the price control are fixed with appropriate reopeners for others) would provide increased certainty of revenue entitlement, which would reduce regulatory risk and help attract necessary equity investment – with potential resulting benefit to the level of airport charges.

Any proposal will need to take account of the need to coordinate with the upcoming 2R H8 price control where the CAA has proposed that the price control period is five years.

Deferred revenue

A deferred revenue scheme would involve HAL deferring recovery of expansion programme capex and revenue into future years. This would reprofile HAL's revenue entitlement for the expansion programme.

It would be achieved via recognition of deferred revenue over the implementation of the programme being capitalised to the Regulated Asset Base (RAB) and returned to HAL by adjusting regulatory depreciation over time.

This mechanism is intended to smooth the impact of airport charge increases over time.

Blended WACC/Dual WACC

A WACC refers to the Weighted Average Cost of Capital and is a central component used by the CAA to set HAL's price control. It is intended to cover the costs of paying equity and debt investors for providing the capital HAL needs to operate and invest in its business.

Under the current regime, HAL's revenue entitlement is determined using a single RAB with a single WACC.

Moving from a single WACC to a Dual or Blended WACC would allow HAL to apply different rates to greenfield / brownfield assets to reflect greenfield project risk for the associated RAB during the implementation of the programme. By applying a higher WACC rate to a smaller asset base, this would delay increases to airport charges compared to using a single WACC, lowering cashflows early and thereby smoothing the impact of airport charge increases.

DPC for Discrete Projects

Direct Procurement for Customers (***DPC***) is a competitive delivery model designed to deliver major infrastructure projects more efficiently and at lower cost to consumers. It was primarily developed by Ofwat for the UK water sector.

In the water sector, a project is considered appropriate for DPC if it offers value for money for customers and satisfies discreteness criteria. In the context of Heathrow's expansion programme, it would involve external contractor(s) tendering to design, build and finance non-core parts of the expansion programme. The CAA could issue an allowed revenue direction to enable Heathrow to recover the costs payable to the DPC Partner from airlines. The DPC partner would not be licensed nor directly regulated by the CAA, nor have a RAB. The DPC partner would raise its own debt and equity.

Hybrid Till Flexibility

HAL is currently regulated using a single till model whereby both the costs and revenues of the aeronautical and commercial businesses are combined into one till to set airport charges. Hybrid till models can come in many forms, but these models work by deducting a proportion of commercial revenues from total revenues to calculate the price cap for airport charges. Hybrid tills therefore lead to some cross-subsidisation of the aeronautical business by the commercial business, but less than under the single till.

A limited form of hybrid till has been proposed by HAL for H8 in respect of certain commercial property, to incentivise investment in peripheral, commercial property assets which have been subject to underinvestment historically. This could incentivise fresh investment, reduce airport charges and benefit customers over time.