

**Heathrow**

## **Heathrow – CAA**

**Commercial Property Development**

30 April 2026



# Agenda

- 1 Background
- 2 Recap: Case for change
- 3 Recap: Proposed solution



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- 1 Background
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# Background

We identified chronic underinvestment in landside property and proposed trialling a new framework in H8 whereby risks are reallocated to unlock property investment while protecting the single till. We remain focused on jointly taking this forward with CAA and airlines.

## In CE and our H8 BP we suggested incentives need to change

- No commercial property investment at Heathrow in 20+ years (EBP aside) = parts of estate deteriorating and at risk of being unlettable due to non-compliance.
- This is despite intense development in the airport vicinity and developers manifesting interest in the opportunities at Heathrow.
- Theoretical comparison with an airport operating in open market showed current regulatory framework inadvertently dampens incentives for investments in commercial property.
- This delivers suboptimal outcomes for customers and passengers.
- We proposed exploring an off-RAB investment model e.g. with a revenue sharing mechanism **to protect airline interests whilst delivering net incremental benefits to the single till.**
- Airlines reactions were mixed. After a positive reaction during CE, they collectively rejected any changes to framework. Later, ██████████ has approached us and discussions continue.

## In November we proposed a win-win approach: more investment + no charge impact

- Within a **fixed capital envelope** investments in commercial property are not prioritised by Heathrow and airlines.
- This has real consequences for consumers: Heathrow's commercial property estate is in **disrepair or nearing end-of-life**, causing lost income opportunities, risks of existing estate becoming unlettable, and a worse airport experience for airport users.
- We recognise CAA's and airlines' concerns with the need to **protect the single till and charge levels.**
- Therefore, we proposed **trialling** an alternative and optional approach in H8 that builds on the single till, rebalances risk and reward and generate shared revenues.
- Modelling of the sharing agreement shows there is **no increase to charge and airlines are never worse off.**

## The IPs do not consider changes are needed

- *“we are **not** proposing to change the treatment of commercial property investment in these initial proposals”*
- **Right risk / reward balance:** *“We note that while commercial property investment in the wider economy may have higher risk, there appears to be some force in airline arguments that the impact of the single till de-risks these investments for HAL by providing a return on the investment added to the RAB.”*
- **Sufficient headroom for property investments:** *“We set HAL's capex allowance as an envelope, within which it is for HAL and the airlines to prioritise projects to take forward”*
- **Appropriate payback period:** *“We consider that, in general, our price controls (and those applied by other regulators) reasonably accommodate investment in long-lived assets by the use of the RAB, which is a prominent feature of most sectors subject to price controls.”*

# Some areas not covered in the IP remain relevant for further joint consideration

While the IPs engage with the theoretical arguments of our Business Plan, which is helpful, they do not reflect the more detailed proposals and evidence provided thereafter.

- As such, they do not address the more fundamental problem of underinvestment and associated impacts, along with the working proposal we have tabled.
- This also influences the understanding of practical combined effect that risk/reward balance, explicit capital headroom for property and payback period have on investment.

We have outlined and illustrated step-by-step the design principles that ensure that a sharing agreement used *if and when* on-RAB development is rejected offers a win-win approach.

We have modelled the sharing agreement's financial results (and provided underlying calculations) to show that development risks would be taken by Heathrow Propco securing benefits to the till and airlines, with no charge increase.

We have shared new consumer evidence highlighting that passengers want landside improvements, in line with standards offered by European competitor airports.

Heathrow - Restricted

### Background

Heathrow has identified chronic underinvestment in landside property and proposed trialling a new incentive framework in H8 whereby risks are reallocated to unlock property investment while protecting the single till. The CAA remains unconvinced that change is required.

In CE and our H8 BP we suggested incentives need to change

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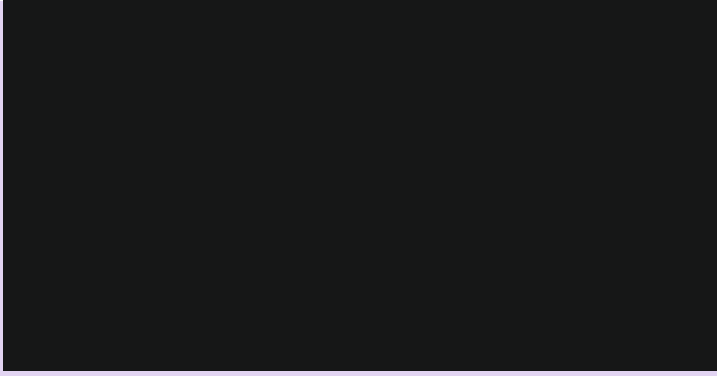
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Classification: Internal

**Conclusion: we have the outline of a "win-win" process**  
There is a way to re-allocate risk to the benefit of all stakeholders

- Right of First Refusal:** process aligned to existing capital governance, no dilution of airline rights to approve or reject capital investments.
- No Worse Off:** "sharing rate" approach gives single till a fair revenue while taking no risk.
- Market-led:** the RICS approved residual land valuation method can determine a sharing rate, and can be undertaken by third party valuer.
- Fair Bet:** license change that embodies principle that sharing rates cannot be reopened or properties returned to RAB post development.
- Trial:** attempt in H7 period for a limited set of properties with view of validating or improving model for H9+ (and expansion).

Passengers	Better spaces More choice
Airline Customers	No increase to charges No more risk Single Till integrity
Shareholders	New investment opportunities
Local Communities	Better spaces More choice
Team Heathrow	Better spaces More choice



Classification: Internal

**Passengers have told us that Heathrow needs investment landside to improve their experience**

We have commissioned new research that heard c. 5,000 passengers and airport users

**Better landside facilities**

Airport users have told us they want better value landside facilities at Heathrow, indicating that there is a clear opportunity to improve

The airport needs improvements to the landside facilities	The airport needs more landside facilities	There are not enough facilities landside to meet basic needs
47%	45%	36%

**Specific improvements**

Heathrow passengers identify specific needs:

- Better Food & Beverage offer with wider set of retail and F&B options
- Better comfort and space with more seating areas

#1	Food outlets open 24 hours a day	12.3%
#2	Shops open 24 hours a day	10.7%
#3	Wide variety of food outlets	10.6%
#4	Convenience store / supermarket	9.5%
#5	More seating	8.6%

**European competitors**

Negative impressions of Heathrow are higher than in relation to European competitors (MUN, AMS, CDG\*)

47%	45%	36%	27%
The airport needs improvements to the landside facilities available	The airport needs more landside facilities	There are not enough facilities landside to meet basic needs	The airport looks old and tired

**Hotel demand**

Passengers, including those who don't currently use airport hotels, are willing to stay in them if a few elements are improved, fixing the perceived key barriers

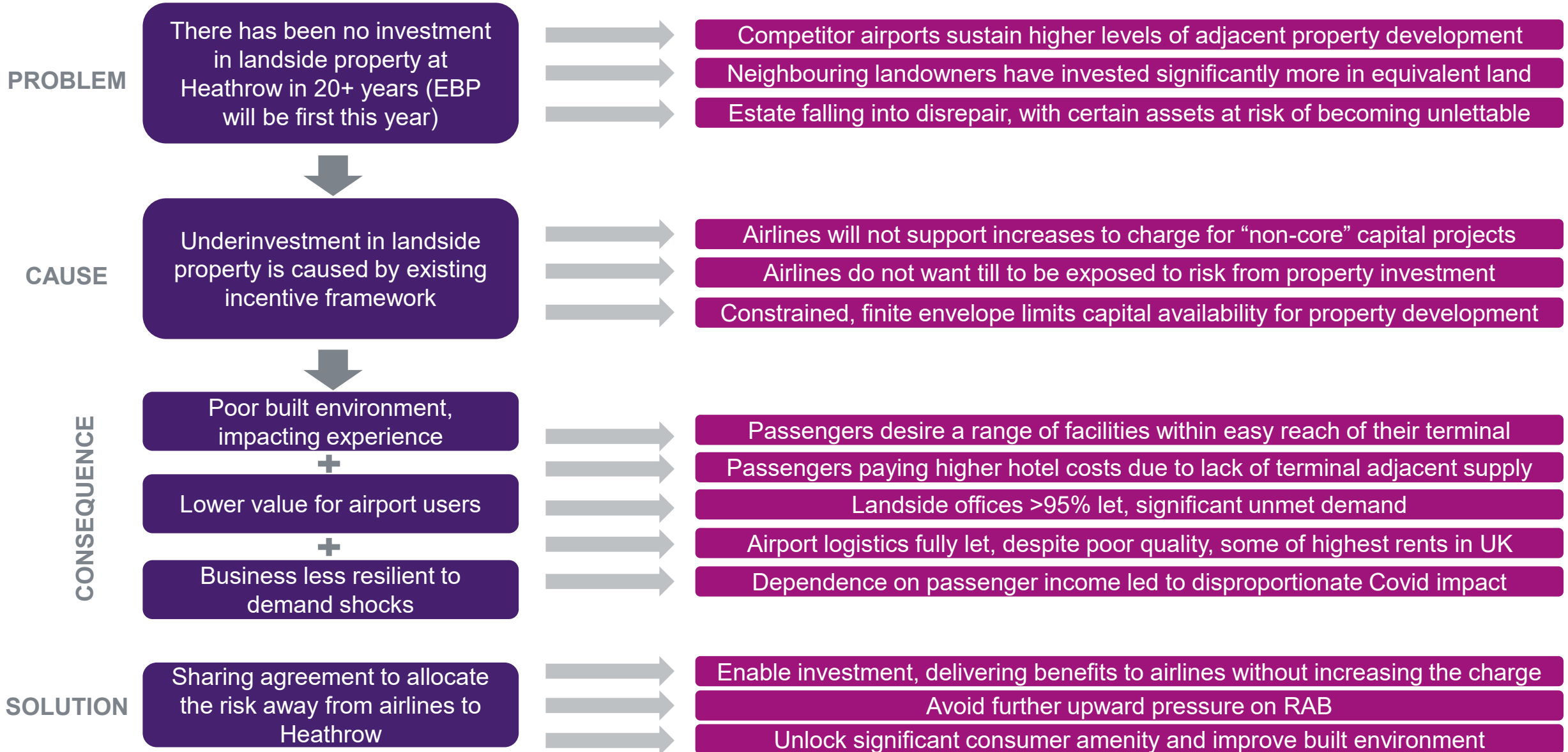
Extra cost/ too expensive	#1	40%
No budget options available	#2	23%
Distance from airport terminal	#3	22%

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# Problem (re)statement



# Vision test: There has been underinvestment in Heathrow's property estate

**Property owned by Heathrow has not developed in line with local supply or equivalent European competitor airports.**

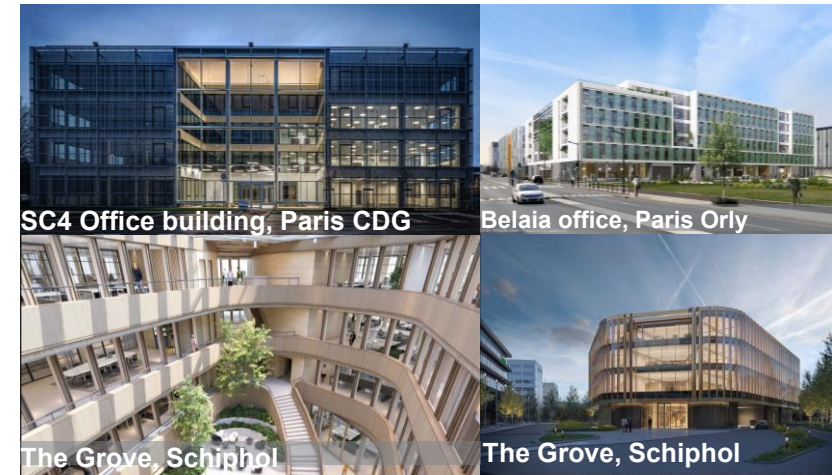
The interests of our airlines and passengers are not served by our commercial property being in a state of disrepair or approaching end of life – especially vs. our competitor hubs who have invested and made the most of both commercial and operational opportunities available.

"Do nothing" is not an option – to stay competitive and realise the full potential of our property portfolio, we must act to modernise our property portfolio, align with the standards set by our competitors and unlock the untapped value. Doing nothing risks assets becoming commercially unlettable, becoming a burden on the single till.

## Heathrow



## Competitor Airports



## Local Landowners



# Airlines have no incentive to support property investment and reject it at programme level at price review

Airlines reject property investments at programme level due to focus on faster payback and zero charge impact from “non-core” programmes. This, combined with the limited explicit allowance for commercial property, and prioritisation towards “core” assets, constrains the ability to even bring forward property investment in practice.

Heathrow proposal	Airlines' position	CAA decision
<p>£600m for Commercial Revenues (including Property projects) – at the Optimal Plan submission.</p> <p>Of this, £200m was for Commercial Property Development (flat phased at £67 each year between 2024-2026).</p>	<p>AOC/LACC response: <i>“Commercial Property Development (HAL H7 Est: £200m): We believe that new property development is not safety, security or resilience. We therefore believe that we should evaluate each business case as required.”</i></p> <p>They suggested £0 for this as part of their Capital Plan proposal.</p>	<p>Of the £157m allowed by the CAA in its Final Decision for Commercial Revenues, Heathrow defined a Wave 1 P1 for this amount, of which Property Development made up £17m of the total split as follows: 2022 - £0.7m; 2023 - £6.9m; 2024 - £5.1m; 2025 - £3.1m; 2026 - £1.1m.</p>
<p>Treat property investments outside capex H8 envelope.</p>	<p>Opposed to any changes to the property investment framework.</p>	<p>In Initial Proposals, CAA not currently supporting framework changes but recognises that, in setting the capex envelope, it prioritises projects related to asset resilience, safety and security.</p>
<p>Trial a new approach through a sharing agreement used <i>if and when</i> on-RAB development is rejected.</p>	<p>The airline ABP has proposed <b>re-including</b> commercial property investment in their proposed £5.5bn H8 capital plan. However, there is no allocation to these investments. They have not been consistently prioritised in capital allocation discussions, nor were they a focus in the airlines' original prioritisation materials provided in early rounds of CE (which removed them given the need to deliver more affordability).</p>	

H7

H8

The example from H7 and current H8 developments illustrate and confirm the property investment challenge

# If nothing changes... property investments are likely to continue being deprioritised, despite presenting attractive development business cases...

Illustrative scenario exposing a clear disparity: a value-creating development that a market-leading property developer would invest in fails to achieve single till hurdles. In a capital-constrained environment these projects will continue to be deprioritised, despite offering longer-term single till benefits that may outperform investments delivering in-period returns. The significant proportion of the capital envelope required to deliver these projects compounds the issue.

Applied assumptions:		Realistic development
WACC (%): 6.50%	Rent (£/sqft)	£26.00
Depreciation (years): 20	Estimated Rental Value (£m)	£13.0
Pax numbers (mppa): 85	Total Cost of Development (£m)	£150
Rent free period: 1yr	<b>Development Appraisal</b>	
Exit yield: 7.00%	Gross Development Value (£m)	£186
<b>Developer hurdles:</b>	Net Development Value (£m)	£173
<b>POC = ~ 15%</b>	Developer Profit (£m)	£23
<b>DY = ~ 8.5%</b>	Profit on Cost (%)	15.1%
	Development Yield (%)	8.7%
	<b>Single Till Appraisal</b>	
<b>Single Till hurdles:</b>	Payback period	12
<b>Payback = 5 years</b>	Year One Charge Impact (£/pax)	+£0.05
<b>Pax charge = Flat/falling</b>	First 5 Year Avg Charge Impact (£/pax)	+£0.04
	20 Year Avg Charge Impact (£/pax)	-£0.01

Goal seeking to meet Single Till hurdles

Unicorn development 1	Unicorn development 2
£26.00	£26.00
£13.0	£13.0
£106	£65
<b>Development Appraisal</b>	
£186	£186
£173	£173
£67	£108
63.5%	165.7%
12.3%	20.0%
<b>Single Till Appraisal</b>	
8	5
-£0.01	-£0.07
-£0.02	-£0.07
-£0.05	-£0.09

Development costs would need to be significantly lower than realistic or achievable to meet one or both hurdles...

... and achieve profit on cost and development yields far exceeding any realistic development scenario

**The implication:** these projects are rarely brought forwards for approval in the first place, despite being strong investments with long-term consumer upside.

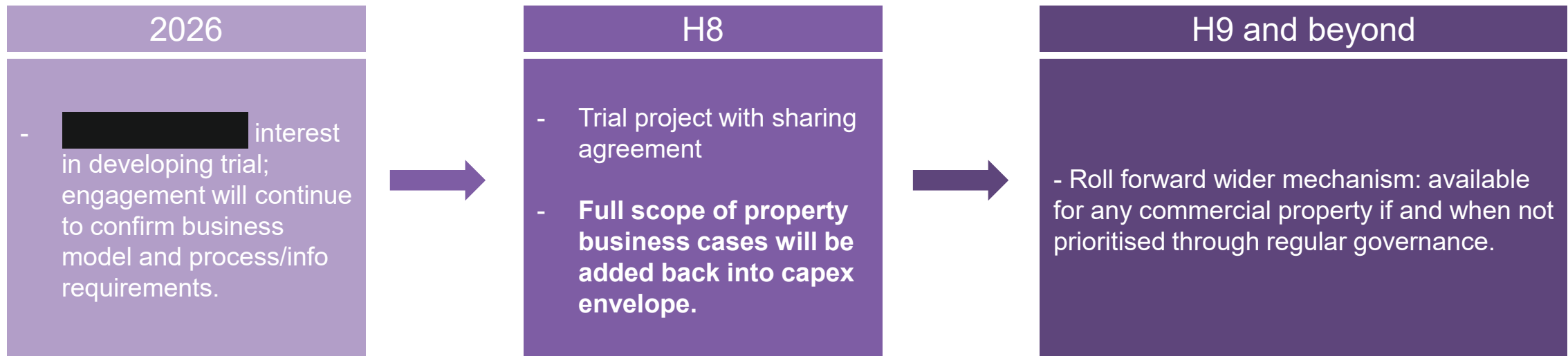
**Meets developer's hurdles** ✓: Developer likely to proceed with investment  
**Does not meet Single Till hurdles** ✗: Unlikely to be brought forwards as unlikely to achieve G3 approval vs. other projects given capital constraints despite development viability and long-term value creation

# ...and the property development portfolio will be brought back into the H8 capex envelope whilst we trial the alternative approach in H8 to roll out in H9



*“we are **not** proposing to change the treatment of commercial property investment in these initial proposals...we remain open to the possibility that there could be circumstances in which an alternative revenue-sharing approach **for specific investments** may provide HAL with an incentive (that may not presently exist) for it to invest in a project that delivers net financial benefits to consumers.”*

- Heathrow remains open and supportive of the option to develop an optional route to deliver commercial property investment.
- However, it is now clear that this will not represent a wider a solution for required investment in commercial property H8.
- CAA support is crucial to enable trial and appropriate consideration for wider roll out in the future.



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# Proposed change: A sharing agreement creating the *option* to reallocate risk if traditional “On RAB” development is not prioritised

These design principles ensure that risk is allocated to the benefit of all stakeholders and deliver a win-win solution

- 1. Right of First Refusal:** Customers (airlines) have right of first refusal on property programmes and projects. On refusal, Heathrow has the *option* to proceed under a different model that reallocates risk entirely to them.
- 2. No Worse Off:** Once rejected, the development should not leave customers any worse off, the RAB should not increase and any future capital risks are borne exclusively by Heathrow.
- 3. Market-led:** The “sharing rate” should be objectively determined by a third party(s) – not an additional burden to regulatory engagement.
- 4. Fair Bet:** The “sharing rate” for properties should not retrospectively be reopened, and nor can properties be retrospectively added to the RAB.
- 5. Trial:** The H8 period is an opportunity to trial this new model in advance of H9+ expansion period.

**Passengers**

Better spaces  
More choice

**Airline Customers**

No increase to charge  
No more risk  
Single Till integrity

**Shareholders**

New investment  
opportunities

**Local Communities**

Better spaces  
More choice

**Team Heathrow**

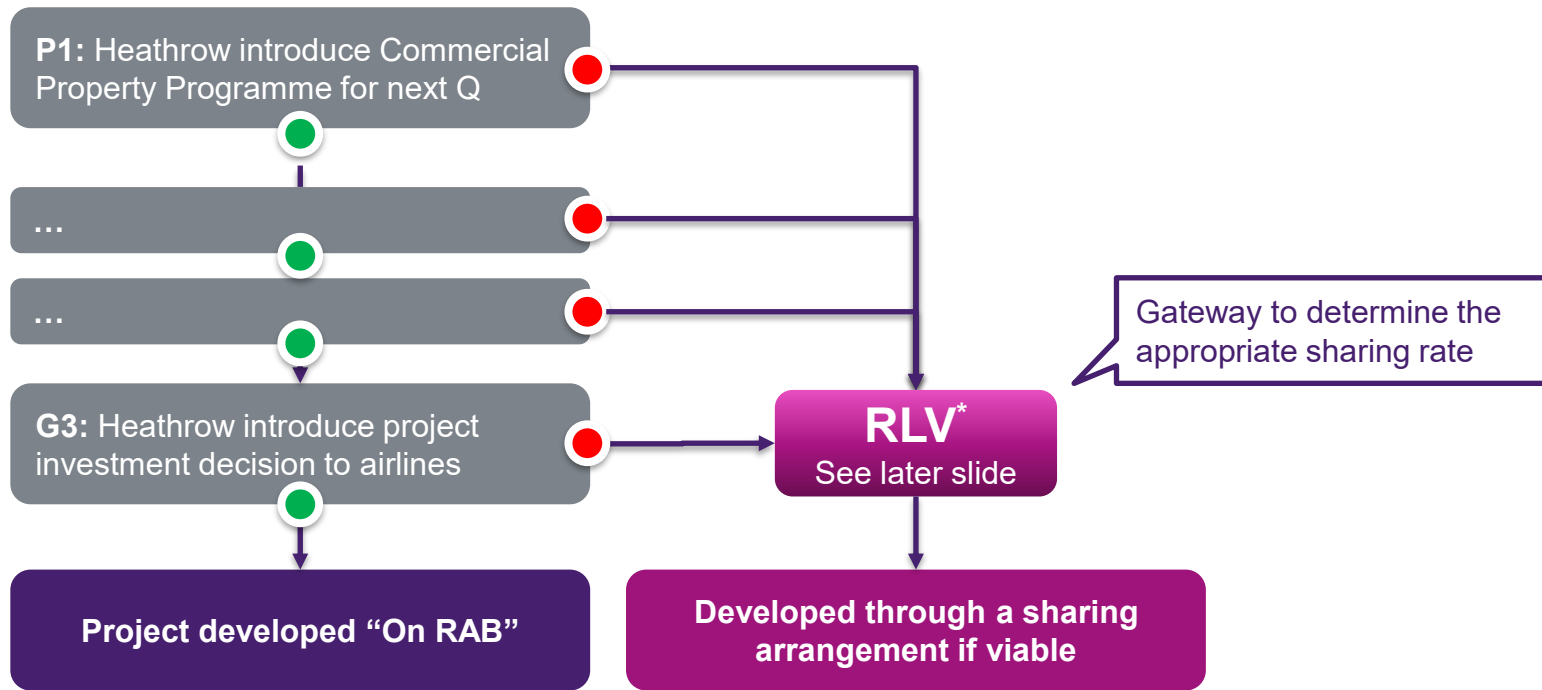
Better spaces  
More choice

# “Right of First Refusal”

Heathrow can use optional process only after initiative has been rejected by airlines

Airlines retain control of what is developed through single till or not.

Different site categories (perimeter, landside, airside) may require specific considerations (see annex)



*All efficiently incurred costs added to RAB, on which Heathrow earn an allowed return. Subject to ex ante and delivery obligations. Revenue forecasts reset every five years.*

*No additional costs added to RAB, all capital risk sits with Heathrow. Revenues split between Heathrow and Single Till at sharing rate.*

\*RLV = Residual Land Valuation

# “No Worse Off”: Eastern Business Park

Approved by the airline community at G3, now being developed “on RAB”

A typical perimeter project where buildings of 1940s were to be mothballed without redevelopment – at a loss of revenue to single till. Redevelopment promised minimal impact to charge, low revenue risk and capital required <1% of H7 total.

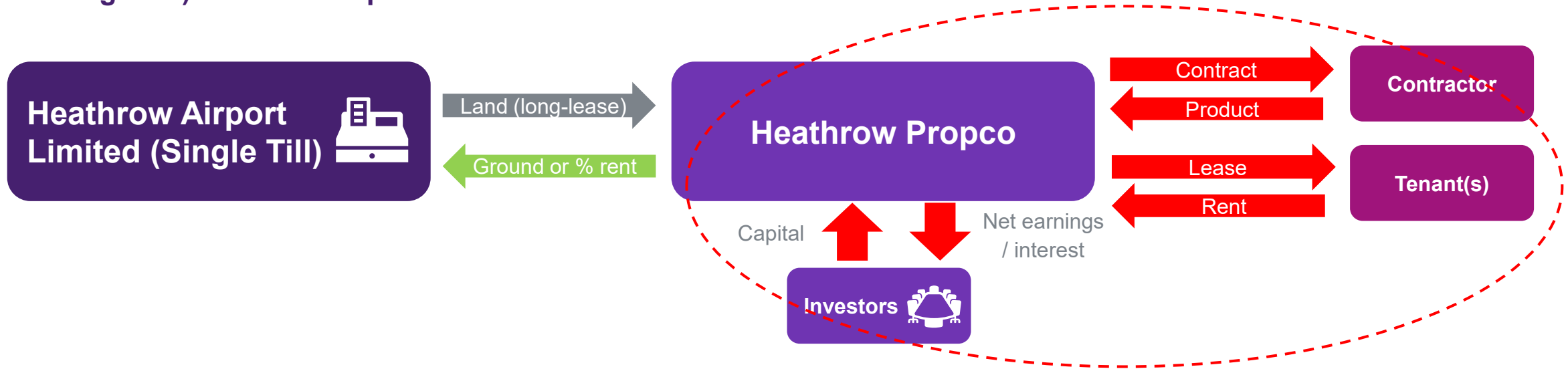


*Model available on request*

**All modelling illustrative only- not verified by Heathrow finance**

# We showed how Heathrow subsidiary or JV would assume costs and risks while making payments to the till

In this model, "Heathrow Propco" takes forward project, takes all capital and revenue risk – pays HAL (and single till) a revenue equivalent to residual value of land.



Model available on request

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## “No Worse Off”: Hypothetical Construction Programme

Same yield as EBP, but at larger scale, over 15 years = more risk to till

A significant capital programme competing against other “core” airport investments, with significant outlay over early periods, keeping charge high until H12/13. Worst case scenarios not attractive investment for the till.



*Model available on request*



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# “No Worse Off”: Hypothetical Construction Programme

## Reallocating risk realigns objectives

Same principle as before, where all risk is taken by Heathrow Propco (who want to take it) and single till receives a revenue equivalent to the residual land value. In all scenarios, the till is better off with development than without it.



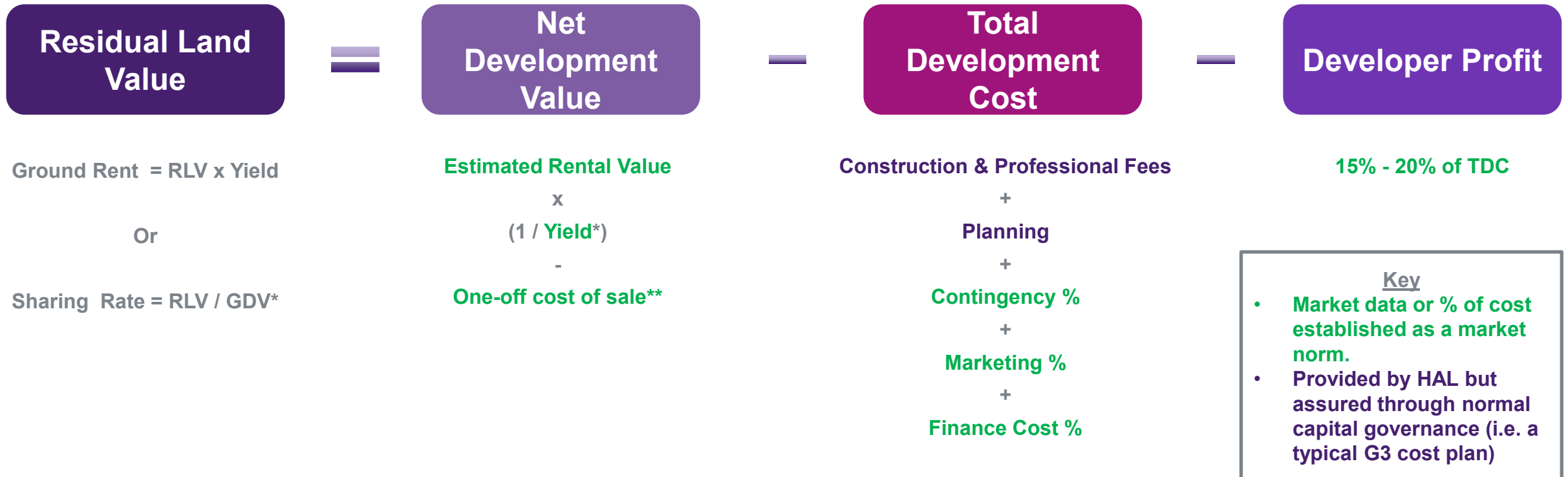
*Model available on request*

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# “Fair Bet”: Residual Land Valuation

## Objective approach to determining sharing rate – for discussion

A simple equation to determine fair land price, and from that, the appropriate sharing rate – recognised by RICS and procured from external valuation agents.



\*\*Yield” is the capitalisation rate of a revenue, i.e. the relationship between rental value and asset value. This varies for type of let and location, but at Heathrow it is typically around 5%.

\*\*typically new tenants are offered 9 months rent free at the start of their tenancy to enable them to undertake fit out works.

\*\*\* GDV is gross development value, which is the same as net development value without accounting for one-off cost of sale.

# “Fair Bet”: Residual Land Valuation

## Example: EBP

A simple equation to determine fair land price, and from that, the appropriate sharing rate – recognised by RICS and procured from external valuation agents.



**ILLUSTRATIVE ONLY – we can commission a third party valuation of EBP land if helpful.**

\*assume G3 cost estimate reflects construction, professional fees, planning and contingency

\*\*marketing assumed to be 1% of GDV, as per industry standard (1% - 3%).

\*\*\*finance assumed to be 6% of all other TDC, as per industry standard.

**Heathrow**

**Annex**



# Third-party model has proven highly suboptimal

## Giving critical land to 3<sup>rd</sup> parties has misaligned incentives, impacting operations

Examples of T2 Garden Hotel, T5 Sofitel, SEGRO Cargo Southside are examples where third parties – responding to different incentives – have diminished value for Heathrow and Airlines

### Terminal Adjacent Hotels



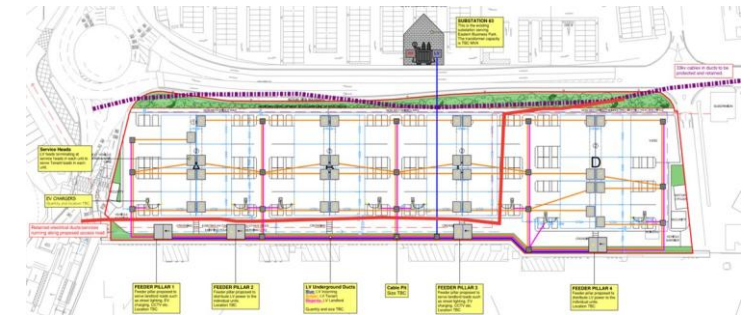
- Surface access policy non-compliance
- Operational incidents (T2 Hilton and runway lights)
- Exploitative pricing of customers (March 2025 power outage)
- Security Risk (BP conference @ T5 Sofitel)

### Airside-Landside Cargo



- Historic underinvestment despite demand for new development from all tenants.
- Diminished cargo capacity = smaller aircraft = higher airport charge
- Security non-compliance risk.
- Health & Safety incidents.
- South of airport loss of water supply due to tenant mismanagement (2022)

### What If? Eastern Business Park



- Delivery risk of HV cable, interrupting power supply to eastern airport (incl. BA maintenance base).
- Security risk (adjacent to airside land / BA maintenance base)
- Fire / smoke risk (immediately below arrivals approach, adjacent to BA maintenance base)

# In combination, existing risk allocation, payback period and capex limits have dampened interest in property investment

While the single-till and RAB provide some cost risk mitigation in principle, the combination of misaligned returns for development risk, constrained and uncertain capex allowances, and short control-period signals on payback materially affects investment behaviour in practice. These factors interact to increase perceived risk and reduce confidence in bringing forward commercial property projects.

	H8 Initial Proposals	Preliminary considerations
<b>Risk and reward</b>	<p><i>“We note that while commercial property investment in the wider economy may have higher risk, there appears to be some force in airline arguments that the impact of the single till de-risks these investments for HAL by providing a return on the investment added to the RAB.”</i></p>	<ul style="list-style-type: none"> <li>• While the single-till provides de-risking, commercial property investment still involves material development, leasing and delivery risk inherent in commercial property.</li> <li>• A commercial redevelopment requiring demolition, remediation and new-build delivery may ultimately be added to the RAB, but Heathrow still bears front-end development risk (planning delay, construction cost escalation, tenant pre-letting risk and ramp-up). If leasing is delayed or rents underperform, returns during the stabilisation period fall materially below allowed levels, discouraging investment despite eventual RAB recovery.</li> </ul>
<b>Capital headroom</b>	<p><i>“We set HAL’s capex allowance as an envelope, within which it is for HAL and the airlines to prioritise projects to take forward”</i></p>	<ul style="list-style-type: none"> <li>• While the capex allowance is framed as an envelope, the limited explicit allowance for commercial property, combined with prioritisation towards “core” assets, and airlines’ focus on faster payback materially constrains the ability to even bring forward property investment in practice.</li> <li>• During H7, Heathrow requested £200m for commercial property development, but only £17m was allowed, with a sifting rule that excluded projects with a payback period longer than 5 years. Airlines have also rejected property investment at programme level. In H8, the airline £5.5bn is unclear about property business case prioritisation (as per slide below). In practice, the within-envelope prioritisation on safety, security and resilience projects, leaves commercially viable property schemes unable to progress despite a positive business case and third-party interest.</li> </ul>
<b>Payback period</b>	<p><i>“We consider that, in general, our price controls (and those applied by other regulators) reasonably accommodate investment in long-lived assets by the use of the RAB, which is a prominent feature of most sectors subject to price controls.”</i></p>	<ul style="list-style-type: none"> <li>• Although the RAB supports long-lived assets in theory, short control-period signals on payback, coupled with allowance uncertainty and incentive design, materially influence investment behaviour. Commercial property developments often require longer development and stabilisation periods than a single control period comfortably accommodates, meaning that—despite RAB principles—investment is discouraged in practice.</li> <li>• The business case for a project that meets airline hurdle rate of zero increase to charge and pays back in 5 years would require a profit on cost of ~100%... unheard of in commercial property. Meanwhile the CAA admittedly prioritises projects that have direct consumer benefits and shorter payback (e.g., H7 as per slide below).</li> </ul>