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By email: [economicregulation@caa.co.uk](mailto:economicregulation@caa.co.uk)

29 May 2026

### **IAG submission to H8 Initial Proposals (CAP3232)**

Dear Rob,

## **1. Introduction and overall position**

International Airlines Group, S.A. ("IAG") welcomes the opportunity to respond to the Civil Aviation Authority's ("CAA") consultation on the H8 price control Initial Proposals for Heathrow Airport Limited ("HAL") for 2027–2031 (CAP3232).

IAG fully supports and endorses the detailed responses submitted by its operating companies Aer Lingus, British Airways, Iberia and Vueling. This response does not seek to restate the analysis and arguments set out in those submissions; rather, it provides a Group-level summary of IAG's key concerns and asks, consistent with the evidence our operating companies have placed before the CAA.

We commend in particular the rigorous independent expert work commissioned by the airline community: the economic analysis by CEPA and academic reports from Professor Robin Mason and Professor Donald Robertson on the weighted average cost of capital ("WACC"), and Skylark's independent assessment of the traffic forecast. Together, these contributions provide a robust and well-evidenced analytical basis for the concerns set out in this response and in our operating companies' individual responses. We strongly encourage the CAA to engage thoroughly and substantively with that body of evidence ahead of its Final Proposals.

Heathrow is an effective monopoly and a critical national infrastructure requiring robust economic regulation. Decisions in H8 will materially shape affordability, the competitiveness of the UK aviation sector and the credibility of the regulatory framework.

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IAG shares its operating companies' concerns that the overall H8 package is materially imbalanced in favour of HAL, insufficiently challenging on costs, provides multiple layers of protection to HAL against risk, and risks embedding charges inconsistent with long-term affordability and consumer interests.

Critically, the H8 price control cannot be assessed in isolation. Heathrow's charges, its role as a hub and the connectivity it provides to UK consumers and businesses are not shaped by H8 alone but by the cumulative weight of concurrent regulatory decisions across multiple workstreams. The CAA has already permitted HAL to recover approximately £320 million (2024 CPI) of early expansion costs for 2025–26, before planning consent has been granted. HAL has indicated its intention to incur a further approximately £6 billion of early expansion-related expenditure during H8, with additional expansion costs expected to run to several billions further. The CAA has itself acknowledged that modernisation and expansion could more than double charges in real terms.

It is therefore all the more vital that H8 charges be set on genuinely efficient costs and that the CAA assesses them in the context of wider cost pressures, including expansion-related costs as well as other pressures such as the transition to SAF and the evolution of Air Passenger Duty.

## 2. Areas of support

IAG supports the following constructive elements in the CAA's Initial Proposals:

- **Capital envelope:** We support the £5.8 billion midpoint and the rigorous methodology used to derive it.
- **Single till:** We strongly support the decision to maintain single till. Any dilution would be contrary to consumer interests.
- **Opex and commercial revenue methodology:** We support the bottom-up approach which represents a clear improvement on previous price controls.
- **HAL's Business Plan:** We agree with the CAA's assessment of HAL's Business Plan as "low quality", reflecting a persistent pattern of inadequate transparency that has constrained meaningful engagement throughout Constructive Engagement.

Notwithstanding these areas of agreement, IAG shares its airlines' view that the proposals require significant adjustment in a number of critical aspects, as set out below.

## 3. IAG's proposals

The adjustments proposed by the airline community produce an **average charge of £24.48 (2024 CPIH) over H8**, compared to the CAA's £28.80, which is a reduction of 15%. When compared against the H7 average of £28.40, it results in a 14% reduction and a 9% reduction against the average charge of £27.00 over 2024–2026, reflecting steady-state post-pandemic traffic. The CAA's own proposal, on the other hand, implies a 7% increase on the same basis, ie. a materially larger increase in real terms than the headline H7/H8 comparison suggests.

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Our proposed reduction is based on a recalibration of the CAA's proposal which currently remains heavily in HAL's favour, one that overstates the efficient cost of capital, sets insufficiently challenging efficiency targets, applies an artificially depressed traffic forecast and fails to provide adequate incentives for service quality. Each of these issues, individually, results in higher charges for consumers. Collectively, they compound into a settlement that risks seriously damaging the affordability and competitiveness of Heathrow for the duration of the H8 period and beyond.

The 15% difference between IAG's proposed charge and the CAA's is largely driven by the cost of capital as well as operating expenditure, commercial revenues, and traffic forecasting. Each are addressed extensively in our operating companies' responses and are briefly summarised below.

#### a. Cost of Capital

IAG's primary concern is the CAA's proposed WACC of 5.87% pre-tax CPIH-real (4.86% vanilla) which is materially overstated given the level of risk faced by HAL, inconsistent with the CAA's own regulatory precedent and its principles of stability and predictability, and conflicts with the CAA's statutory duty under Section 1 of the Civil Aviation Act 2012. It also departs from the approach taken by leading European regulators assessing the same comparator airports.

IAG proposes a **WACC of 4.68% pre-tax CPIH-real (3.74% vanilla)**, in line with CEPA's independent analysis and the academic evidence of Professors Mason and Robertson, approximately 120 basis points below the CAA's proposal.

The financial consequence of the CAA's overstatement is substantial as it would deliver **more than £1.2 billion in additional returns to HAL over H8, equivalent to over £3 per passenger**, with no corresponding benefit to airport quality or capacity.

#### **The asset beta**

The CAA proposes an asset beta of 0.5, whereas independent analysis by CEPA, informed by reports from Professor Mason and Professor Robertson, arrive at a post-adjustment asset beta of 0.42. This suggests that the CAA may be **overestimating the systematic risk faced by HAL by 20%**; adding approximately £1.30 per passenger.

This overstatement arises from a number of factors, in particular because the CAA has:

- Made factual errors in terms of assuming comparator airport groups face similar capacity constraints to HAL;
- Used unstable, inconsistent and inefficient beta estimates with embedded volatility that are not aligned with the regulatory horizon;
- Failed to adjust for the fact that HAL faces lower systematic risk given it is a single, capacity-constrained hub operating under single-till, compared to the comparator airport groups AENA, AdP and Fraport which are dual-till and operate international, riskier, unconstrained airports globally.

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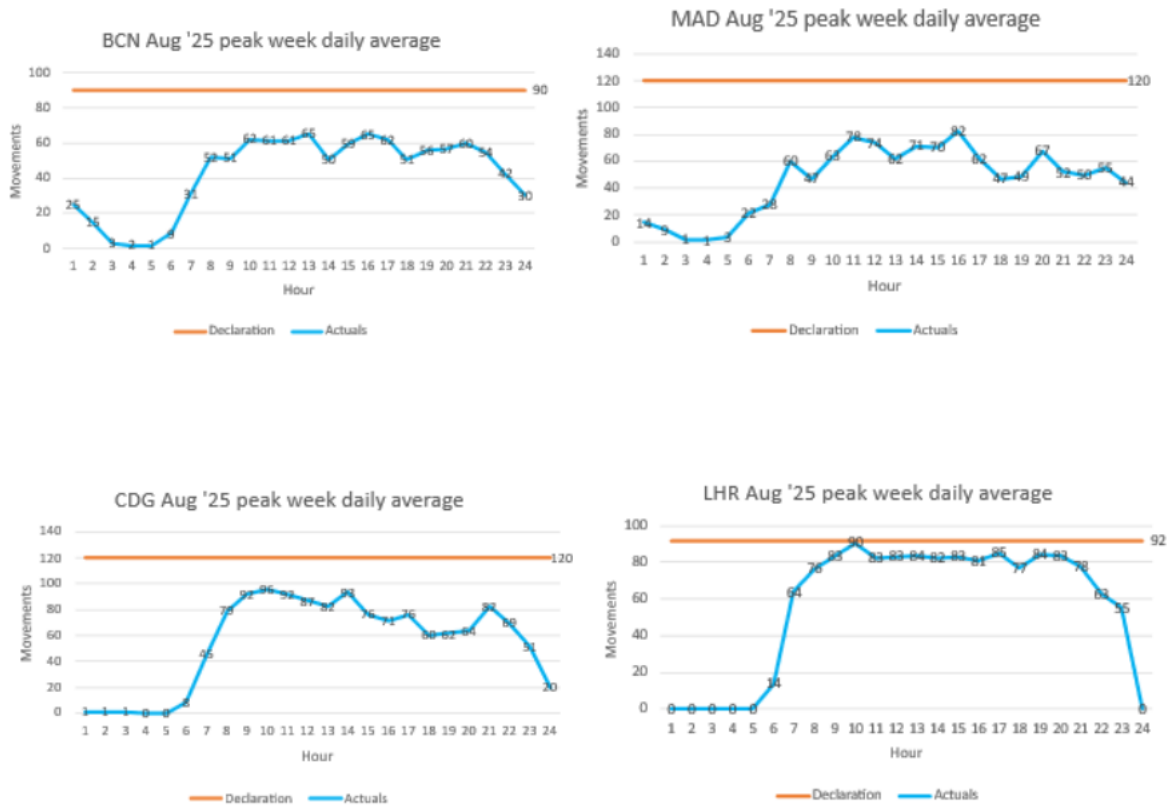
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**Factual errors on the extent that comparator airports are capacity-constrained**

The CAA's decision not to apply a relative risk adjustment is partly grounded in an incorrect finding that the European comparators face capacity constraints similar to Heathrow. IAG's own analysis of OAG schedule data for the August 2025 peak week shows:

- **London Heathrow (LHR):** 90 movements per hour against a declared limit of 92 - consistently close to its limit throughout the operating day.
- **Paris CDG:** 96 movements per hour against a declared limit of 120.
- **Madrid (MAD):** 82 movements per hour against a declared limit of 120.
- **Barcelona (BCN):** 65 movements per hour against a declared limit of 90.

The following charts, based on our own internal analysis of OAG schedule data for the August 2025 peak week, illustrate the contrast between Heathrow and each of the three comparator airports:



Source: IAG analysis, OAG schedule data. Declared capacities: COHOR (CDG), DORA II (MAD/BCN), CAA (LHR).

AENA also operates 46 airports across Spain, the vast majority unconstrained. Comparing HAL to the consolidated AENA group without adjustment introduces systematic upward bias into the beta.

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### **Beta estimates**

The CAA relies on unadjusted 2-year and 10-year OLS regressions. The 10-year window gives disproportionate weight to Covid-period outliers that artificially inflate the beta. CEPA demonstrates that outlier-mitigation reduces the 10-year beta by around 0.07. The CAA's own H7 approach rejected unadjusted OLS betas for exactly this reason but no explanation has been given for reverting to it.

### **Systematic risk faced by HAL versus comparator airports**

The CAA has failed to apply a relative risk adjustment reflecting HAL's structurally lower risk profile. HAL is a single-site, capacity-constrained monopoly operating under a single till, insulated from commercial and demand-side risks by the TRS, has RAB certainty and price control protections. The CAA's own consultants (FTI) acknowledge that HAL's risk profile has lowered since H7 and is largely unchanged from Q6<sup>1</sup>. At Q6, the CAA applied downward beta adjustments for AdP and Fraport; at H7, it quantified a beta uplift for pandemic-era demand reduction. The roll-forward logic for H8, now that capacity constraints are fully restored, should be a downward adjustment.

In April 2026, the French ART gave its initial opinion on AdP's regulatory proposal on airport charges for 2027–2034 in which the comparator airports used by AdP were AdP itself and AENA, Fraport and Zurich (the same 4 comparator airports being used by the CAA in estimating HAL's beta). In its opinion, the ART explicitly identified an upward bias in the comparison of AdP to airport groups with holdings in international airports such as AENA, Fraport and Zurich, given that such activities increase the overall risk profile of these comparator group airports and in turn may exceed that of the regulated activity of AdP. The ART goes on to make recommendations for how to adjust for such risk.<sup>2</sup>

If the ART identifies an upward bias in the comparator set for AdP, which is not a single-site airport and is not as capacity-constrained as Heathrow, the case for drawing the same conclusion for HAL is even stronger. By comparison, the CAA has not offered any analysis explaining why it reaches the opposite conclusion, and does not seem to have used its judgement in a manner similar to the ART. IAG considers this a significant gap that must be addressed in Final Proposals.

### **Cost of debt and internal consistency**

The CAA's decision to change its policy and use HAL's actual cost of senior debt rather than a notional efficient benchmark creates perverse financing incentives. The CAA's own Initial Proposals acknowledge this creates "a limited incentive on HAL to issue senior debt efficiently" yet does not address this risk effectively.

CEPA estimates the **notional cost of debt at 1.85% real CPIH** against the CAA's 3.14%, a difference estimated to add **up to £2 per passenger to charges**, embedding an expectation of debt cost pass-through that is particularly damaging in the context of future expansion.

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<sup>1</sup> FTI Consulting, Cost of Capital Strategy for H8, November 2024, prepared for the CAA.

<sup>2</sup> Autorité de Régulation des Transports (ART), Avis n° 2026-012, avril 2026, relatif au contrat de régulation économique d'Aéroports de Paris pour la période 2027–2034.

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The CAA also retains a 60% notional gearing assumption that is high relative to comparator airports, while simultaneously moving to an actual debt approach. This is an internal inconsistency that transfers the consequences of HAL's specific financing choices onto consumers. IAG supports reverting to a notional benchmark, as recommended by CEPA.

### Data cut-off and financeability

The CAA's headline data cut-off of 1 November 2025 for proposals published 31 March 2026 represents a 21-week gap against Ofwat's 11 weeks<sup>3</sup> and the French ART's 8 weeks<sup>4</sup>, resulting in beta estimates that embed Covid-era outliers which are no longer relevant to H8. IAG requests an updated, consistently applied cut-off for Final Proposals.

On financeability, IAG has not seen any persuasive evidence that Heathrow faces a constraint at a WACC of 4.68%. HAL continues to enjoy strong capital market access and investment-grade credit metrics, and financeability should not be used to override an evidence-based assessment of the allowed return.

### Cumulative imbalance

Considered holistically, the H8 package provides HAL with multiple overlapping layers of protection. Within the WACC, a consistent bias towards the upper end of plausible ranges on beta, TMR, cost of debt and gearing compounds into a materially overstated estimate.

IAG considers that, even within the CAA's own range, the appropriate response to these multiple risk protections is to select a point estimate at the lower end. This is the approach the French ART has signalled for AdP. IAG urges the CAA to adopt the same principle for Heathrow.

### Capital Expenditure

IAG supports the £5.8 billion capital envelope and the CAA's overall methodology. However, this support is **conditional on a fundamentally strengthened governance framework**. HAL's capital programme has been delivered late and over budget across successive regulatory periods, and the CAA's proposed minor refinements are insufficient.

IAG calls for a reformed Capital Investment Committee with genuine airline representation; robust escalation and 'pause' mechanisms; decision-grade information as a prerequisite for unlocking allowances; and continued portfolio reprioritisation. These reforms are necessary for H8 and essential for expansion.

IAG also notes the lack of transparency on depreciation. The CAA's reliance on HAL's Fixed Asset Register, without disclosure to airlines or adequate independent assurance, is not consistent with proper regulatory scrutiny. For the purposes of our price cap of £24.48, British Airways has adopted a pragmatic mid-point asset life of 19 years which sits between HAL's proposed 18-year lives and a 20-year average

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<sup>3</sup> Ofwat, PR24 Final Determinations.

<sup>4</sup> Avis n° 2026-012.

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from HAL's statutory accounts. IAG endorses this approach and calls on the CAA to require disclosure of the Fixed Asset Register ahead of Final Proposals.

### Operating Expenditure

IAG supports the CAA's base-step-trend approach, including its bottom-up analysis supported by top-down benchmarking, and the rigorous application of need, additionality and efficiency tests in the rejection of most of HAL's proposed overlays. The efficiency targets set by the CAA are, however, insufficiently stretching. HAL's persistent information deficiencies that are acknowledged by the CAA in its "low quality" assessment of HAL's Business Plan, have constrained scrutiny and produced allowances that are cautious by construction.

IAG proposes **£309 million additional challenge on opex (proposed allowance: £7,480 million vs CAA's £7,790 million, 2024 CPIH)**.

### Commercial Revenues

IAG similarly supports the CAA's base-step-trend approach for assessing commercial revenues, however, a similar lack of transparency has constrained effective scrutiny and resulted in a conservative baseline.

There is strong evidence that Heathrow has been underperforming versus its peers; a gap the CAA fails to capture in its assumptions.

IAG proposes a **£412 million additional challenge on commercial revenues (proposed allowance: £5,905 million vs CAA's £5,493 million, 2024 CPIH)**, reflecting Heathrow's structural commercial advantage as a global capacity-constrained hub.

### Traffic forecast

IAG supports the use of an independent forecast by the CAA but is concerned the CAA's approach continues a pattern of systematic under-forecasting that has characterised previous price controls.

IAG proposes a **forecast of 447.6 million passengers over H8** (versus the CAA's shocked baseline of 438 million; Steer's unshocked baseline is 442 million), based on the independent analysis conducted by Skylark.

The shock factor is both unnecessary and duplicative. By applying a downward adjustment to the baseline forecast, it requires passengers to pre-fund the cost of "unforecasted events" that may never materialise. If such events do occur, they should be managed through the TRS mechanism, which exists precisely for that purpose. The CAA's own rationale for the shock factor is to improve forecast accuracy, yet since its introduction there is no evidence that this objective has been met.

The shock factor should be removed entirely. If retained, it must at minimum be recalibrated to remove the systematic downward bias and to eliminate the overlap with the TRS.

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### **Other Regulated charges (“ORCs”)**

IAG is concerned that the ORC framework has materially deteriorated over successive regulatory periods and now operates, in practice, as a cost pass-through mechanism with inadequate efficiency incentives and limited airline visibility over cost drivers. The collaborative governance model originally envisaged is no longer being realised.

IAG proposes an **ORC allowance of £614 million** against the CAA’s £1,289 million (2024 CPIH).

The principal driver of this difference is the reclassification of baggage/HBS out of ORCs and into aeronautical charges where they properly belong and where they would be subject to appropriate regulatory incentives and transparency. IAG also has no objections to HAL’s proposals to move taxi feeder park revenues to Commercial Revenues.

IAG considers that without this structural reform, the ORC framework will continue to undermine cost discipline and fail to protect consumers from inefficient cost recovery.

### **Service Quality incentives**

The MTI calibration remains insufficient to address persistent underperformance.

While IAG welcomes the introduction of a baggage rebate, the proposed 98% target would not capture the consumer harm of major recurring system outages.

IAG endorses the airline community’s proposals for tighter targets on departing baggage, security, T5 track transit and PCA.

Service quality bonuses should be removed as they reward HAL for delivering what should be the baseline expectation of a monopoly infrastructure provider.

### **Business Plan incentive (“BPI”)**

IAG strongly agrees with the CAA’s assessment of HAL’s Business Plan as “low quality”. This, in our view, justifies a penalty under the BPI and precludes any basis for a bonus.

HAL’s persistent failure to provide transparent, high-quality information has constrained regulatory scrutiny, potentially produced allowances that would otherwise have been set more challenging, and undermined the effectiveness of Constructive Engagement.

Strong safeguards are also required against the introduction of substantive new information outside the structured Constructive Engagement process.

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## 4. Expansion and the regulatory framework

As outlined in separate responses to the CAA, IAG supports Heathrow expansion in principle, but not at any cost. Expansion must be affordable for consumers and must not proceed on the basis of a regulatory framework that already embeds excessive charges.

The CAA must ensure that the principles embedded in H8 on the cost of capital, capital governance and affordability do not set harmful precedents for the expansion project. Early expansion costs already flowing through charges must be assessed cumulatively with the H8 baseline in terms of the affordability criterion and the impact of charges on connectivity and competitiveness of Heathrow as a hub.

## 5. Conclusion

IAG's overarching concern is that the H8 Initial Proposals, as currently constructed, risk failing consumers.

The adjustments set out in this response and in our operating companies' detailed submissions produce a proposed average charge of £24.48 (2024 CPIH) over H8, compared to the CAA's proposal of £28.80 which is a reduction of 15% and a 9% decrease against the 2024–2026 average of £27.00.

In this context, IAG calls on the CAA to:

- Adopt a WACC of 4.68% pre-tax CPIH-real, removing at least £1.2 billion of unjustified returns;
- Apply tighter targets on opex (£309m additional challenge) and commercial revenues (£412m additional challenge);
- Reform the ORC framework and reclassify the baggage/HBS charge from ORCs to aeronautical charges;
- Retain the £5.8 billion capital envelope subject to fundamentally strengthened governance, and require disclosure of the Fixed Asset Register;
- Adopt a traffic forecast of 447.6 million passengers and remove or recalibrate the shock factor;
- Apply a Business Plan Incentive penalty and maintain robust safeguards against late submissions;
- Tighten MTI targets, remove service quality bonuses; and
- Assess H8 affordability holistically, together with other cost pressures.

IAG and its operating companies remain committed to constructive engagement as the process moves towards Final Proposals and welcome further dialogue on any of the matters raised in this response.

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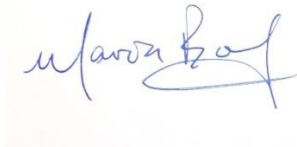
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Yours sincerely,

A handwritten signature in blue ink, appearing to read 'Maria Borg', is placed over a light blue rectangular background.

**Maria Borg**  
Group Head Airport Regulation  
International Airlines Group, S.A.

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