



HEATHROW (SP) LIMITED AND HEATHROW FINANCE PLC

INVESTOR REPORT DECEMBER 2022

16 December 2022

Heathrow¹

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Defined terms used in this document (other than in Appendix 6) have the same meanings as set out in the Master Definitions Agreement unless otherwise stated. Defined terms in Appendix 6 have the same meanings as set out either in the Master Definitions Agreement or in Heathrow Finance's facilities agreements and bond terms and conditions.

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“The UK aviation sector was hit hardest of any major market by border controls and lack of government support, and it is a testament to the forward planning and the hard work of colleagues in keeping Britain’s hub airport running, growing faster and serving more passengers than any other airport in Europe. This year we have welcomed around 61 million passengers, about 25% fewer passengers than before the pandemic. There are strong headwinds facing the economy, and UK aviation will probably not have recovered full capacity until the end of 2023. Our priorities remain working closely with our airline partners to provide excellent passenger experience and to safely get back to full capacity as quickly as possible.”

“We continue to believe in the strong plan we have put forward for investing in passenger services over the coming years, but the ongoing regulatory uncertainty is holding back investment and adding costs to any financing, weakening our ability to deliver the hub airport the UK needs and that passengers want. We encourage the CAA to deliver a final settlement based on the regulatory building blocks that balances risk and return and efficiently incentivises investments in passenger journeys.”

John Holland-Kaye | Heathrow CEO

Heathrow

1. OVERVIEW

This report sets out the forecast financial performance and ratios for Heathrow (SP) in 2022 and 2023, together with key business updates. Additional information specific to Heathrow Finance is set out in Appendix 6.

2022 finally saw the end of all UK travel restrictions and, as the aviation sector has recovered from the impact of the pandemic, we have seen a strong recovery in traffic at Heathrow through the year. 55.7 million passengers travelled through the airport in the first eleven months of 2022. As a result of the ramp-up plan we initiated in Q4 last year, we had all operations open before the Summer peak. The temporary departing passenger cap which we put in place in July successfully improved passenger journeys and was removed at the end of October without compromising service. Building back to full capacity remains our top priority. Team Heathrow has already recruited 16,000 people since last November and we continue to work alongside airlines and their ground handlers to boost recruitment next year. The work we have undertaken since summer means that we head into the winter peak without any restrictions on passenger numbers. Despite potential strike action by Border Force this month, our aim is to protect full operating schedules and the vast majority of passengers will be unaffected.

For 2022, we anticipate traffic to be 61.4 million – at the upper end of the 60 – 62 million guidance we published with our Q3 results and 7 million higher than the forecast in our June Investor Report. This is just over 75% of 2019 levels. Given the strong traffic outturn, adjusted EBITDA is forecast to be £1,678 million, an increase of £308 million versus the June forecast. This reflects higher revenue as demand has recovered, with operating costs flat versus the June forecast. Our liquidity position remains strong, and we expect to finish the year with £4.3 billion of cash and committed facilities available, sufficient to meet all obligations until 2025 under our base case.

We have also set out our financial forecast for 2023. This is based on 67.2 million passengers, representing further recovery to 83% of 2019 levels. Adjusted EBITDA is forecast to increase by 4% to £1,747 million. In respect of aeronautical revenue, we have prepared our financial forecast using a charge of £31.57, in line with the 2023 interim price cap proposal published by the CAA on 8th December. Our RAB is forecast to be £22.1 billion at the end of 2022 and £22.8 billion at the end of 2023 as we progress our investment plans. This assumes we receive a full RAB adjustment of £2.5 billion (2018p) as set out in our responses to the CAA's H7 proposals. We have also shown year end ratios, assuming no further RAB adjustment, in the footnotes to slides 18, 20 and 23.

On 28th June 2022, the CAA published its Final Proposals for the H7 period. This proposed an average charge of £24.14 (2020 CPI) across the period. Our analysis shows that the CAA's proposals, as currently set out, are not deliverable or financeable due to errors in the CAA's forecasts of key regulatory building blocks. If these errors are not rectified, it will restrict investment in the UK's hub airport when the country's economic recovery needs it most. We responded to the CAA's Final Proposals on 9th August 2022, detailing why implementation of its Final Proposals would result in an airport that falls far short of what our passengers expect. We are clear on the key outcomes consumers expect in H7 – in advance of its final decision the CAA must reconsider its forecast of the key regulatory building blocks to ensure the price control is a deliverable and investable proposition which can deliver on these outcomes. The H7 decision is already over 12 months late against the original plan and we lack clarity on the final timeline; we currently expect the CAA to issue the final determination for the H7 review together with the associated licence modifications early in the new year.

2022 and 2023 financial performance

(£m unless stated)	2022 (F)	2023 (F)	Trigger / Forecasting Event
Passengers (m)	61.4	67.2	
Summary financials			
Revenue	2,895	3,187	
Adjusted EBITDA ⁽¹⁾	1,678	1,747	
Cashflow from operations ⁽²⁾	1,685	1,737	
Regulatory Asset Base (RAB)	22,082	22,829	
Nominal net debt			
Senior net debt	12,485	12,680	
Junior net debt	2,137	2,349	
Consolidated net debt	14,622	15,029	
Interest paid			
Senior interest paid	102	492	
Junior interest paid	70	78	
Total interest paid⁽⁴⁾	172	570	
Ratios⁽³⁾			
Senior(Class A) RAR	56.5%	55.5%	72.5% / 72.5%
Junior (Class B) RAR	66.2%	65.8%	85.0% / 85.0%
Senior(Class A) ICR	12.16x	2.60x	1.40x / 1.60x
Junior (Class B) ICR	7.21x	2.25x	1.20x / 1.40x
(£m unless stated)	2022 (F)	2023 (F)	Covenant
Heathrow Finance			
Borrower net debt	1,239	1,390	
Group net debt	15,861	16,418	
Borrower interest paid	118	95	
Group interest paid	290	665	
Group RAR ⁽³⁾	71.8%	71.9%	92.5%
Group ICR ⁽³⁾	4.29x	1.93x	1.00x

- 1) Pre-exceptional earnings before interest, tax, depreciation and amortisation
- 2) Adds back cash one-off items, non-recurring extraordinary items & exceptional items
- 3) Ratios calculated using unrounded data. Ratio definitions and calculations in Appendices 2, 3 and 6
- 4) Total Interest Paid increases significantly in 2023 due to the end of the swap reprofiling benefit realised in 2021 and 2022

2. BUSINESS DEVELOPMENTS

TRAFFIC

Passenger numbers have continued to improve, with November seeing just over 5.5 million passengers or 89% of 2019 levels. Over the first eleven months of 2022, a total of 55.7 million passengers travelled through the airport (2021: 16.3 million). We also recorded the busiest summer out of any European hub airport. Although demand continues to be driven by outbound leisure, inbound leisure and business travel are showing signs of recovery. The increase in passenger numbers this year is higher than at any other airport in Europe. Passenger growth was seen in all regions, with Latin America, North America and Europe, in particular, driving the increase in passenger numbers compared to 2021. North America has now recovered to over 80% of 2019 traffic with Latin America growing by 23% compared to 2019 levels. Our cargo tonnage decreased by 2.3% compared to the eleven months of 2021. This was due to airlines shifting focus towards passenger flights, where the majority of cargo is carried in the belly hold of planes. Load factors also significantly increased compared to 2021, in line with the overall increase in demand. During the third quarter, business travel reached 21.5% of overall traffic, compared to 28% in the same period pre-pandemic.

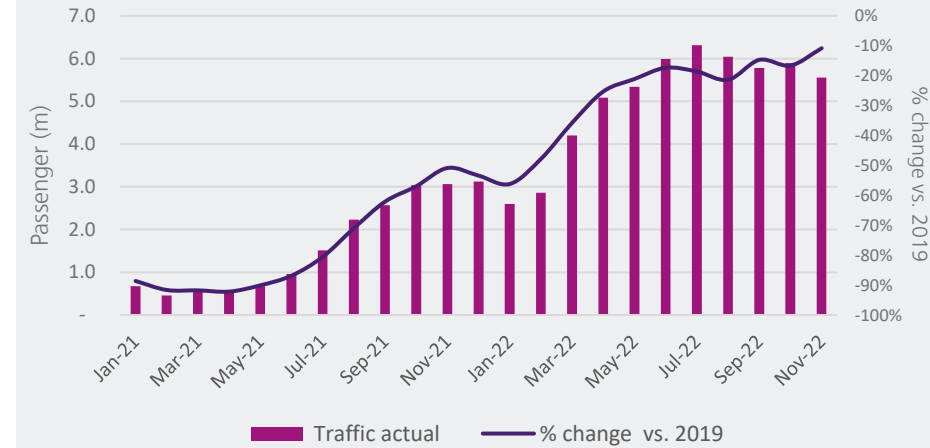
BUILD BACK CAPACITY

In the summer, the entire airport ecosystem was stretched due to scaling up so quickly and this led to periods when standards dropped to levels which were not acceptable. As a result, we decided to introduce a departing passenger cap in order to keep supply and demand in balance. The temporary capacity limit successfully improved passenger journeys with fewer last-minute cancellations, better punctuality, and shorter queue times.

We plan to progressively increase capacity for Winter 2022 with a view to being back to full capacity by the end of 2023. To achieve this goal, we have established a 'Build Back Capacity' programme covering all aspects of the airport ecosystem. The programme aims to build back capacity, resilience and service levels and includes capacity and demand alignment to ensure the operation is not over-stretched during this critical period, a recruitment taskforce to reduce Heathrow's vacancy gap and airline ground handling medium-term resilience and efficiency enhancements.

We announced in November that we will not require a capacity cap for the Christmas peak. This is due to our work with our airline partners to develop a more targeted mechanism that protects existing airline schedules and will manage capacity during peak days around the winter holidays.

Monthly passenger traffic



Traffic and operating statistics

	Jan - Nov 2019	Jan - Nov 2021	Jan - Nov 2022	2022 vs. 2019 (%)
Passengers (m)	74.3	16.3	55.7	(33.4)
Long-haul traffic growth/(decline) %	2.2	(31.6)	318.8	N/A
Short-haul traffic growth/(decline) %	(0.6)	(13.7)	184.6	N/A
Passengers ATM	435,090	137,681	333,302	(23.4)
Cargo ATM	2,773	27,741	9,226	237.6
Load factors (%)	79.9	54.8	76.7	(4.0)
Seats per ATM	213.4	215.9	217.6	2.6
Cargo tonnage ('000)	1,464	1,271	1,242	(15.2)

Note:

Air Transport Movement 'ATM' – means a flight carried out for commercial purposes and includes scheduled flights operating according to a published timetable, charter flights, cargo flights but it does not include empty positioning flights, and private non-commercial flights



2. BUSINESS DEVELOPMENTS

SERVICE STANDARDS

We achieved an ASQ rating of 3.86 out of 5.00 (2021: 4.22) in the third quarter of 2022, reflecting operational pressure in early Summer. Our European competitor airports also recorded decreases in levels of passenger satisfaction. 69% of passengers surveyed rated their Heathrow experience 'Excellent' or 'Very good' (2021: 83%). The main reason for the decrease was that more passengers rated their Heathrow experience as 'Very Good', 'Good' or 'Fair' compared to the 'Excellent' rating we were seeing in 2021. Some challenges in our operational metrics, in particular on departure punctuality, still reflects that the efficiency of aircraft turnaround is not yet back to where it was pre-pandemic. Even with the decline in Overall Satisfaction, perceptions with the Courtesy and Helpfulness of airport staff continued to perform strongly and ahead of 2019 levels (Q3 2022: 4.35). In the 12 months to 30 November 2022, rebates of £28,584,724 were paid by Heathrow under the SQR scheme in relation to terminals security, transfer search and control post security search, mainly in the second quarter. However, in relation to the same period, a £4,446,359 bonus is also expected for exceeding performance targets.

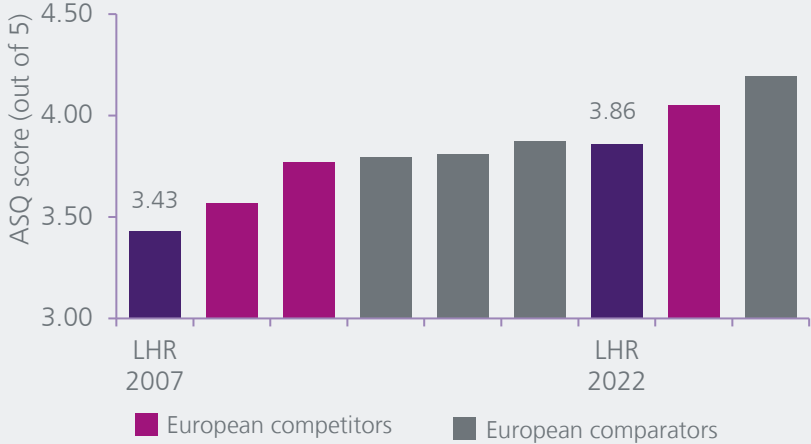
CAPITAL INVESTMENT

2022 marked the start of our next regulatory period, with six core programmes running throughout H7. Across the H7 period, our capital plan is based on £4.1 billion (2018p) of investment. For 2023 our capital investment forecast is £588m, which is 26% higher than in 2022. Our 2023 capital forecast is a continuation of 2022, working towards our H7 programme delivery objectives. Significant investments include our Security Programme, where we will finalise the design works and begin delivery, Asset Management and Compliance which will focus on the continuation of the cargo and main tunnel refurbishment, runway resurfacing and begin delivery of our virtual control facility. Across the other H7 programmes we will see a focus on our cargo and digital proposition, continue to develop airspace modernization and T1 baggage asset replacement will begin.

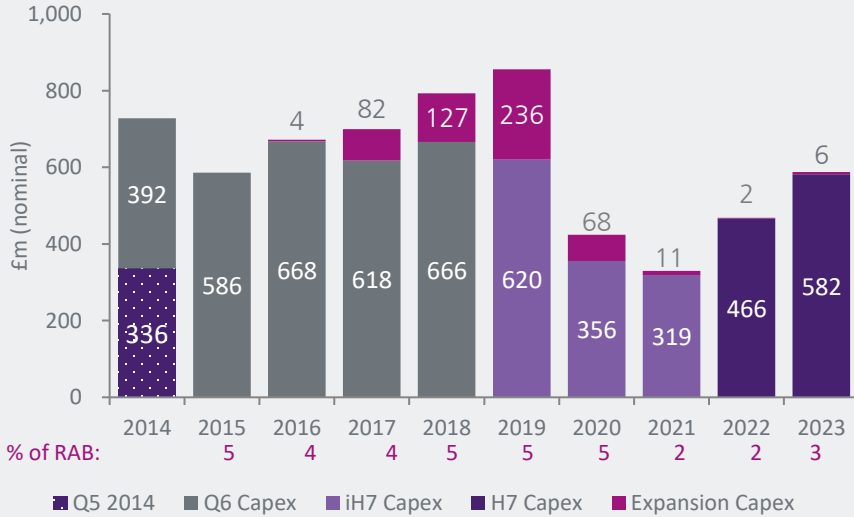
EXPANSION DEVELOPMENTS

While we have paused work to expand Heathrow during COVID-19, recovery from the pandemic has shown the pent-up demand from airlines to fly from Heathrow, as well as how critical Heathrow is for the UK's trade routes. We are currently conducting an internal review of the work and will announce our intended next steps in due course. The Government's ANPS continues to provide policy support for our plans for a third runway and the related infrastructure required to support an expanded airport.

Q3 2022 Passenger satisfaction European ranking



Forecast capital expenditure profile



2. BUSINESS DEVELOPMENTS

Our refreshed sustainability strategy sets out the goals we will work towards this decade. It focuses on delivering outcomes that align with the most material environmental, community and colleague issues for the airport.

Heathrow's Surface Access Strategy was published in August. It sets out plans to increase passenger public transport mode share, reduce colleague single-occupancy-car mode share, reduce carbon emissions and improve air quality, and increase public transport catchment to support the delivery of the goals and targets set out in both key pillars of Heathrow 2.0.

NET ZERO AVIATION

Our net zero plan sets out how we will get to net zero carbon emissions for our own operations, and our contribution to decarbonising wider UK aviation. It includes stretching goals to cut carbon "in the air" by up to 15% and "on the ground" by at least 45% against 2019 levels by 2030. Its eight goals show where we will cut our emissions and how we plan to do that, including how we will work in partnership and influence others where we do not directly control emissions. Investment is key to delivering our net zero plan. As part of our "H7" business plan we put forward £207 million of capital expenditure in a carbon programme, covering everything from modernising airspace to electric vehicle charging. Our regulator, the CAA, backed notionally the full programme in its final proposals, although the overall plan is not financeable and our proposals risk being not deliverable. A historic global aviation net zero deal was reached at the ICAO General Assembly on 7th October. This agreement on a net zero 2050 goal marks a pivotal moment in the sector. Committed advocacy work by our CEO and leadership team has played an important role, including our CEO's Chairship of the Sustainable Markets Initiative (SMI) Aviation Taskforce on behalf of HM The King. Alongside WEF's Clean Skies for Tomorrow and other industry partners, SMI activity, such as engaging States at the Commonwealth Heads of Government Meeting in Kigali in June, helped to make it possible. Following the publication of its Jet Zero Strategy in July, we continue to support the Government on its plans to introduce the mandates and consult on the price incentives needed to stimulate domestic investment in Sustainable Aviation Fuel (SAF). We look forward to the Jet Zero Strategy aim to have five new SAF facilities in development in the UK by 2025 and working with the Government on SAF's wider commercialisation and scale-up, alongside investment in new technology, including zero-carbon emission aircraft, delivery of critical airspace modernisation and supporting carbon removal technologies. Heathrow continues to play its part in accelerating the use of SAF at the airport. Our SAF landing charges incentive – designed to deliver 0.5% SAF at Heathrow during 2022 – was over-subscribed. We are planning to increase the level to 1.5% in 2023 and further increase it steadily in the coming years, complementing the Government's new Jet Zero policy.

A GREAT PLACE TO LIVE AND WORK

We are committed to Heathrow being a great place to live and work and taking action to deliver positive changes this decade. We have continued to roll out the Sustainable Travel Zone, launched earlier this year. Highlights since June were the introduction of free travel between Hatton Cross and Heathrow terminals on the Piccadilly line and improved timetables on several bus and coach routes to the north, west and south of the airport. In July, it was confirmed that Heathrow has successfully retained the Wildlife Trust's Biodiversity Benchmark Award for the 14th year running, recognising our continued commitment to biodiversity and nature and we also celebrated passing a milestone as 4,000 species have now been identified on Heathrow's biodiversity sites. To date in 2022, the Heathrow Employment and Skills Academy has supported 409 candidates through job offers. In addition, 1,142 Security Officers have been directly recruited, supporting the target of 10,000 early career opportunities by 2030. 2,676 experiences of workdays have been delivered so far this year through the Virtual Work Experience programme, T-Level placements, and Essential Skills Masterclasses for young people with additional learning needs. This supports the target within Heathrow 2.0 of 15,000 by 2030. In September, we marked National Inclusion Week by hosting an event to bring together colleagues from across Heathrow to explore how we can work collectively to continue to make progress. In November, Heathrow organized the first Heathrow Business Summit since 2019. In response to feedback from local SMEs, chambers and business organisations, extensive preparation is being done with tier 1 suppliers to maximise the opportunity of bringing potential suppliers and Team Heathrow companies together.

Heathrow 2.0

Connecting People and Planet.



3. REGULATORY DEVELOPMENTS

The CAA published its Final Proposals for the next five-year regulatory period to start in 2022, known as H7, on 28th June 2022. This proposed an average charge of £24.14 (2020 CPI) across the H7 period. Our analysis shows that the CAA’s proposals, as currently set out, are not deliverable or financeable due to errors in the CAA’s forecasts of key regulatory building blocks. It is also the case that changing economic conditions since the Final Proposals render many of the assumptions in the CAA’s Final Proposals out of date.

We responded to the CAA’s Final Proposals on 9th August 2022, detailing why implementation of its Final Proposals for H7 would result in an airport that falls far short of what our passengers expect. Our response requested that the CAA correct the basic errors across the building blocks of its Final Proposals. These include errors in its passenger traffic, commercial revenue and operating costs forecasts, which are undeliverable. We also included further evidence of the need for our £4.6 billion (2020 CPI) capital investment plan, which has been built based on extensive consumer insight to deliver for consumers in H7. Finally, we reiterated key points made in our previous submissions – in particular calling for the CAA to recognise: the inherent uncertainty currently faced by Heathrow when calibrating its price control; the need to set an appropriate Weighted Average Cost of Capital (WACC) for the period, which reflects the risk to which Heathrow is exposed; and the need for an appropriate Regulatory Asset Base (RAB) adjustment following the impact of COVID-19.

The CAA will continue its H7 process into 2023. The decision is already over 12 months late against the original plan and we lack clarity on the final timeline; we currently expect the CAA to issue the final determination for the H7 review together with the associated licence modifications early in the new year. To ensure that the CAA has the most up to date information on which to base its decision, we will continue to engage and highlight, in particular, the changing economic conditions on our forecasts for the H7 period. Our revised traffic forecast for H7 is set out on page 11.

CAA’s Final Proposals (June 2022)

H7 Charge £24.14 (2020p)	Capex Plan £3.6bn (2020p)	WACC 4.2%	RAB Adjustment £0.3bn (2020p)
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H7 Timetable



4. HISTORICAL FINANCIAL PERFORMANCE

This section summarises the results for the Group for the nine months to 30 September 2022. A full description of performance is provided in the results published on 26 October 2022, available at the Investor Centre on [heathrow.com](https://www.heathrow.com).

TRAFFIC

In the first nine months of 2022, traffic increased by 335.0% to 44.2 million passengers (2021: 10.2 million) reflecting the recovery in traffic since travel restrictions were lifted. Heathrow recorded the busiest summer out of any European hub airport.

ADJUSTED EBITDA

In the first nine months of 2022, Adjusted EBITDA increased 970.1% to £1,252 million (2021: £117 million).

REVENUE

In the first nine months of 2022, total revenue increased 203.0% to £2,106 million (2021: £695 million). This was driven by an increase of 315.7% in aeronautical income, an increase of 238.5% in retail income and an increase of 37.9% in other income. Aeronautical income increased predominantly due to higher passenger numbers and an increase in aero charges set by the CAA's H7 interim tariff for 2022. Retail income increased due to higher departing passengers, car parking revenue, premium services and the mix of retail services available in the nine months of 2022, compared to 2021 when the governmental restrictions on non-essential shops were in place in the first five months. Other revenue increased by 37.9% due to higher ORC revenue in line with higher passenger numbers. The significant increase in Heathrow Express revenue was distorted by the lower level of services in 2021.

ADJUSTED OPERATING COSTS (EXCLUDING DEPRECIATION, AMORTISATION AND EXCEPTIONAL ITEMS)

In the first nine months of 2022, adjusted operating costs increased by 47.8% to £854 million (2021: £578 million). The increase in operating costs reflects the ramp up of operations, mainly in Terminal 3 and Terminal 4. This includes costs relating to additional colleagues, overtime, recruitment and training as well as the end of the Government's furlough scheme. There has been an increase in operational and maintenance costs as a result of the reopening of operations and higher passengers compared to 2021 when we operated with only one runway and two terminals. Utilities and other costs have also been impacted by higher consumption and higher energy prices.

REGULATORY ASSET BASE (RAB) AND FINANCIAL RATIOS

At 30 September 2022, the RAB was £18,674 million (31 December 2021: £17,474 million). At 30 September 2022, the Regulatory Asset Ratios, measuring nominal net debt to RAB, were 66.4% for senior debt and 77.7% for junior debt (31 December 2021: 64.6% and 76.3% respectively) compared with respective trigger levels of 72.5% and 85.0%.

INTEREST PAYABLE AND PAID

In the first nine months of 2022, net finance costs before certain re-measurements were £1,127 million (2021: £577 million) driven by a higher accretion charge given higher levels of inflation. Net interest paid was £241 million (2021: £228 million) or £131 million excluding interest paid on the debenture to Heathrow Finance plc.

NET DEBT (EXCLUDING DEBENTURE BETWEEN HEATHROW (SP) LIMITED AND HEATHROW FINANCE PLC)

At 30 September 2022, nominal net debt was £14,514 million (31 December 2021: £13,332 million), comprising £13,982 million in bond issues, £1,430 million in other term debt, £751 million in index-linked derivative accretion, working capital facilities and £34 million of additional lease liabilities. This was offset by cash, cash equivalents and term deposits of £1,683 million. Nominal net debt consisted of £12,406 million in senior net debt and £2,108 million in junior debt.

LEASE LIABILITIES

We applied IFRS 16 on 1 January 2019. The capitalised value of existing operating leases pre-dating the transition to IFRS 16 is excluded from our net debt covenant calculations. Additional lease liabilities are however taken into account when calculating net nominal debt and amounted to £34 million as at 30 September 2022. The aggregate lease liability of all leases classified as Existing Operating Leases as at 30 September 2022 was £375 million.

5. FORECAST FINANCIAL PERFORMANCE

TRAFFIC

In 2022, traffic is expected to increase 216% to 61.4 million passengers vs. last year (2021: 19.4m). This is at the upper end of the guidance released with our Q3 results and is an increase from the forecast published in June 2022, and reflects the stronger passenger traffic recovery since travel restrictions were lifted in the UK in March. In 2023, traffic is forecast to increase 9% versus 2022 to 67.1 million passengers. Further detail on our traffic forecasts can be found on page 11.

ADJUSTED EBITDA

Adjusted EBITDA in 2022 is forecast to increase 337.0% to £1,678 million (2021: £384 million). This is driven by higher passenger numbers, with total revenue increasing by 138.5% to £2,895 million. Operating costs have increased by 46.5% to £1,217 million, reflecting the reopening of operations as we build back capacity. In 2023, we forecast Adjusted EBITDA to increase by 4.1% to £1,747 million on the back of further passenger growth.

REVENUE

Revenue in 2022 is forecasted to increase by 138.5% to £2,895 million. Aeronautical income is forecast to increase 238.7% to £1,877 million (2021: £554 million), mainly driven by traffic recovery and uplift in aero charges. Retail income is expected to increase 152.4% to £548 million (2021: £217 million), particularly as a result of strong car parking performance. However, the removal of tax-free shopping has resulted in a decline in spending per passenger to £8.93 (2021: £11.19). Other revenue is expected to increase by 6.2% to £470 million (2021: £443 million). In 2023 revenue is forecast to increase to £3,187 million as traffic continues to recover, driven by a 14.5% increase in aeronautical revenues, a 7.2% increase in retail revenues and a 4.0% decrease in non-retail revenues.

ADJUSTED OPERATING COSTS (EXCLUDING DEPRECIATION, AMORTISATION AND EXCEPTIONAL ITEMS)

Adjusted operating costs in 2022 are forecast to increase to £1,217 million (2021: £830 million) because of the increased operation ramp up costs in the year and the implementation of our build back capacity plan which builds resilience for the airport at increase passenger traffic levels. Operating costs on a per passenger basis are expected to be decreasing by 51.4% at £20.81. In 2023, operating costs are forecast to increase 18.3% to £1,440 million to support the increase in passengers, the full year effect of re-opened terminal facilities and higher utilities costs.

REGULATORY ASSET BASE

At the end of 2022 and 2023, the RAB is forecast to be £22,082 million and £22,829 million respectively (2021: £17,474 million). The increase in RAB in 2022 is driven by increasing inflation partly offset by lower capital expenditure and regulatory depreciation. The forecasts for 2022 and 2023 assume capital expenditure of £468 million and £588 million and average RPI of 11.5% and 10.4%, respectively.

NET DEBT AND FINANCIAL RATIOS

At 31 December 2022, nominal net debt is forecast to be £14,622 million (2021: £13,332 million). Net external interest paid is forecast to be £172 million in 2022 (2021: £87 million), an increase of £7 million compared to June's guidance. The Regulatory Asset Ratio (RAR) is forecast to be 56.5% for senior debt and 66.2% for junior debt (31 December 2021: 64.6% and 76.3%) driven by the expected increased growth in the RAB and increased cash balances. For the year ending 31 December 2022, the Interest Cover Ratio (ICR) is forecast to be 12.16x for senior debt and 7.21x for junior debt (2021: 10.36x and 3.15x).

All current and forecast ratios are calculated based on applicable generally accepted accounting principles.

5. FORECAST FINANCIAL PERFORMANCE

APPROACH

Heathrow has developed a forecasting approach that combines bottom-up analysis of travel restrictions by market level, with top-down analysis of longer-term econometric factors. A number of potential scenarios are considered and then a weighted combination is taken to create the below mid-case passenger forecast. This methodology reflects the amount of risk faced and so creates a balanced forecast with 50% chance of out-performance and 50% chance of under-performance. With the continuing levels of uncertainty, which have largely shifted from being pandemic focussed to the impact of the cost-of-living crisis and widely forecast expected recession, we continue to consider a range in our forecasts. The bottom-up modelling approach reflects the impact of travel restrictions at a granular market level, macro-level restrictions such as the impact on airlines and demand due to Russian airspace closure, and analysis of airline and airport capacity, such as airline fleet and availability of resource. The econometric side of our modelling considers the impact of GDP on passenger demand, as well as the potential impact from permanent reduction of business travel and the impact of the cost of carbon on fares.

ASSUMPTIONS - BASE CASE

Whilst the majority of covid restrictions have been removed we now face further uncertainty from an economics perspective with key markets already in recession or predicted to be in 2023; the fast-paced levels of growth seen in 2022 are expected to slow considerably. Air fares are expected to remain high, and will likely dampen growth as the impact of the cost-of-living is fully realised. 2022 volumes were heavily driven by pent up demand in the 'Visiting Friends & Relatives' market however this is likely to be a short-term change in behaviour following lengthy lockdowns, rather than a sustained long-term trend. We therefore expect a higher weighting of business and leisure markets to return going forwards, which have had slower rates of recovery so far. It is expected that East Asia gradually eases restrictions throughout 2023 but the impact of the Ukraine-Russian war is ongoing.

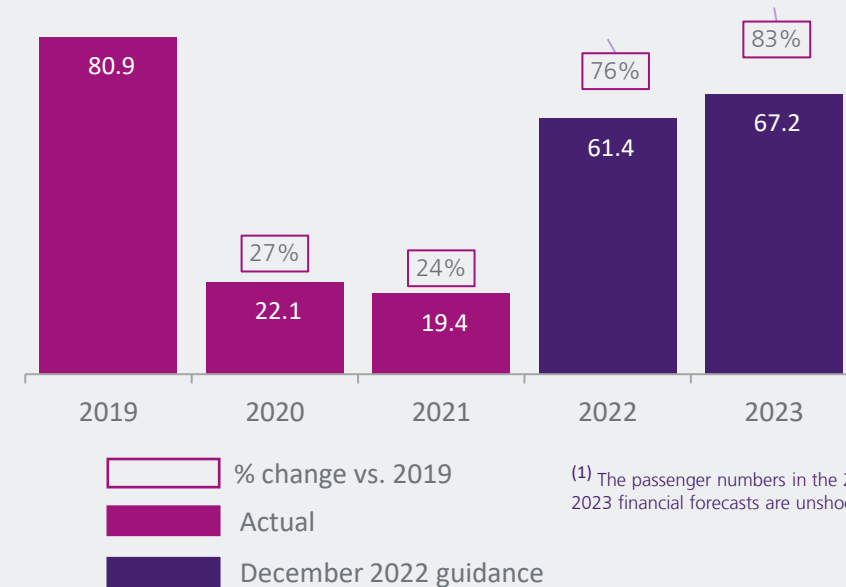
Our forecast for 2023 is based on the continuation of the recovery seen in the second half of 2022 however with some softening due to the economic climate. 2023 is expected to return to a more typical pre-Covid travel profile across the year. For the remainder of H7 the rate of growth slows over time, and we expect to be at 93% of 2019 levels (equivalent to 2016 passenger numbers).

ASSUMPTIONS – HIGH AND LOW

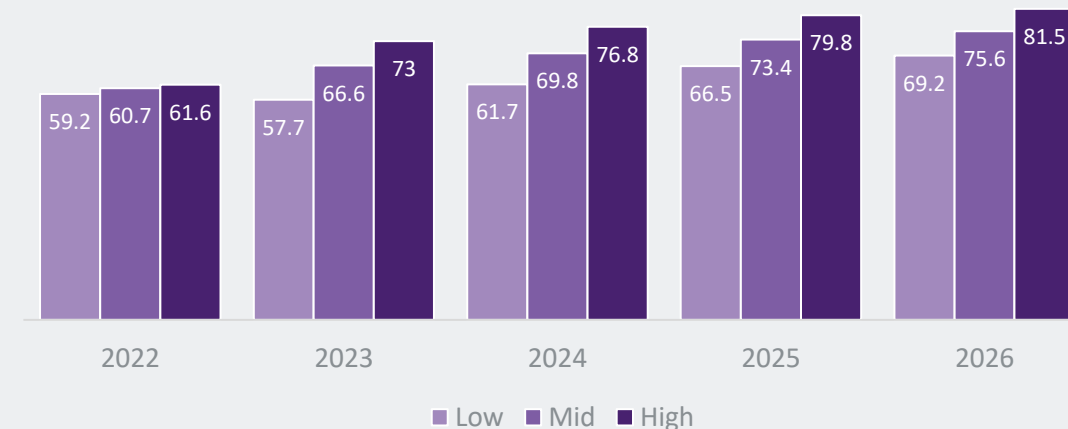
In our high scenario, the main differences in assumptions to the base case are that: all covid restrictions have lifted by early 2023; the economic outlook is aligned with a slower tightening of policy; there is a faster easing of restrictions in East Asia and Russian airspace; and an improved recovery of business travel.

In our low scenario, the main differences in assumptions to the base case are that: existing covid restrictions remain in place for longer; the pessimistic economic outlook is more pronounced and prolonged; the East Asia markets remain effectively closed throughout 2023; Russian airspace remains closed throughout H7; and business travel is slower to recover.

Annual traffic forecast⁽¹⁾ (m)



Revised H7 Passenger Forecast (December 2022)⁽²⁾



(2) The passenger numbers in the H7 revised forecast are shocked

6. FINANCING MATTERS

NEW FINANCING AND CHANGES TO FACILITIES

Since the previous Investor Report was distributed on 23 June 2022, we completed our funding plan by raising a further £210 million in new debt financing. In August, we priced £60 million of new Class A debt in the private placement market with a maturity of 2047 and, in October, we priced £150 million of new Class A debt in the private placement market across 10-year and 30-year tranches, which settled in November 2022. In total, we have raised £546 million of new term debt across 2022. Finally, in September, we successfully concluded the refinancing of our Revolving Credit Facility at a size of £1.32 billion, up from £1.15 billion, providing additional protection to our liquidity position over the H7 period. These transactions complement our robust liquidity position and show a continued appetite for Heathrow debt. During 2022, we also made early paydowns of accretion on our inflation swaps totalling £490 million.

DEBT MATURITIES AND REPAYMENTS

Since the previous Investor Report was distributed on 23 June 2022 there was a £2m amortisation repayment on a Class A index linked bond in July.

HEDGING

No derivatives have been executed since the publication of the previous Investor Report on 23 June 2022. The portfolio of derivatives has no breaks.

At 13 December 2022, the total notional value of cross-currency swaps was £5,533 million, the total notional value of index-linked swaps was £5,707 million, and the total notional value of interest rate swaps was £7,378 million.

At 13 December 2022, 92.7% and 56.4% of interest rate risk exposure on the Obligor's and Heathrow Funding's existing debt are hedged for the regulatory periods ending on 31 December 2026 and 31 December 2031, respectively. This is consistent with the requirement to hedge at least 75% and 50% of interest rate risk exposure over those periods.



6. FINANCING MATTERS

LIQUIDITY

The Security Group expects to have sufficient liquidity to meet all our forecast needs well into 2025 under our base case traffic forecast or until at least December 2023 under the extreme stress-test scenario of no revenue. The obligations include forecast operational costs and capital investment, debt service costs, debt maturities and repayments. The liquidity forecast takes into account £4.7 billion at 30 November 2022, comprising cash resources held at the Security Group and Heathrow Finance as well as committed but undrawn loan facilities and the expected operating cash flow over the period. .

HISTORICAL AND FUTURE RESTRICTED PAYMENTS

The financing arrangements of the Security Group restrict certain payments unless specified conditions are satisfied. These restricted payments include, among other things, payments of dividends, distributions and other returns on share capital; any redemptions or repurchase of share capital; and payments of fees, interest or principal on any intercompany loans.

Since the previous Investor Report was distributed on 23 June 2022, no further restricted payments have been made by Heathrow SP above the £1.1 billion (2021: nil) made in the first half of the year. In December, Heathrow Finance made a controlled payment of £0.1bn to service interest on debt held at ADIF2. The liquidity position at Heathrow Finance remains at £1.1 billion following this payment. No dividend payments to ultimate shareholders were made during the period.

CREDIT RATINGS

Management's assessment of liquidity and access to debt capital markets in affordable terms are reliant on Heathrow's ability to maintain a stable credit rating, returning to A- as soon as possible. Since the previous Investor Report was distributed on 23 June 2022 and following the publication of the H7 Final Proposals, S&P maintained their Class A (BBB+) and Class B (BBB-) ratings on CreditWatch with negative implications. In early August, Fitch affirmed the Class A (A-), Class B (BBB) and Heathrow Finance (BB+) ratings with negative outlook. Although our plans are financeable and forecast no breach of covenants, we remain of the view that the charges set out by the CAA in their Final Proposals, if they were to crystallise in the final settlement, would put pressure on our credit rating metrics.



7. CORPORATE MATTERS

ACQUISITIONS, DISPOSALS AND JOINT VENTURES

There have been no material acquisitions, disposals and joint ventures entered into related to any Obligor since the previous Investor Report was distributed on 23 June 2022.

OUTSOURCING

There have been no material outsourcing contracts entered into related to any Obligor since the previous Investor Report was distributed on 23 June 2022.

BOARD AND MANAGEMENT CHANGES

There have been no key management changes since the last Investor Report was distributed on 23 June 2022.



8. CONFIRMATION

16 December 2022

To the Borrower Security Trustee, the Issuer, the Bond Trustee, each Rating Agency, and the Paying Agents

We confirm that each of the Ratios set out on page 4 has been calculated in respect of the Relevant Period or as at the Relevant Date for which it is required to be calculated under the Common Terms Agreement.

We confirm that the historical ratios have been calculated using, and are consistent with and have been updated by reference to, the most recently available financial information required to be provided by the Obligors under Schedule 2 (Covenants) of the Common Terms Agreement.

We confirm that all forward-looking financial ratio calculations and projections:

- have been made on the basis of assumptions made in good faith and arrived at after due and careful consideration;
- are consistent and updated by reference to the most recently available financial information required to be produced by the Obligors under Schedule 2 (Covenants) of the Common Terms Agreement; and
- are consistent with the Applicable Accounting Principles (insofar as such Applicable Accounting Principles reasonably apply to such calculations and projections).

We also confirm that:

- no Default or Trigger Event has occurred or is continuing;
- the Group is in compliance with the Hedging Policy; and
- this Investor Report is accurate in all material respects.

Javier Echave



Chief Financial Officer

For and on behalf of LHR Airports Limited as Security Group Agent

APPENDICES



APPENDIX 1 - QUARTERLY PASSENGER TRAFFIC (2008 TO 2022)

Heathrow passenger traffic and air transport movement evolution

Change versus previous year (totals and changes based on unrounded data)

Passengers (m)	2008	2009	2010	2011	2012	2013	2014	2015	2016	2016	2018	2019	2020	2021	2022
Jan-Mar	15.4	14.4	14.6	15.0	15.7	16.0	16.0	16.4	16.8	17.2	17.7	17.9	14.6	1.7	9.7
Change %	0.6	(6.4)	1.6	2.5	4.4	1.8	0.5	2.0	2.6	2.2	3.1	1.4	(18.3)	(88.5)	474.9
Apr-Jun	17.1	16.8	15.5	17.9	17.9	18.4	19.0	19.2	18.9	20.0	20.4	20.8	0.7	2.2	16.4
Change %	(1.3)	(1.5)	(7.9)	15.3	0.4	2.9	3.2	0.7	(1.1)	5.4	2.1	2.1	(96.2)	176.6	657.1
Jul-Sep	18.6	18.6	19.5	19.8	19.4	20.4	20.6	21.4	21.6	21.9	22.5	22.2	3.5	6.3	18.1
Change %	(1.2)	0.3	4.4	1.5	(2.0)	5.5	0.7	3.9	0.9	1.7	2.4	(1.1)	(84.1)	78.3	187.2
Oct-Dec(1)	15.9	16.0	16.1	16.8	17.0	17.5	17.7	18.0	18.4	18.9	19.6	19.9	3.1	6.1	11.5
Change %	(3.6)	1.1	0.7	3.8	1.6	2.7	1.3	1.9	1.8	3.0	3.4	1.8	(84.3)	194.3	N/A
Full year	66.9	65.9	65.7	69.4	70.0	72.3	73.4	75.0	75.7	78.0	80.1	80.9	22.1	19.4	55.7
Change %	(1.4)	(1.5)	(0.2)	5.5	0.9	3.4	1.4	2.2	1.0	3.1	1.4	1.0	(77.7)	(12.3)	187.1
ATM ('000)	473	460	449	476	471	470	471	472	473	474	476	476	201	190	343
Change %	(0.5)	(2.8)	(2.3)	6.0	(1.0)	(0.4)	0.2	0.3	0.2	0.2	0.3	0.0	(57.8)	(5.4)	80.2

(1) Oct-Dec 2022 excludes December.

APPENDIX 2 - COMPUTATION OF INTEREST COVER RATIOS⁽¹⁾ (‘ICR’)

<i>(See important notice on page 2 of this document)</i>	Trigger Level	Year to 31 December 2022 (£m)	Year to 31 December 2023 (£m)
Cashflow from Operations ⁽²⁾		1,685	1,737
Add back: Cash payments in respect of prior year exceptional items		-	-
Adjusted Cashflow from Operations		1,685	1,737
Less: corporation tax relief / (paid)		-	-
Less: 2 per cent of Total RAB		(442)	(457)
Cash Flow (A)		1,243	1,280
Interest and equivalent recurring charges paid on Senior Debt ⁽³⁾⁽⁴⁾			
Interest paid – Class A bonds and swaps		55	435
Interest paid and received – other Class A debt and new debt issued since 1 January 2022		25	35
Interest paid – Class A revolving credit facilities		-	-
Lease interest		20	18
Commitment fees on liquidity and revolving credit facilities		2	4
Total interest on Senior Debt (B)		102	492
Interest and equivalent recurring charges paid on Junior Debt ⁽³⁾⁽⁴⁾			
Class B debt		70	78
Total interest on Junior Debt (C)		70	78
Total interest (D=B+C)		172	570
Senior ICR (A/B)⁽⁵⁾⁽⁶⁾⁽⁷⁾	1.40x	12.16x	2.60x
Junior ICR (A/D)⁽⁵⁾⁽⁶⁾⁽⁷⁾	1.20x	7.21x	2.25x

(1) 2022 and 2023 figures are forecasts; values calculated on unrounded figures

(2) Reconciliation of cash flow from operations with Adjusted EBITDA is set out on page 19

(3) Reconciliation of interest paid with interest payable is set out on page 19 for 2022

(4) Excludes interest on debenture between Heathrow (SP) Limited and Heathrow Finance plc as this is not included in calculation of ratios under the Common Terms Agreement

(5) Interest Cover Ratio is cash flow from operations less 2% of RAB and corporation tax paid to HMRC divided by net interest paid

(6) Ratios calculated on unrounded figures

(7) We have run a sensitivity on Senior and Junior RAR assuming no further RAB adjustment to the £300m granted by the CAA. Under this sensitivity we forecast closing RAB of £19,219m and £19,795m for 2022 and 2023 respectively. Senior ICR would be 12.72x and 2.73x respectively. Junior ICR would be 7.55x and 2.35x respectively.

APPENDIX 2 - COMPUTATION OF INTEREST COVER RATIOS⁽¹⁾ – RECONCILING INCOME STATEMENT TO CASH FLOW

(See important notice on page 2 of this document)

	Year to 31 December 2022 (£m)	Year to 31 December 2023 (£m)
Income		
Aeronautical income	1,877	2,148
Non-aeronautical income - retail	548	587
Non-aeronautical income – non-retail	470	452
Total income	2,895	3,187
Operating costs⁽²⁾	(1,217)	(1,440)
Adjusted EBITDA	1,678	1,747
Working capital and cash one-off non-recurring extraordinary or exceptional items		
Cash payments in respect of prior year exceptional items	-	-
Trade working capital	7	(11)
Pension	-	1
Cashflow from operations	1,685	1,737

	Year to 31 December 2023	Year to 31 December 2022			Cash flow £m
	Cash flow £m	Income statement incl. amortisation ⁽³⁾⁽⁴⁾ £m	Less amortisation ⁽³⁾ £m	Less variation in accruals ⁽³⁾ £m	
Interest paid – Class A bonds and swaps	435	164	(44)	(65)	55
Interest paid and received – other Class A debt and new debt issued since 1 January 2022	35	27	-	(2)	25
Lease interest	18	17	-	3	20
Commitment fees on liquidity & RCFs ⁽⁵⁾	4	1	-	1	2
Interest paid – Class B debt	78	66	2	2	70
Total interest⁽¹⁾	570	275	(42)	(61)	172

(1) 2022 and 2023 figures are forecasts; values calculated on unrounded figures

(2) Adjusted operating costs: operating costs excluding depreciation, amortisation and exceptional items.

(3) Excludes capitalised interest; Excludes interest on debenture between Heathrow (SP) Limited and Heathrow Finance plc as this is not included in calculation of ratios under the Common Terms Agreement

(4) Includes amortisation of refinancing fees and excludes accretion on Index Linked Swaps and bonds

(5) RCFs: Revolving Credit Facilities

APPENDIX 3 - COMPUTATION OF REGULATORY ASSET RATIOS⁽¹⁾ ('RAR')

<i>(See important notice on page 2 of this document)</i>	Trigger Level	Year to 31 December 2022 (£m)	Year to 31 December 2023 (£m)
Closing Heathrow RAB (A)		22,082	22,829
Senior Debt			
Class A existing bonds		11,856	11,216
Class A EIB facilities		-	-
Non - Existing Operating Lease debt		55	55
Other Class A debt and new debt issued since 1 January 2022		1,651	2,251
RPI swap accretion		684	803
Total Senior Debt (B)		14,246	14,325
Junior Debt			
Class B existing debt		2,137	2,349
Other Class B debt		-	-
Total Junior Debt (C)		2,137	2,349
Cash and cash equivalents (D)		(1,761)	(1,645)
Senior net debt (E=B+D)		12,485	12,680
Senior and junior net debt (F=B+C+D)		14,622	15,029
Senior RAR (E/A)⁽²⁾⁽³⁾⁽⁴⁾⁽⁵⁾	72.5%	56.5%	55.5%
Junior RAR (F/A)⁽²⁾⁽⁴⁾⁽⁵⁾	85.0%	66.2%	65.8%

(1) 2022 and 2023 figures are forecasts; values calculated on unrounded figures

(2) Regulatory Asset Ratio is the ratio of nominal net debt (including index-linked accretion) to RAB (Regulatory Asset Base)

(3) Senior RAR does not take into account ability to reduce senior debt using undrawn junior debt under revolving credit facilities

(4) Ratios calculated on unrounded figures

(5) We have run a sensitivity on Senior and Junior RAR assuming no further RAB adjustment to the £300m granted by the CAA. Under this sensitivity we forecast closing RAB of £19,219m and £19,795m for 2022 and 2023 respectively. Senior RAR would be 65.0% and 64.1% respectively. Junior RAR would be 76.1% and 75.9% respectively.

APPENDIX 4 – NOMINAL CONSOLIDATED NET DEBT OF OBLIGORS, HEATHROW FUNDING LIMITED AND HEATHROW FINANCE PLC AS AT 30 SEPTEMBER 2022

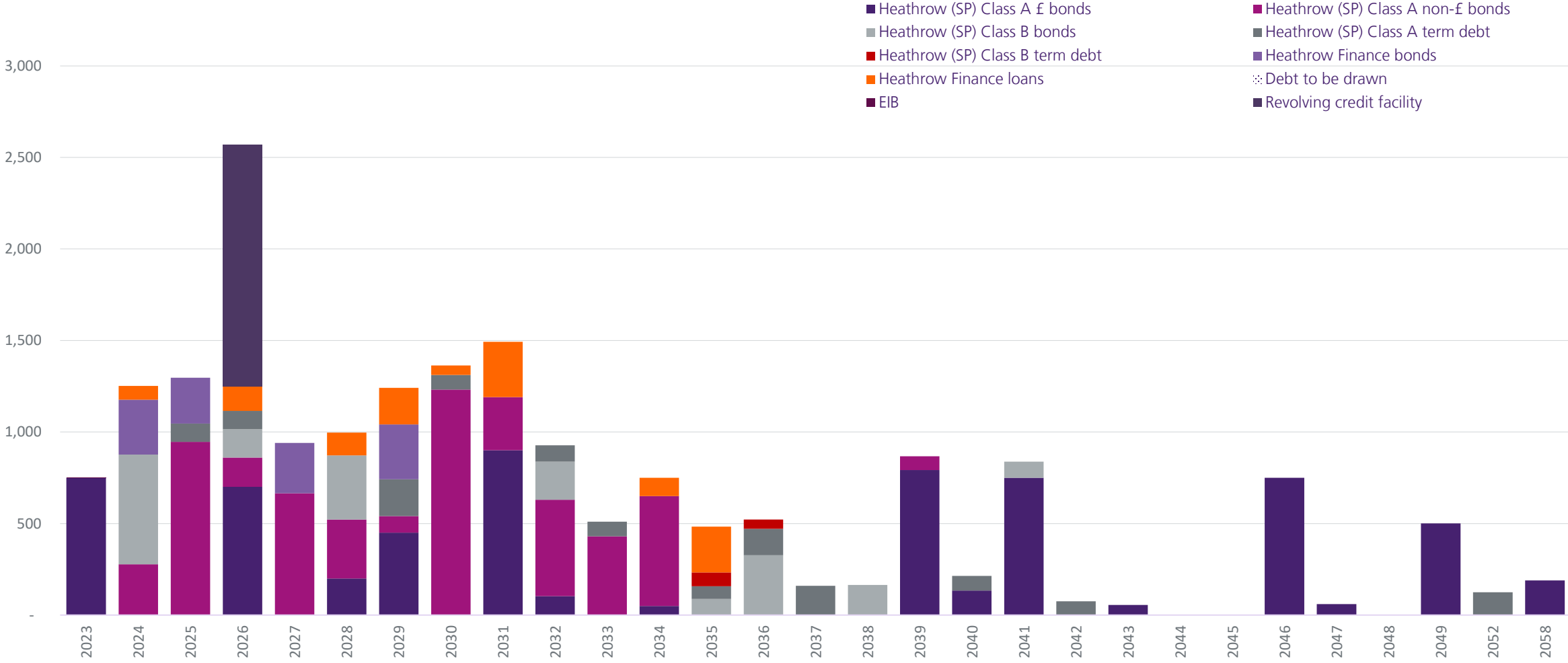
Heathrow (SP) Limited	Amount	Available	Maturity
Senior debt	(£m)	(£m)	
£750m 5.225%	750	750	2023
CHF400m 0.5%	277	277	2024
C\$500m 3.25%	266	266	2025
£750m 1.50%	681	681	2025
CHF210m 0.45%	161	161	2026
£700m 6.75%	700	700	2026
NOK1,000m 2.65%	84	84	2027
C\$650m 2.7%	374	374	2027
C\$400m 3.4%	226	226	2028
£200m 7.075%	200	200	2028
A\$175m 4.150%	96	96	2028
CHF165m 1.800%	136	136	2029
£450m 2.75%	450	450	2029
NOK1,000m 2.50%	91	91	2029
€750m 1.5%	566	566	2030
C\$400m 3.872%	238	238	2030
€500m 1.125%	427	427	2030
C\$500m 3.661%	291	291	2031
£900m 6.45%	900	900	2031
€50m Zero Coupon	42	42	2032
£75m RPI +1.366%	103	103	2032
€50m Zero Coupon	42	42	2032
€500m 1.875%	443	443	2032
C\$300m 3.7%	363	363	2033
€650 1.875%	559	559	2034
£50m 4.171%	50	50	2034
€50m Zero Coupon	40	40	2034
£50m RPI +1.382%	67	67	2039
€86 Zero Coupon	75	75	2039
£460m RPI +3.334%	724	724	2039
¥10,000m 0.8%	71	71	2039
£100m RPI +1.238%	133	133	2040
£750m 5.875%	750	750	2041
A\$125m 3.500%	68	68	2041
£55m 2.926%	55	55	2043
£750m 4.625%	750	750	2046
£60m 4.702%	60	60	2047
£75m RPI +1.372%	101	101	2049
£400m 2.75%	400	400	2049
£160m RPI +0.147%	189	189	2058
Total senior bonds	11,999	11,999	
Term debt	1,305	1,305	Various
Index-linked derivative accretion	751	751	Various
Revolving / WC facilities	0	970	2026
Operating lease liability	34	34	Various
Total other senior debt	2,090	3,060	
Total senior debt	14,089	15,059	
Heathrow (SP) Limited cash	(1,683)		
Senior net debt	12,406		

Heathrow (SP) Limited	Amount	Available	Maturity
Junior debt	(£m)	(£m)	
£600m 7.125%	600	600	2024
£155m 4.221%	155	155	2026
£350m 2.625%	350	350	2028
£182m 0.101%	208	208	2032
£75m RPI + 0.347%	89	89	2035
£75m RPI + 0.337%	89	89	2036
£180m RPI +1.061%	238	238	2036
£51m RPI + 0.419%	60	60	2038
£105m 3.460%	105	105	2038
£75m RPI + 0.362%	89	89	2041
Total junior bonds	1,983	1,983	
Term debt	125	125	Various
Junior revolving credit facilities	0	350	2026
Total junior debt	2,108	2,458	
Heathrow (SP) Limited group net debt	14,514		

Heathrow Finance plc	Amount	Available	Maturity
	(£m)	(£m)	
£300m 4.75%	300	300	2024
£250m 5.75%	250	250	2025
£275m 3.875%	275	275	2027
£300m 4.125%	300	300	2029
Total bonds	1,125	1,125	
£75m	75	75	2024
£135m	135	135	2026
£125m	125	125	2028
£150m	200	200	2029
£52m	53	53	2030
£301m	301	301	2031
£52m	100	100	2034
£300m	250	250	2035
Total loans	1,239	1,239	
Total Heathrow Finance plc debt	2,364	2,364	
Heathrow Finance plc cash	(1,255)		
Heathrow Finance plc net debt	1,109		

Heathrow Finance plc group	Amount	Available
	(£m)	(£m)
Heathrow (SP) Limited senior debt	14,089	15,059
Heathrow (SP) Limited junior debt	2,108	2,458
Heathrow Finance plc debt	2,364	2,364
Heathrow Finance plc group debt	18,561	19,881
Heathrow Finance plc group cash	(2,938)	
Heathrow Finance plc group net debt	15,623	

APPENDIX 5 – DEBT MATURITY PROFILE AS AT 30 SEPTEMBER 2022



APPENDIX 6 – ADDITIONAL INFORMATION FOR HEATHROW FINANCE PLC CREDITORS⁽¹⁾

<i>(See important notice on page 2 of this document)</i>	Covenant / Trigger Level	As at or for year to 31 December 2022 (£m)	As at or for year to 31 December 2023 (£m)
Calculation of Group ICR⁽²⁾			
Cash Flow (A)		1,243	1,280
Interest			
Paid on Senior Debt (B)		102	492
Paid on Junior Debt (C)		70	78
Paid on Borrowings (D)		118	95
Group Interest Paid (E=B+C+D)		290	665
Group ICR (A/E) ⁽²⁾⁽⁵⁾	1.00x	4.29x	1.93x
Calculation of Group RAR⁽³⁾			
Total RAB (F)		22,082	22,829
Net debt			
Senior Net Debt (G)		12,485	12,680
Junior Debt (H)		2,137	2,349
Borrower Net Debt (I)		1,239	1,389
Group Net Debt (J=G+H+I)		15,861	16,418
Junior RAR ((G+H)/F) ^{(3) (4)}	82.0%	66.2%	65.8%
Group RAR (J/F) ⁽⁴⁾⁽⁵⁾	92.5%	71.8%	71.9%

(1) 2022 and 2023 figures are forecasts

(2) ICR or Interest Cover Ratio is defined on page 18

(3) RAR or Regulatory Asset Ratio is defined on page 20

(4) Ratios calculated on unrounded data

(5) We have run a sensitivity on Group ICR and Group RAR assuming no further RAB adjustment to the £300m granted by the CAA. Under this sensitivity we forecast closing RAB of £19,219m and £19,795m for 2022 and 2023 respectively. Group ICR would be 4.48x and 2.02x respectively. Group RAR would be 82.5% and 82.9% respectively.

Heathrow