

BAA and Regulation

May - 2007

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BAA 

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- I. Regulatory bodies – Regulatory reviews**
- II. Setting the price cap**
- III. Q4 performance to date**
- IV. CAA Q5 March 07 proposal**
- V. White Paper**
- VI. CC Market investigation (OFT referral)**
- VII. Airport charges in Europe**

I. Regulatory bodies – Regulatory review



Department for Transport

- Responsible for setting aviation policy (security levels)
- DfT decides which airports are price controlled
- In Feb 07 the DfT published the proposed designation and de-designation criteria for airports.



Civil Aviation Authority

- Independent of government
- Set Price caps for “designated airports”



Competition Commission

- Independent of government
- Price control – to review CAA proposals and advise CAA
- Structure – consider any OFT reference and conclude (or advise) on any findings



Office of Fair Trading

- Independent of government
- Investigation of market dominance under Competition Act
- Investigation of market structure under Enterprise Act



Competition Appeal Tribunal

- Independent of government and the regulators
- Decides appeals on regulatory decisions made by CC or OFT, but not CAA
- Anyone can appeal
- Also decides appeals on non-decisions



Department for Transport ("DfT")

- Responsible for setting aviation policy
- Policy objectives set out in 2003 Air Transport White Paper and confirmed in Dec 2006 in the Progress Report
 - Stansted 2nd runway as soon as possible
 - Heathrow 3rd runway, if environmental constraints met
 - If constraints not met at Heathrow, then second runway at Gatwick
 - But not before 2019
- ADI commitment to White Paper objectives is critical
- DfT decides which airports are price controlled: In Feb 2007 the DfT issued the proposal for designation and de-designation for airports.



Civil Aviation Authority (“CAA”)

- Independent of government
- Duties and objectives set out in 1986 Airports Act
- Price caps are set for “designated airports”
 - Heathrow, Stansted, Gatwick from BAA and Manchester Airport.
 - DfT decides on designation or de-designation or re-designation
- The Airports Act specifies that the CAA must perform its regulatory functions in setting price caps in the manner which it considers best calculated:
 - To further the reasonable interest of users of airports within the UK
 - To promote the efficient, economic and profitable operation of such airports
 - To encourage investment in new facilities at airports in time to satisfy anticipated demands by the users of such airports
 - To impose the minimum restrictions that are consistent with the performance by the CAA of these functions

CAA Objectives in Comparison with other Regulators

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- In contrast to other UK regulators, CAA must encourage investment and promote efficient, economic and profitable operation of airports

Network Rail (ORR)	Gas and Electricity (Ofgem)	Water Sector (Ofwat)	Airports (CAA)
ORR's principal functions are: ▶ Effective regulation to ensure that Network Rail manages the network efficiently and in a way that meets the needs of users ▶ Encourage improvement of health and safety performance and ensure compliance with relevant health and safety law, taking enforcement action as necessary ▶ Develop policy and enhance relevant railway health and safety legislation ▶ License operators of railway assetsSet the terms for access by operators to the network and other railway facilities Enforce domestic competition law	Ofgem's principal functions are: ▶ Protect and advance the interests of consumers by promoting competition where possible, and through regulation only where necessary ▶ Make gas and electricity markets work effectively ▶ Regulate monopoly businesses intelligently ▶ Secure Britain's gas and electricity supplies ▶ Meet its increased social and environmental responsibilities Ofgem operates under the direction and governance of the Gas and Electricity Markets Authority, which makes all major decisions and sets policy priorities for Ofgem	Ofwat main roles are: ▶ To regulate in a way that provides incentives and encourages the companies to achieve a world-class service in terms of quality and value for customers in England and Wales • Setting limits on what companies can charge • Ensuring companies carry out their responsibilities under the Water Industry Act 1991; • Protecting the standard of service • Encouraging companies to be more efficient; • Helping to encourage competition where appropriate	CAA's duties: ▶ To further the reasonable interests of users of airports in the UK ▶ To promote the efficient, economic and profitable operation of such airports ▶ To encourage investment in new facilities at airports in time to satisfy anticipated demands by the users of such airports ▶ To impose the minimum restrictions that are consistent with the performance by the CAA of its functions under those sections



Competition Commission ("CC")

- Independent of government
- Two roles
 - Price control – to review CAA proposals and advise CAA
 - Duties set out as for CAA in Airports Act
 - Structure – to consider the OFT reference and conclude (or advise) on any findings before March 2009
 - Duties set out in Enterprise Act

Office of Fair Trading (“OFT”)

OFFICE OF FAIR TRADING

- Independent of government
- Two roles
 - Investigation of market dominance under Competition Act
 - Investigation of market structure under Enterprise Act



Competition Appeals Tribunal (“CAT”)

- Independent of government and the regulators
- Decides appeals on regulatory decisions made by CC or OFT, but not CAA
- Anyone can appeal
- Also decides appeals on non-decisions

Q5

Setting aeronautical tariffs (2008/2013)
(Heathrow & Gatwick)

March 2007

CAA made reference to the Competition Commission (CC)

September 2007

CC reports to the CAA

November 2007

CAA publishes firm proposal for Q5

January 2008

CAA conducts oral hearings

March 2008

CAA issues price cap decision for Q5

April 2008

New price controls take effect

OFT

Review of BAA
(All airports)

March 2007

OFT made reference to the CC

Late 2007 / early 2008

CC publishes “emerging thinking” statement

Late 2008

CC publishes “remedies”

March 2009 (at the latest)

CC publishes report

2010

Possible further consultation by CAA or government
or appeal to Competition Appeals Tribunal

- **Five year review period**

- but can be extended

- **Price Cap**

- For each of the years during the five year period the CAA stipulates the level of change in aeronautical charges in terms of a formula related to changes in inflation as Retail Price Index ("RPI"). This is known as RPI - X.

- **Single-till approach**

- A method for setting a price cap for airport charges which takes account of the assets, costs and revenues of both aeronautical and commercial activities of the airport operator and relevant companies within its group.

- **Standalone basis**

- Under this approach individual price caps are set for each airport with reference to the individual airport's revenues and costs. Under this mechanism, the CAA would set charges for each airport based on its own return on RAB.

- By contrast on the "system basis", price caps are set based on consideration of the BAA London airports combined revenues and costs.

- In 2005, airlines and airports were tasked by CAA to agree some of the main inputs of the price control. This process will continue until June 2007.
- These elements included
 - Airport strategy
 - Traffic volumes
 - Capital expenditure priorities
 - Capital expenditure efficiency
 - Service quality
 - Opportunities for operating expenditure efficiencies
 - Non regulated revenues
- Extensive consultation structure at Heathrow and Gatwick. Broad agreement reached on
 - Traffic, capital expenditure efficiency, airport strategy and service quality. Capex priorities agreed at Gatwick and Heathrow
- A positive innovative regulatory step
 - Mitigates regulatory risk going into the next Quinquennium
 - BAA and airlines making in effect a joint submission to the regulator on these issues and therefore more likely to get regulatory approval
- Stansted
 - Formal CE process did not work

II. Setting the price cap

- **Building blocks**
- **Return on RAB**
- **Capital expenditure**
- **Allowed return**
- **Regulatory depreciation**
- **Opex**
- **Pricing profile**
- **Other income/ Commercial revenue**
- **Traffic forecast**

Building Blocks Approach

+ **Return on RAB** = Average Closing RAB x WACC + PPA

+ **Return of RAB** = Regulatory Depreciation

+ **Operating Expenditure**

Total Revenue Requirement

- **Commercial Revenues – Non-regulated charges – Other revenues**

Net Revenue Requirement

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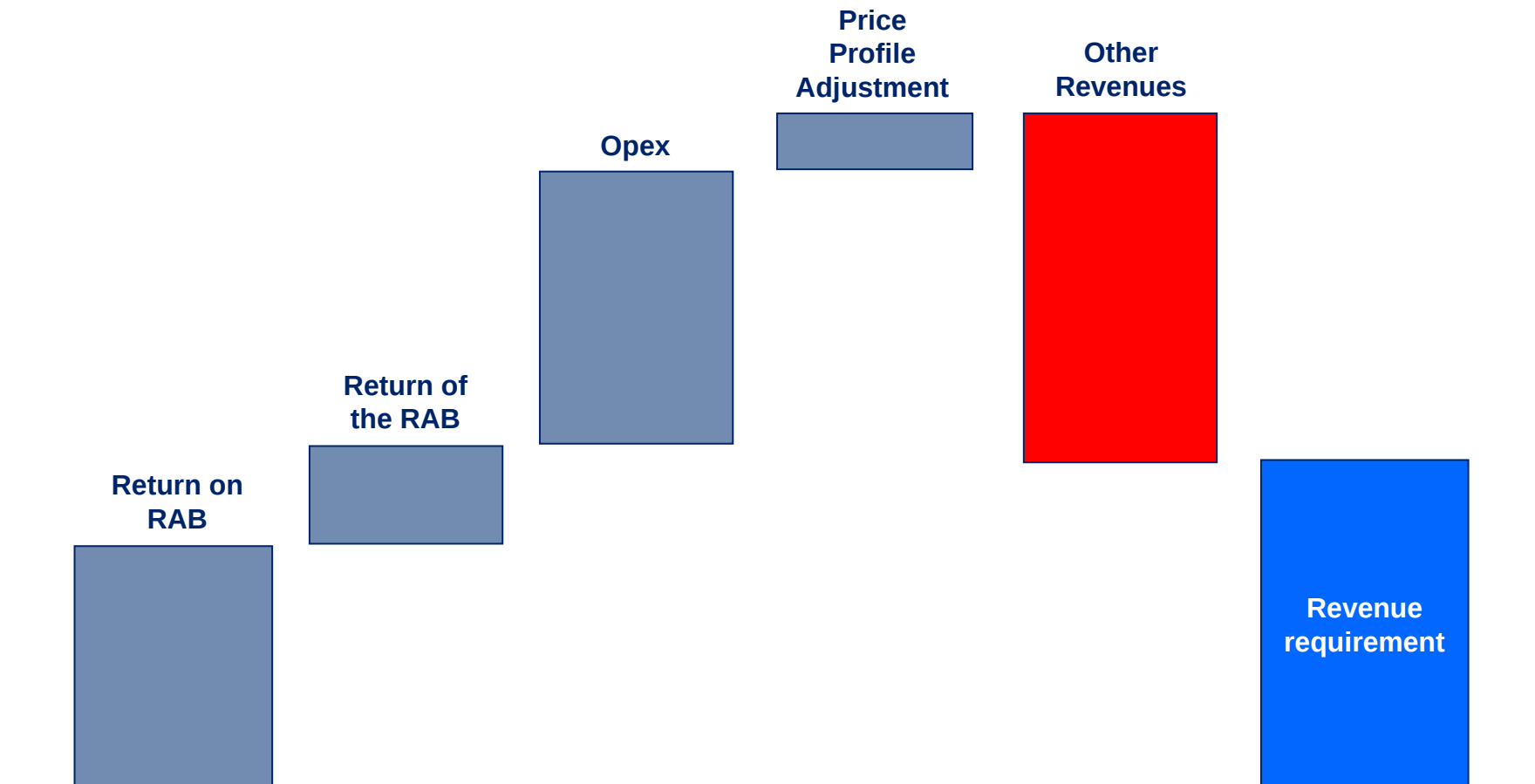
Passengers

Yield per passenger = Maximum allowed aeronautical charges

Profiled yield per passenger

‘Single till’ scheme

Decision set in real prices leads to airport charges in “money of the day”



- **RAB**: all airport operational assets – runways, terminals, shops, car parks, offices, cargo, maintenance.
- The RAB includes
 - Capex, assets in the course of construction, profiling adjustments, capitalised operating costs
 - Includes Heathrow Express and assets of HAL, GAL and STAL
 - Excludes property in APP transaction
 - Q5 RAB should include actual Q4 capex (but not financing cost / benefit of any over-spend / under-spend)
- The RAB is calculated by CAA at the start of each quinquennium
 - It is not further endorsed by CAA until the start of the next quinquennium
- Assets currently removed at “open market value” at the time of transaction but not endorsed by CAA until setting the opening RAB
- The RAB is adjusted **annually** by:
 - Opening RAB (Indexed to RPI)
 - + Capex
 - Forecast regulatory depreciation
 - Proceeds from disposals (if any)
 - Closing Basic RAB
 - =====
 - +/-PPA
 - Closing RAB
 - =====
- The RAB is reported in BAA’s regulatory accounts

Capital Expenditure

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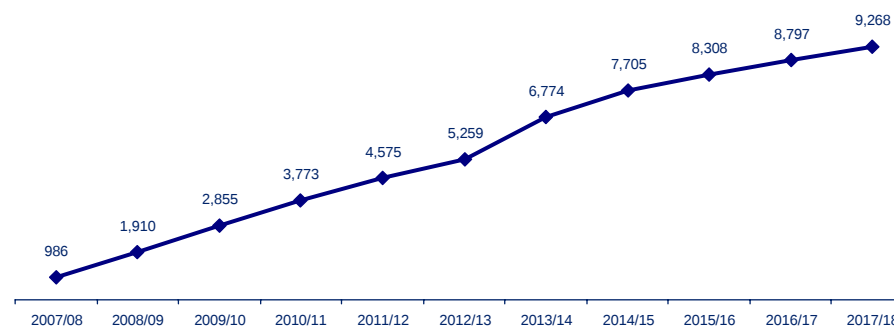


- The business has a substantial capital investment programme with £9.3bn is to be spent on the three Designated airports, the principle projects at which comprise:

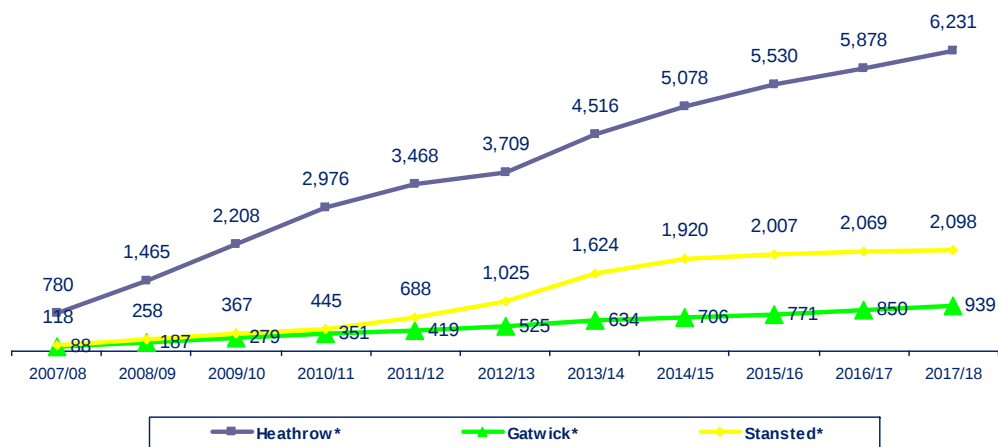
Project	Date	Amount
LHR T5	2007-12	£ 0.7 bn
LHR East Ph.1	2007-12	£ 1.1 bn
LHR East Ph.2	2013-16	£ 0.5 bn
STN G2 Ph.1	2007-16	£ 1.5 bn

- Within a five year price control period, the published regulatory RAB will flex to capture actual capex over- or under-spend, as reported in the regulatory accounts

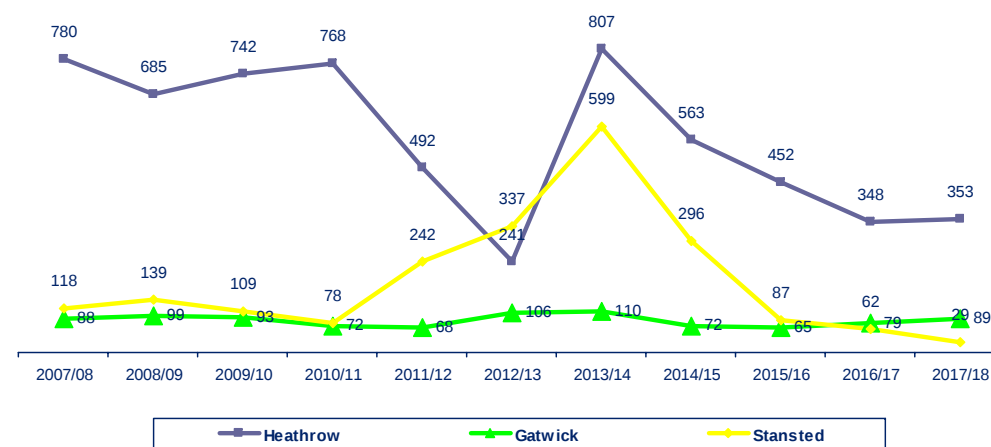
Cumulative investment programme 2007/18 in London airports



Cumulative investment programme 2007/18 by Airports



Investment programme 2007/18 by Airports



▪ CAA's proposal is **unacceptable**

▪ Debt Beta: inconsistent with Q4 calculations

▪ Unprecedented reduction in the return on regulated assets

▪ Lack of commitment and incentive

CC Q4		Parameter	Heathrow CAA Q5	
Low	High		Low	High
2.50%	2.75%	Real Risk Free Rate (Rf)	2.00%	2.00%
2.50%	4.50%	Equity Market Risk Premium (EMRP)	4.50%	4.50%
		Debt beta	0.20	0.20
0.60	0.75	Asset beta	0.58	0.63
25%	25%	Gearing (% of debt)	60%	60%
0.80	1.00	Equity Beta post-tax	1.13	1.26
4.50%	7.25%	Cost of equity (post tax)	7.09%	7.68%
30.00%	30.00%	Taxation Adjustment	30.00%	30.00%
6.43%	10.36%	Cost of equity (pre - tax)	10.12%	10.97%
0.90%	1.20%	Debt premium	1.00%	1.00%
3.40%	3.95%	Cost of debt	3.00%	3.00%
5.67%	8.76%	Pre - Tax WACC	5.85%	6.19%
0.25%	T5 adjustment			
0.25%	ERP adjustment			
7.75%	Pre-tax WACC			

Allowed return – Gatwick

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CC Q4			Gatwick CAA Q5	
Low	High	Parameter	Low	High
2.50%	2.75%	Real Risk Free Rate (Rf)	2.00%	2.00%
2.50%	4.50%	Equity Market Risk Premium (EMRP)	4.50%	4.50%
		Debt beta	0.20	0.20
0.60	0.75	Asset beta	0.64	0.71
25%	25%	Gearing (% of debt)	60%	60%
0.80	1.00	Equity Beta post-tax	1.30	1.48
4.50%	7.25%	Cost of equity (post tax)	7.80%	8.70%
30.00%	30.00%	Taxation Adjustment	30.00%	30.00%
6.43%	10.36%	Cost of equity (pre - tax)	11.20%	12.43%
0.90%	1.20%	Debt premium	1.00%	1.00%
3.40%	3.95%	Cost of debt	3.00%	3.00%
5.67%	8.76%	Pre - Tax WACC	6.28%	6.70%
0.25%	T5 adjustment			
0.25%	ERP adjustment			
7.75%	Pre-tax WACC			

- For a quinquennium the Allowed return on assets can be calculated as an IRR
- The calculations are done in real prices (charges are set in real prices)
- The Allowed return is the IRR of the following cash flows in real prices:
 - Opening RAB as an cash outflow
 - + EBITDA
 - CAPEX
 - + Closing RAB

Example – Heathrow Q4 Determination

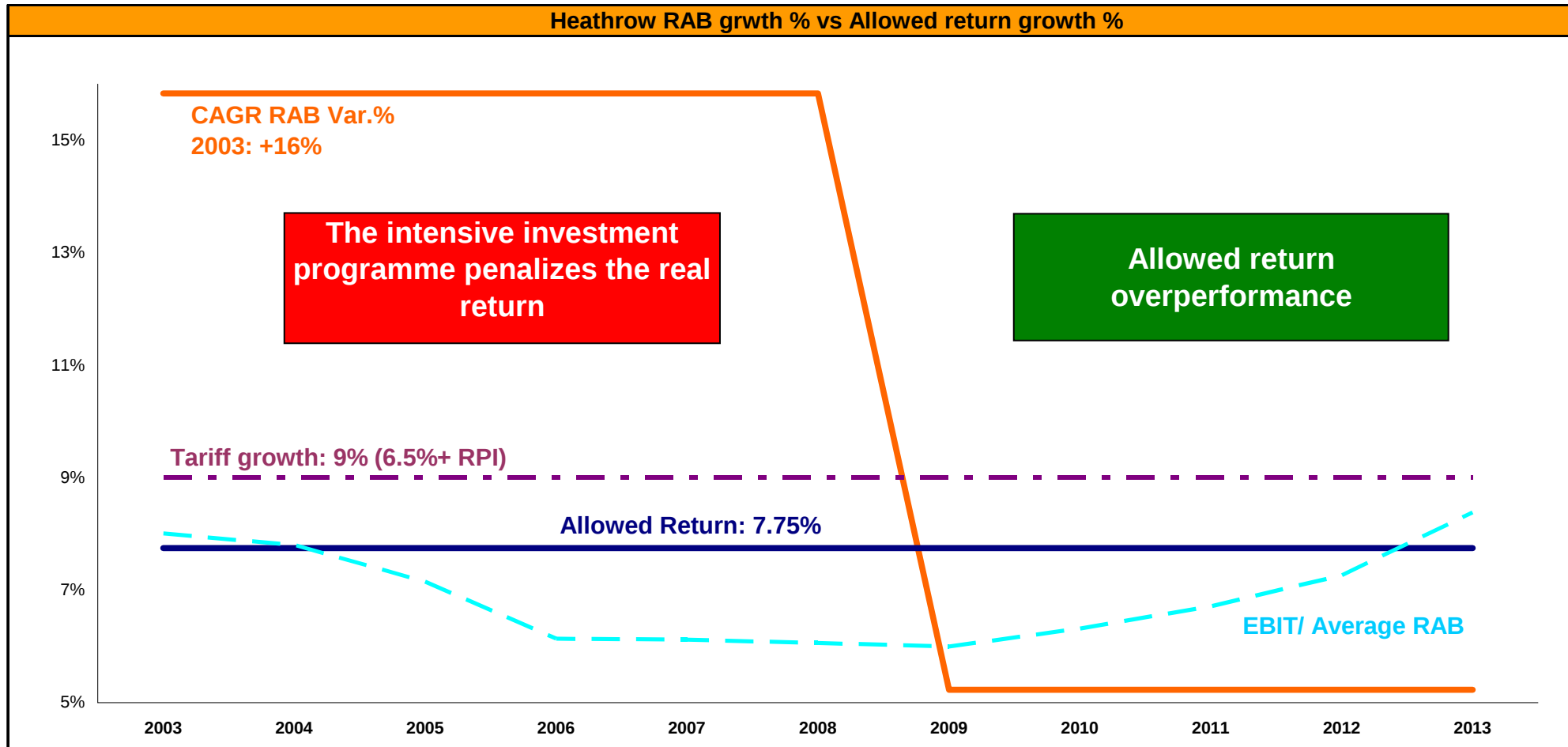
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IRR and accounting rate of return							
	31/03/2003	30/09/2003	30/09/2004	30/09/2005	30/09/2006	30/09/2007	31/03/2008
RAB	4,025,657	4,529,827	5,073,560	5,776,969	6,340,539	6,918,887	6,918,887
Operating Revenue		926,570	958,834	990,456	1,028,269	1,068,000	
Operating Cost		-414,008	-421,400	-435,350	-437,768	-444,749	
Capex		-792,088	-817,431	-948,334	-796,497	-801,407	
Cashflow		-279,526	-279,997	-393,228	-205,996	-178,156	
Clawback		-94,385	-94,385	-94,385	-94,385	-94,385	
Profiling		-135,651	-111,466	-81,099	-64,573	-43,578	
Depreciation		-152,267	-162,232	-163,826	-168,354	-179,481	
Regulated Cashflow	-4,025,657	-185,141	-185,612	-298,843	-111,611	-83,771	6,918,887
Accounting rate of return		7.47%	7.47%	7.47%	7.47%	7.47%	
IRR	7.74%						

Regulated cashflow = operating revenue - operating cost - capex + clawback

Accounting rate of return = (operating revenue - profiling + clawback - operating cost - depreciation) / average RAB



- Regulatory depreciation is forecast by CAA in setting the formula
- Based on BAA forecasts
- Standard depreciation calculation, but based on indexed cost
 - ie Gross (indexed) Book Value / asset lives
- But, forecast depreciation not actual depreciation is used to roll the RAB forward
- Reported in regulatory accounts
- Differences between Q4 forecast and actual (on regulatory basis) as at April 2006
 - Heathrow, actual £83m higher
 - Gatwick, actual £7m lower
- So, Q5 RAB is lower than it should be for Heathrow, but higher for Gatwick
- The differences between the regulatory and the statutory depreciation are:
 - Investment properties are carried at fair value in the statutory accounts and at cost (indexed) in the regulatory accounts. These are not depreciated in the statutory accounts but are depreciated in the regulatory accounts
 - The RAB is indexed every year, whereas the asset register used for the statutory purposes is not
 - The asset values in the statutory asset register incorporate capitalised financial expenses

Operating expenditure

Year ended 31 March 2006

	Heathrow		Gatwick	
	Regulatory accounts	Statutory accounts	Regulatory accounts	Statutory accounts
£ millions				
Staff	181.8	181.8	80.3	80.3
Maintenance equipment	63.4	63.4	21.7	21.7
Rent and rates	55.4	55.4	20.4	20.4
Utility costs	60.3	60.3	21.3	21.3
Police	27.4	27.4	12.6	12.6
Rail	42.7	0	0	0
Retail expenditure	0	6.3	0	2.9
Other costs	46.4	46.4	17.9	17.9
Intra-group charges	53	148.2	31.5	35
Reorganisation cost	25.4	25.4	18	18
Service quality rebate	-1.7	0	-0.3	0
Profit on disposals	0	-2.8		
Operating cost (ex depreciation)	554.1	611.8	223.4	230.1
Operating cost (incl. depreciation)		780.3		280.9

- Security costs arising from new security directives issued in 2006
 - Heathrow £38m
 - Gatwick £17m
 - Stansted £8m
- The CAA recognises that the airport operator may have to bear additional security costs due to factors beyond the airport operator's control. Hence the “+S” mechanism is included in the regulatory formula
- Additional security costs arising from a new security directive can in part be passed on to the airlines
- De minimis thresholds operate at each of the airports, and only 75% of the cost above the threshold can be passed on. The thresholds are:
 - Heathrow £14m
 - Gatwick £6m
 - Stansted £3m
- The CAA is proposing to maintain threshold levels and increase percentage pass through:
 - Heathrow £14m and 90% pass through
 - Gatwick £ 6m and 90% pass through
- The thresholds apply over the five years of the price control period. Additional costs can be cumulated over a number of years in order to reach the threshold. Recovery is lagged by a year hence any security costs from 2007/08 should be included in the Q5 forecast.
- The mechanism only applies to new directives within the quinquennium. The costs of dealing with existing directives should be included in the operating costs of the business. BAA will be negotiating with CAA the appropriate ongoing security costs for Q5 in the price control determination

- BAA Claim of the Security costs on Q4 :
 - return to 10 minute queue standard 95% of time
 - additional resilience in system

⇒ 5 minute queues 95% of time

- The additional security resources are:

Heathrow Airport

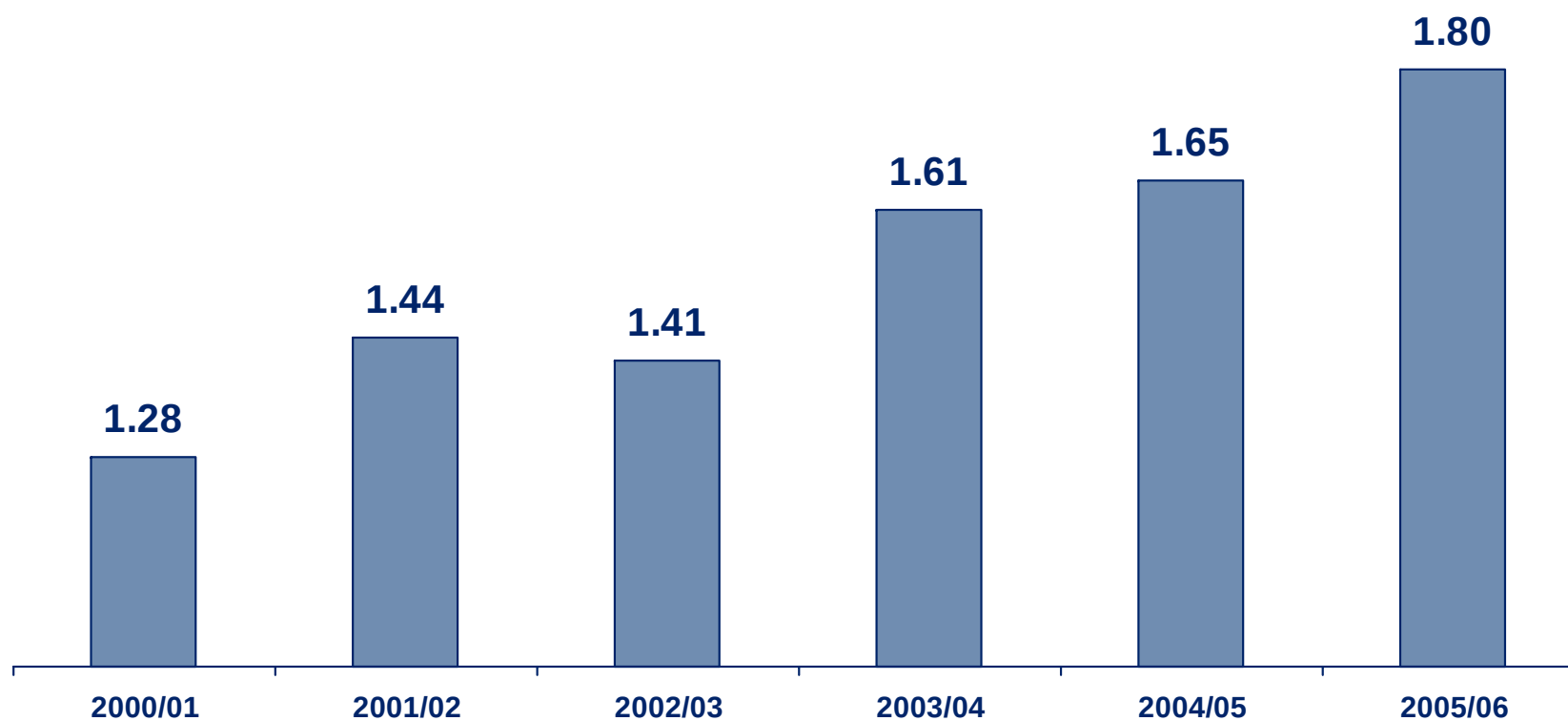
- 499 additional security guards
- 10 new search cones
- 14 new shoe X-rays

Gatwick Airport

- 168 additional security guards
- 7 new search cones

Security costs per passenger

£m, 2006/07 prices

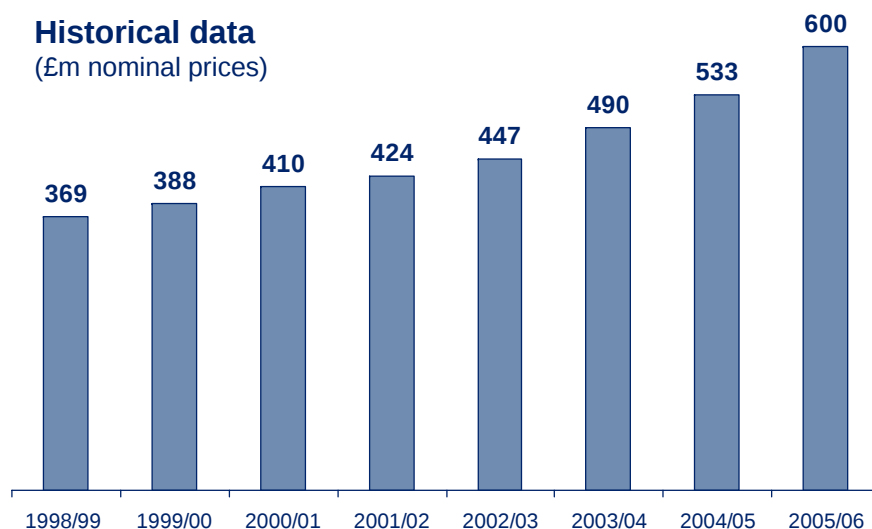


Opex- Heathrow historical & forecasted evolution

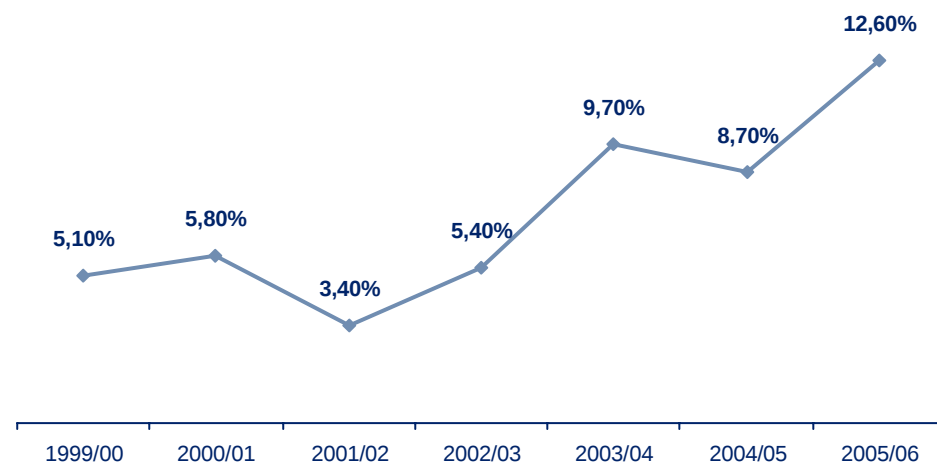
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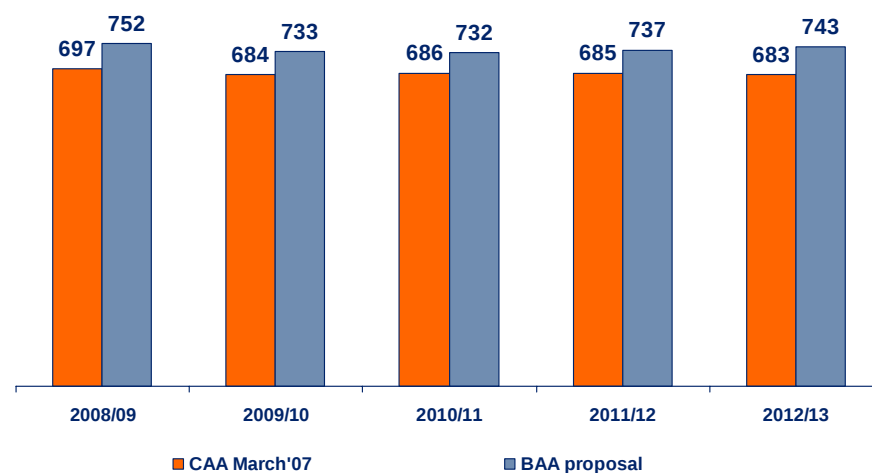
Historical data
(£m nominal prices)



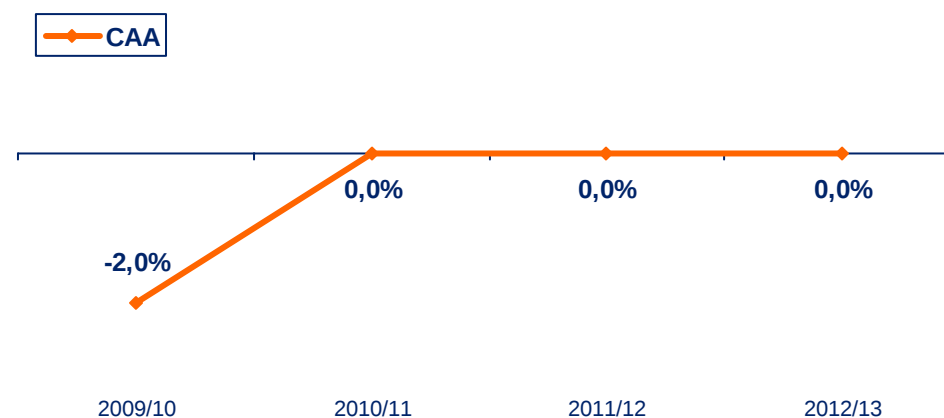
1999-2006 Historical annual growth (%)



Q5 Opex forecast real
(£m 2006/07 prices)



2008-2013 Forecasted annual growth (%)
(CAA figures do not include all security costs)



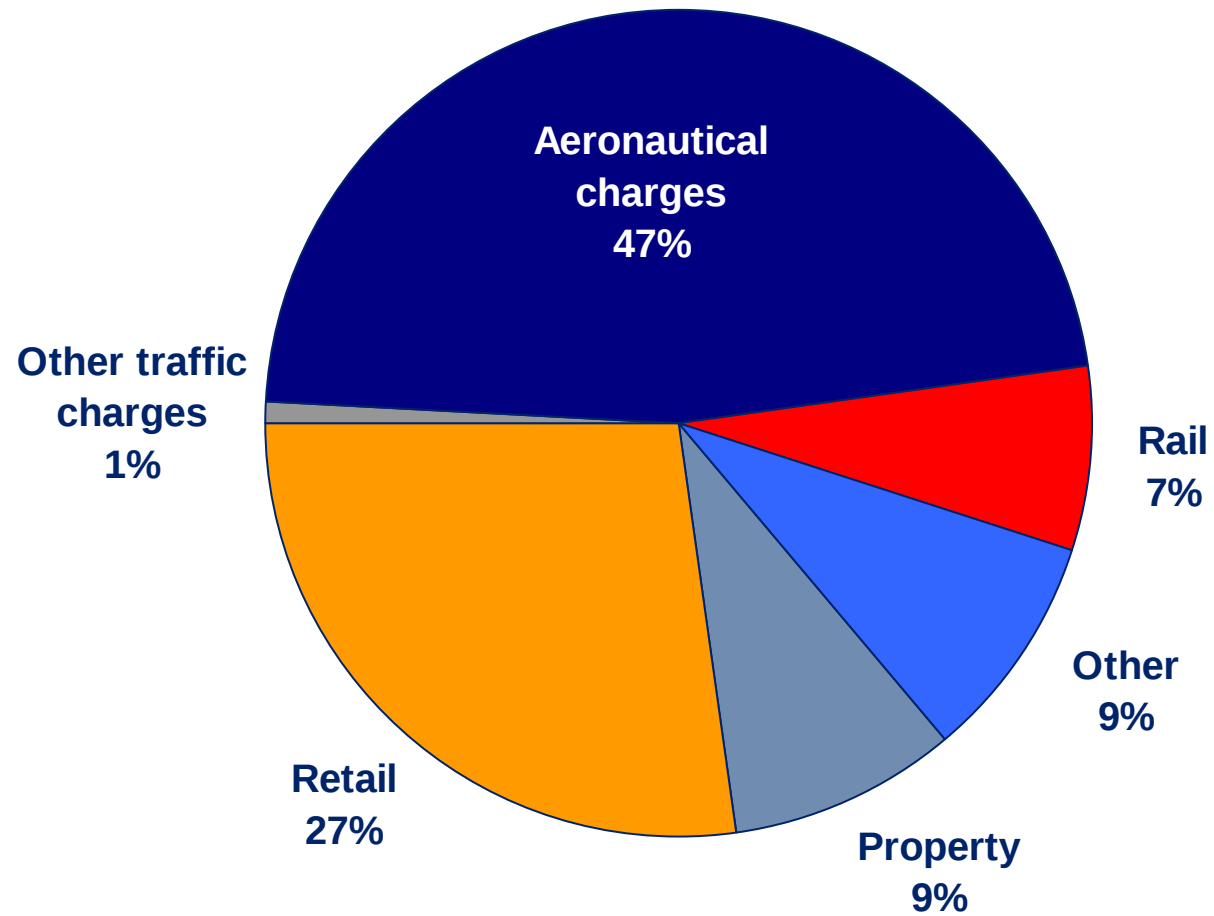
- In previous determinations the CAA has “smoothed” revenues :
 - Recognising that investment in airport assets is “lumpy” and that a **ten-year view** on large capital projects is required to provide a higher degree of certainty to incentivise investment
 - Seeking to avoid large, one-off, “step-ups” in airport charges that might be opposed by users
 - Advancement of revenue also incentivises BAA to invest
- Examples of smoothing include:
 - T5 revenue advancement in Q4. To mitigate against an increase in charges at the beginning of Q5 due to the opening of T5, the CAA advanced revenues to ensure a smoother price profile
 - ‘Clawback’ in Q4. Due to delays in T5 planning approvals, the capital programme envisaged for Q3 did not materialise. As a consequence the CAA ‘clawed back’ revenues advanced to BAA in Q3. The CAA stated at the time that this should be considered a ‘one-off’
- The pricing profile adjustment in effect works like a credit
 - When the revenues are advanced they are added to revenue and deducted from the RAB
 - When it is unwound in the next quinquennium, revenues are deducted from the revenues of that period and added back to the RAB.
 - In Q4 Heathrow has earned revenues brought forward from Q5 so the increase in charges due to T5 is smoothed. These revenues are deducted from the RAB.
 - In Q5 this adjustment is reversed and therefore there is a deduction of revenues, that is why the PPA is negative. Also the RAB is increased by the same amount.

Pricing Profile - Example

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Heathrow	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11	2011/12	2012/13
Regulated revenue requirement (reflecting advancement & claw back)	410,253	448,788	483,473	517,074	552,993	627,986	707,612	766,594	830,211	900,942
Other revenues	516,317	510,046	506,983	511,195	515,007	564,302	584,508	592,657	606,682	616,608
Operating expenditure	-414,008	-421,400	-435,350	-437,768	-444,749	-553,270	-573,146	-573,724	-595,034	-598,001
Depreciation	-152,267	-162,232	-163,826	-168,354	-179,481	-283,174	-299,271	-310,738	-337,756	-342,468
EBIT	360,296	375,201	391,280	422,148	443,770	355,843	419,703	474,790	504,104	577,080
Revenue claw back	-94,385	-94,385	-94,385	-94,385	-94,385					
Profiling adjustment	-135,651	-111,466	-81,099	-64,573	-43,578	169,090	124,623	87,709	65,775	-10,829
Average profiled RAB	4,273,038	4,796,620	5,418,701	6,053,495	6,624,316	7,030,889	7,290,642	7,534,049	7,632,902	7,584,305
Average basic RAB	4,339,598	4,986,965	5,705,612	6,413,396	7,038,488	7,384,289	7,496,771	7,633,668	7,655,573	7,578,790
Annex 5 annual returns including advancement excluding claw back	7.47%	7.47%	7.47%	7.47%	7.47%	7.47%	7.47%	7.47%	7.47%	7.47%
Annex 5 annual returns including advancement including claw back	5.26%	5.50%	5.72%	5.91%	6.04%	7.47%	7.47%	7.47%	7.47%	7.47%
Basic RAB annual returns including advancement excluding claw back	10.48%	9.42%	8.51%	8.05%	7.65%	4.82%	5.60%	6.22%	6.58%	7.61%
Basic RAB annual returns including advancement including claw back	8.30%	7.52%	6.86%	6.58%	6.30%	4.82%	5.60%	6.22%	6.58%	7.61%



Heathrow Regulatory accooounts 2005/06

Non-regulated charges

- Fixed electrical ground power supplied to aircraft
- CIP Lounges
- Utility revenue from supplying water and electricity recharged to users
- Check-in desks
- Fast-track passenger security processing
- Baggage systems
- Desks licences
- Staff car parking
- Staff ID cards
- Airside vehicle licences

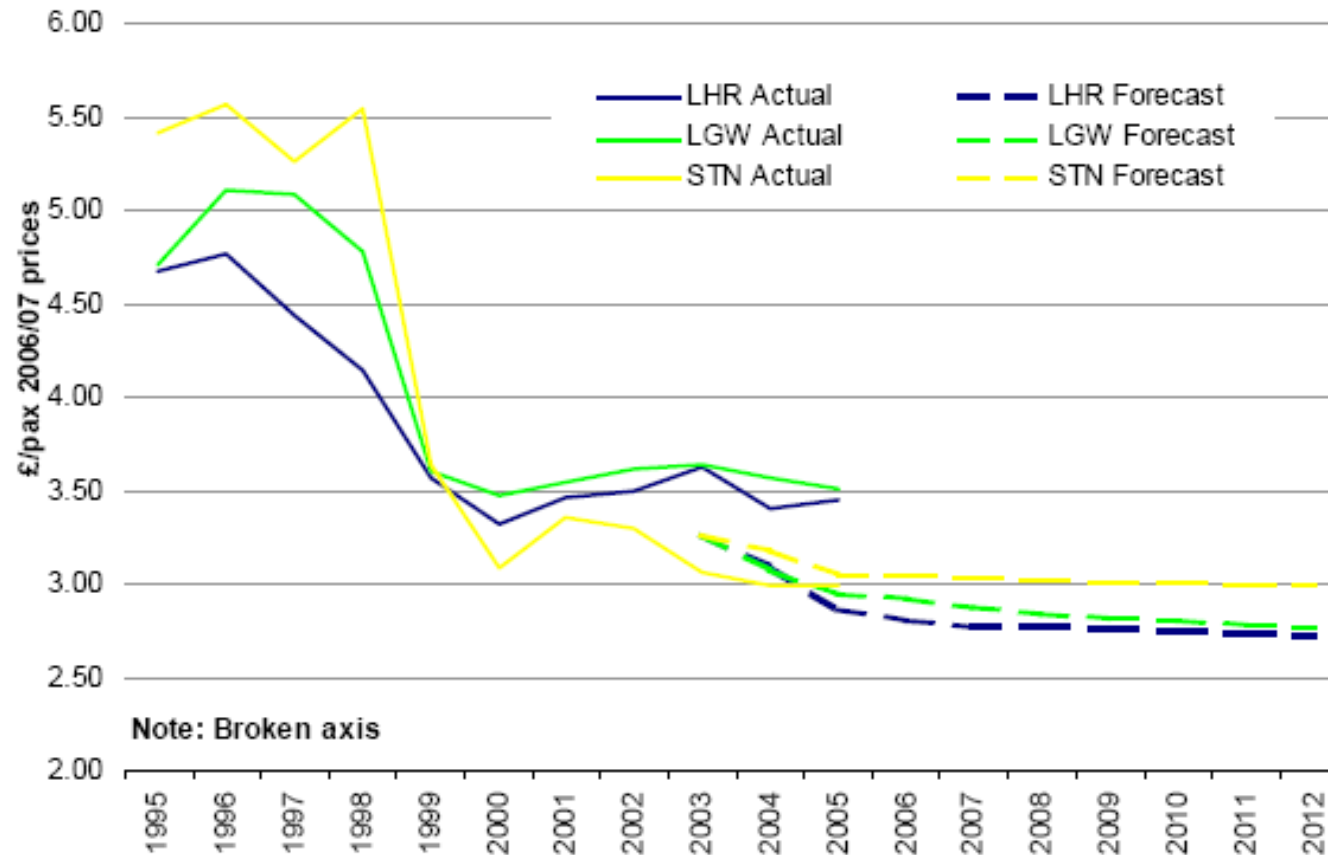
Commercial revenues

- Duty Free
- Bureau de change
- Catering
- Other retail
- Car park
- Property

Other Revenues

- Heathrow Express
- Intercompany Revenues

Retail revenue per passenger at BAA's London airports, actual versus forecast

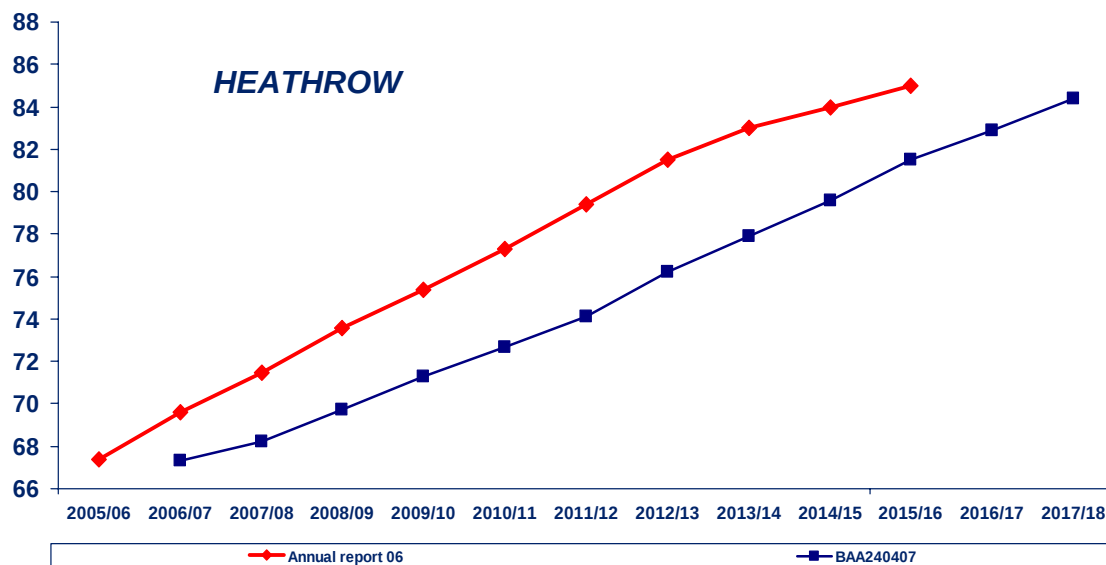


Source: BAA and CAA price control decision 2003

- Decline of Far East market
- Abolition of EU Duty & Tax Free (1999)
- Tobacco Ad ban
- EU enlargement
- Increased passenger security restrictions
- T5 opening
- UK Adopts the Euro

Traffic forecast

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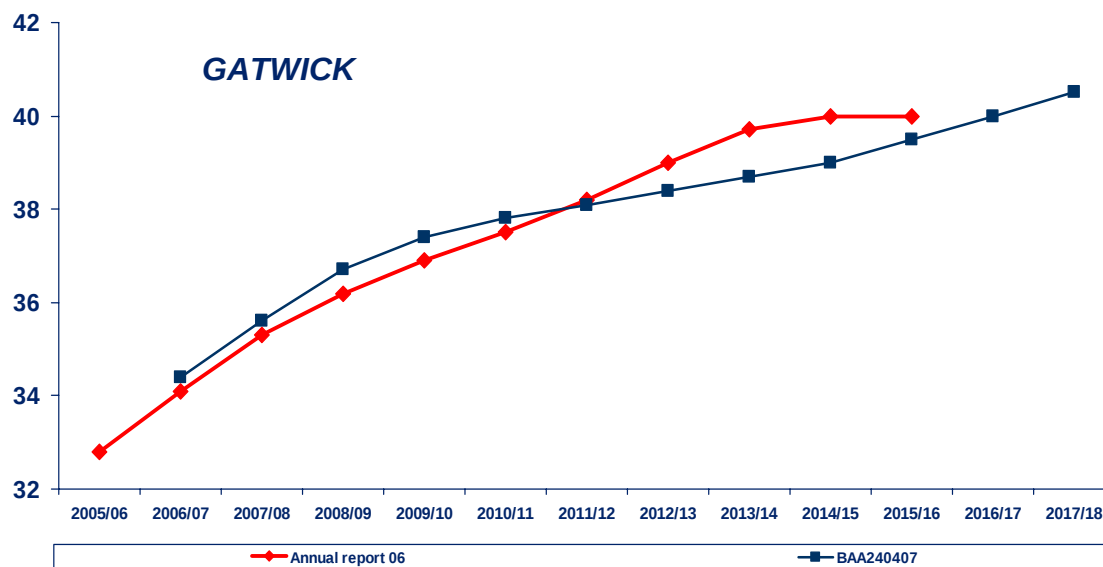


Forecasts are capacity - constrained, reflecting assessed volume of airline seats likely to be on offer per annum, and the proportion of those seats that will be taken up by pax.

Review of forecasts undertaken during winter 2006.

Heathrow

Lower airline capacity forecast (ie fewer seats per aircraft than previously assumed), and a more cautious view of demand - side prospects (including the effects of a doubling in UK Air Passenger Duty, and the assumed incorporation of aviation into the EU Emissions Trading System from 2011).



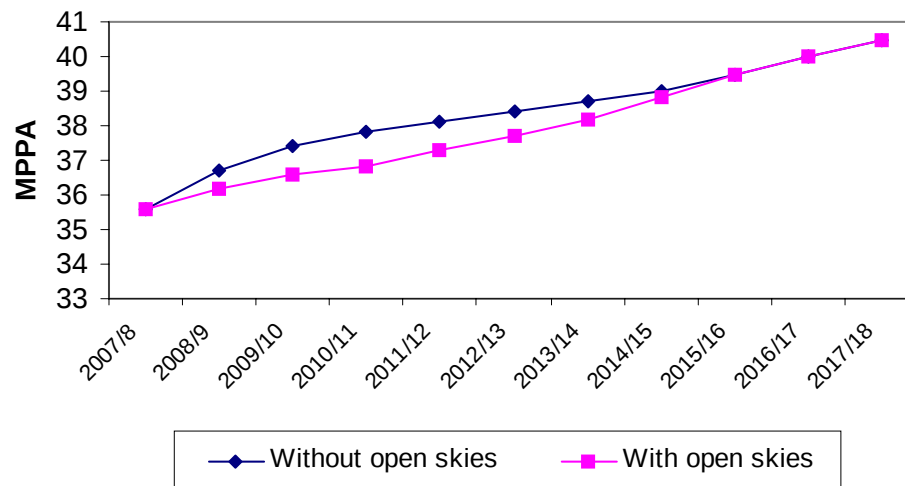
Gatwick

Forecast rephased to reflect airline plans (short term) and impact of APD / EU ETS (medium term).

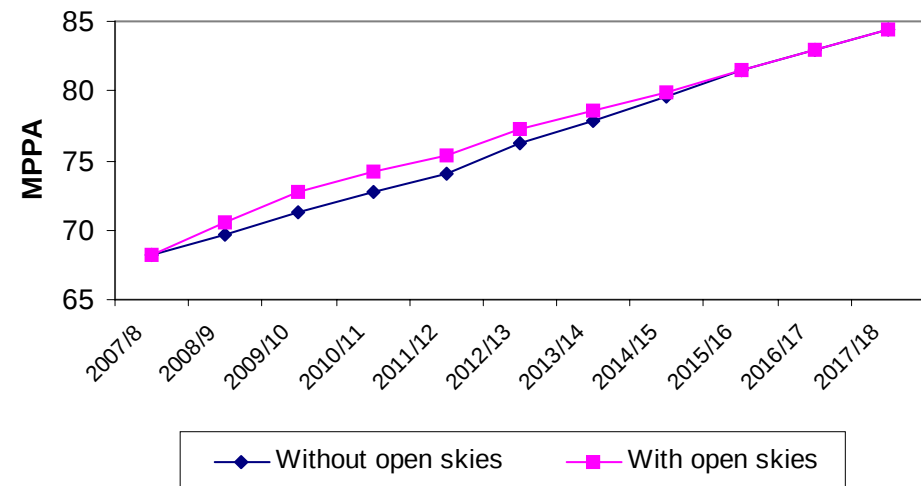
Lifting of previous UK/US bilateral constraints on air service provision between Heathrow and the US, replaced by new EU / US Open Skies deal, to be implemented at Heathrow in time for summer 2008.

Impact is currently being assessed using latest airline thinking, but previous assessment suggested small net gain to London system airports (+ 2.3m pax in total over the course of Q5 and Q6).

Gatwick Airport



Heathrow Airport



III. Q4 performance to date

Compared to CAA	Heathrow	Stansted	Gatwick	BAA 2003-08 (e)
Passengers				
Opex				
Capex				
Retail revenue				
Other revenue				
Overall return				

- **Passengers**

- lower at Heathrow and Gatwick: Iraq war & SARS
- higher at Stansted: Low cost carrier



- **Operating costs** have been higher than forecast, by 10%;

- enhanced security requirements;
- efficiency savings have been delayed
- costs of the change management programme fall mainly in Q4
- significant rise in utility costs
- increase in White Paper costs / noise etc



- Out-performance of **commercial revenues**

- Heathrow returning £.4.45 / pax vs £3.91 / pax in CAA forecast
- Increased revenue at Gatwick (despite lower passenger numbers)
- Lower yields at Stansted (albeit higher passenger numbers)
- Car parking yields particularly lower;



- Under-performance of **other revenues**
 - Property income falls due to APP transaction
- **Capital expenditure** is slightly above CAA forecasts by 4%;
 - T5 advancement, and earlier spend
 - Lower than forecast spending at Gatwick
 - Lower than forecast spending at Stansted
 - Foregone Q4 return on pre-spend



Q4 performance to date

ferrovial



Table A-11 BAA's Q4 performance (2003/04)

	Heathrow		Gatwick		Stansted	
	Outturn	Determ.	Outturn	Determ.	Outturn	Determ.
Passenger numbers	64,261	67,075	30,058	31,200	19,409	17,500
Revenues						
Airport charge revenue	414.9	435.9	129.8	135.3	54.3	91.3
Other revenue	563.2	548.4	188.9	180.0	93.5	98.1
Total revenues	978.1	984.3	318.7	315.3	147.8	189.4
Costs						
Opex	457.9	441.0	184.3	174.6	81.4	103.0
Depreciation	162.2	162.2	62.7	62.7	31.7	31.7
Total costs	620.1	603.2	247.0	237.4	113.1	134.7
Regulatory return	358.0	381.1	71.7	77.9	34.7	54.7
Weighted average RAB	4,848.6	4,705.8	1,262.0	1,239.8	868.5	876.0
Return on the RAB	7.38%	8.10%	5.68%	6.28%	3.99%	6.24%

Source: BAA regulatory accounts

Note: The table shows BAA's view of the outturn Stansted RAB. This reflects BAA's view of the outturn capital expenditure at Stansted, including its view of the capital expenditure associated with Stansted G2 that should be rolled into the Stansted RAB.

Table A-13 BAA's Q4 performance (2005/06)

	Heathrow		Gatwick		Stansted	
	Outturn	Determ.	Outturn	Determ.	Outturn	Determ.
Passenger numbers	67,421	69,900	32,845	36,000	22,237	20,300
Revenues						
Airport charge revenue	532.2	543.6	153.4	165.2	72.5	112.8
Other revenue	608.9	569.6	201.7	203.7	103.1	113.9
Total revenues	1,141.1	1,113.2	355.1	368.9	175.6	226.7
Costs						
Opex	554.1	490.7	223.4	195.8	100.5	122.6
Depreciation	184.7	184.7	63.8	63.8	36.4	36.4
Total costs	738.8	675.4	287.2	259.6	136.9	159.0
Regulatory return	402.3	437.8	67.9	109.3	38.7	67.7
Weighted average RAB	6,950.1	6,514.0	1,390.0	1,368.2	886.6	991.9
Return on the RAB	5.79%	6.72%	4.88%	7.99%	4.37%	6.82%

Source: BAA regulatory accounts

Note: The table shows BAA's view of the outturn Stansted RAB. This reflects BAA's view of the outturn capital expenditure at Stansted, including its view of the capital expenditure associated with Stansted G2 that should be rolled into the Stansted RAB.

Table A-12 BAA's Q4 performance (2004/05)

	Heathrow		Gatwick		Stansted	
	Outturn	Determ.	Outturn	Determ.	Outturn	Determ.
Passenger numbers	67,654	69,000	32,007	33,760	21,169	19,300
Revenues						
Airport charge revenue	479.0	491.7	143.5	150.9	62.4	104.2
Other revenue	589.2	558.4	198.7	191.6	101.7	108.4
Total revenues	1,068.2	1,050.1	342.2	342.5	164.1	212.6
Costs						
Opex	496.8	462.8	193.7	183.0	90.5	113.7
Depreciation	178.2	178.2	65.2	65.3	31.8	31.8
Total costs	675.0	641.0	258.9	248.3	122.3	145.6
Regulatory return	393.2	409.1	83.3	94.2	41.8	67.0
Weighted average RAB	5,857.9	5,552.0	1,335.6	1,295.9	868.0	924.1
Return on the RAB	6.71%	7.37%	6.23%	7.27%	4.81%	7.25%

Source: BAA regulatory accounts

Note: The table shows BAA's view of the outturn Stansted RAB. This reflects BAA's view of the outturn capital expenditure at Stansted, including its view of the capital expenditure associated with Stansted G2 that should be rolled into the Stansted RAB.

IV. CAA's Q5 March 07 Proposal

	Allowed return	Price
Heathrow:	5.9% / 6.2%	RPI +4% / +8%
Gatwick:	6.3% / 6.7%	RPI -2% / +2%
Stansted	Extend Q4 formula 1 year and proposed De-regulation	

- All Q4 capex to be allowed into RAB
- All Q5 capex to be allowed into RAB
- Further constructive engagement required
- CAA has forecast greater opex savings than BAA (around 1% a year)
- CAA has forecast greater commercial revenues than BAA (just under 1% a year)
- APP transaction approved
- CAA is proposing to de-regulate Stansted
- CAA Initial proposal for Q5 is at <http://www.caa.co.uk/default.aspx?categoryid=5&pagetype=90&pageid=7162>
- CAA March 07 proposal is at http://www.caa.co.uk/docs/5/ergdocs/ccreference_march07.pdf

V. White paper

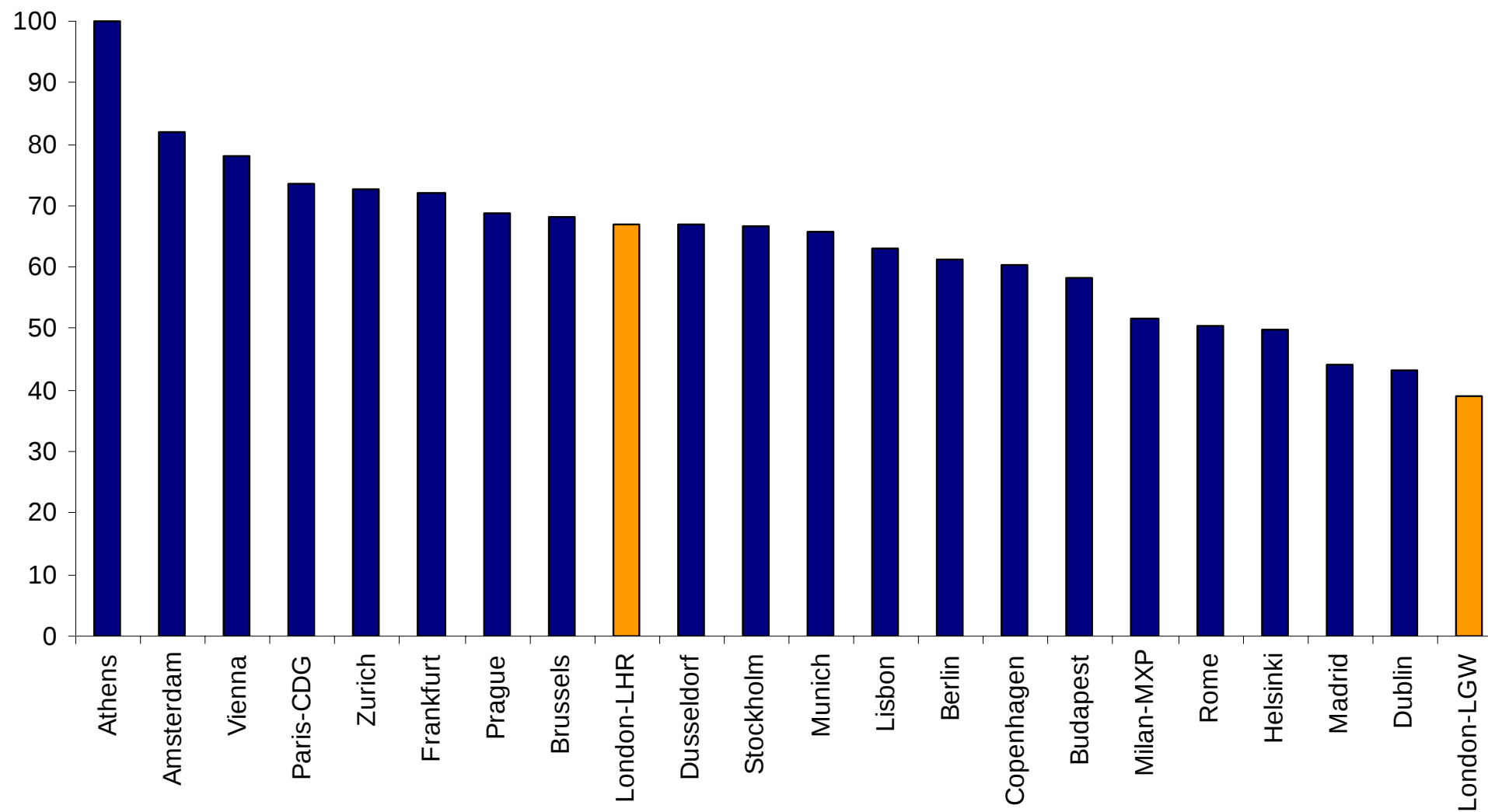
- **White Paper sets out government policy for airport development**
- **2003 White Paper called for 2 runways in the South East**
 - **The first at Stansted as soon as possible (currently scheduled for 2015)**
 - **The second at Heathrow (subject to environmental constraints being overcome)**
 - **And if not Heathrow, at Gatwick (but not before 2019)**
- **December 2006 “progress report” on White Paper**
- **Government confirmed support for airport development in the South East**
- **Government also signalled a consultation on the de-regulation of Stansted**
- **Government support is key for BAA’s plans to develop Stansted and Heathrow**

VI. CC Market investigation (OFT referral)

- OFT referred the 7 UK BAA airports, WDF and Lynton to the CC in March 07
- Identifies features of BAA's airports that require investigation
 - Common ownership by BAA
 - Lack of capacity
 - Nature of regulation
- CC has up to March 09 to take a decision
- CC has the power to break up BAA

VII. Airport charges in Europe

TRL Index 2006



- 2007 will be an exceptionally important year for BAA
- New owners
- ... new price control announced in Feb-March 08....
- ... future of company at stake
-refinancing to be completed
- But
- Government committed to new capacity in the South East
- Significant price rises at Heathrow seem likely in Q5
- Deregulation of Stansted presents new opportunities and risks ...
- ... all roads head to the Competition Commission

**Thank you for
your patience**