S&P Global Ratings

RatingsDirect®

Bulletin:

Higher Passenger Volumes Improved Heathrow's 2022 Performance But Regulatory Decisions Cloud The Horizon

February 23, 2023

This report does not constitute a rating action.

PRIMARY CONTACT

Vinicius Ferreira
London
44-20-7176-0526
vinicius.ferreira
@spglobal.com

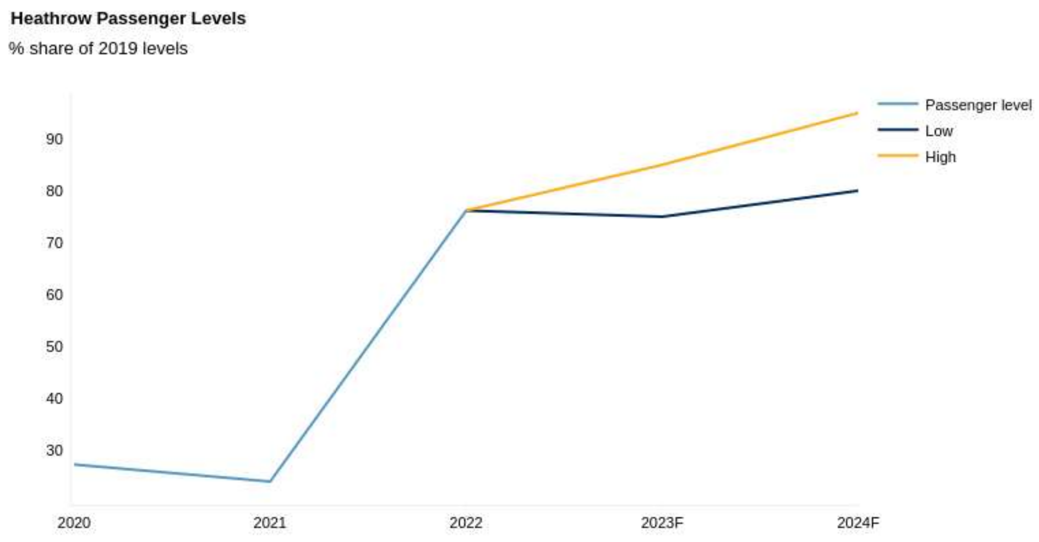
SECONDARY CONTACT

Juliana C Gallo
London
44-20-7176-3612
juliana.gallo
@spglobal.com

RESEARCH ASSISTANT

Piers Robinson
London
44-2071766748
Piers.Robinson
@spglobal.com

LONDON (S&P Global Ratings) Feb. 23, 2023--S&P Global Ratings said today that higher passenger volumes led Heathrow Funding Ltd. (Heathrow; Class A debt rated BBB+/Watch Neg and Class B debt rated BBB-/Watch Neg), the U.K.'s largest airport, to deliver better 2022 results than we previously expected. However, it is still uncertain if the company will be able to achieve and sustain credit metrics commensurate with the current ratings over the next 24 months--notably S&P Global Ratings-adjusted funds from operations (FFO) to senior debt of 7% for Class A and FFO to total debt of 5% for Class B. The regulator, Civil Aviation Authority (CAA)'s final decisions for Heathrow's H7 regulatory period (2022-2026) are still pending, including the charge cap. In our view, the recent deteriorating macroeconomic environment and Heathrow's better than expected traffic performance may change some of CAA's assumptions when it releases the final decisions, most likely in March 2023 (of which were published in the regulator's final proposal in June 2022). The extent of these considerations and the effects are still unknown. Hence, a lower than forecast tariff without any mitigating action or compensation may compromise the recovery of Heathrow's credit metrics and our ratings.



Source: S&P Global Ratings.

After travel restrictions were lifted in 2022, pent-up demand boosted the number of travellers in the airport and reached 61.6 million--equal to 76.2% of 2019 levels and higher than our expectation of 65% of 2019 levels. We expect passenger volumes will grow in 2023, mainly on the back of no current additional global travel restrictions. However, the growth path should be slower, as passengers' disposable income is shrinking, ticket prices are higher, and the recovery in business travel is lagging--especially when compared to that of leisure travel.

The company's reported revenues reached £2.9 billion in 2022 (£1.2 billion in 2021). This was driven by a higher number of passengers at terminals that pay an average tariff of £30.19 and commercial activities as new stores opened and the average expenditure per passenger reached £9.16. Throughout the year, the airport reopened all terminals to the public, resulting in higher operating expenses. Thanks to its fixed contracts and hedge policies in place, Heathrow was able to keep utility expenses under control during the year, with the main increase relating to higher staff salaries. Despite this, the company was still able to post a reported EBITDA of £ 1.7 billion (£384 million in 2021) and EBITDA margin of 57.8% (31.6% in 2021), close to pre-pandemic levels.

On the other hand, Heathrow's indebtedness increased in 2022 and reached a reported net debt of £14.6 billion (£13.3 billion in 2021), mostly because of the higher inflation adjustment on its total debt as RPI reached 13.4%. Even taking this into consideration and pending our final analytical adjustments, we anticipate FFO to senior debt should be above 6.0% and FFO to total debt will be higher than 5.0%. We will monitor the CAA's announcements to determine if Heathrow will be able to continue improving its earnings and cash flow.

Related Research

- Industry Top Trends 2023: Transportation Infrastructure, Jan. 23, 2023
- Europe's Remarkable Air Passenger Traffic Recovery Faces A Trickier 2023, Nov. 21, 2022
- Heathrow Funding Ltd. Class A And Class B Ratings Remain On CreditWatch Negative After Regulator's Final Proposals, July 7, 2022