Heathrow Funding Limited

Annual report and financial statements for the year ended 31 December 2022

Company registration number: 99529 (Jersey)

Heathrow Funding Limited

Contents

Heathrow Funding Limited

Officers and professional advisers

Directors
Yuanyuan Ding
Javier Echave
Nicholas Golding– Resigned 31 March 2022
Martin Bailey – Appointed 1 April 2022
Lisa Aune– Resigned 6 June 2022

Company secretary
Apex Group Secretaries Limited (formerly Sanne Secretaries Limited)

Registered office
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Independent auditors
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Heathrow Funding Limited

Directors' report

The directors present their annual report and the audited financial statements for Heathrow Funding Limited (the 'Company') for the year ended 31 December 2022.

Principal activities

The Company's primary purpose is to raise funding through the issuance of bonds and to provide funding to Heathrow (SP) Limited and its subsidiaries (together the 'SP Group'). FX and interest rate risks are managed by the use of external derivatives. The proceeds raised are distributed to Heathrow Airport Limited ('Heathrow'), a fellow subsidiary of Heathrow (SP) Limited, under the terms of Borrower Loan Agreements ('BLAs'). The advances under BLAs are secured and are issued on substantially the same terms as the bonds issued by the Company, taking into consideration any related hedging instruments.

The Company is a direct subsidiary of Heathrow (SP) Limited and forms part of the Heathrow Airport Holdings Limited group (the 'HAHL Group'). The Company is incorporated in Jersey but is resident in the United Kingdom for taxation purposes.

Cross-currency swaps, interest rate swaps and index-linked swaps are entered into by the Company to hedge the SP Group's and the wider HAHL Group's exposures. Interest rate and index-linked derivatives are mainly passed through to Heathrow as back-to-back derivatives, or otherwise incorporated into related BLAs. The Company's cross-currency swaps are packaged with their associated non-Sterling debt and passed through to Heathrow under the BLAs.

For the year ended 31 December 2022, net finance expense was £294 million (2021: Net finance expense of £177 million). The movement was predominantly driven by the fair value loss of £294 million (2021: £132 million loss) on financial instruments, specifically the Company's cross-currency swap portfolio resulting from increasing interest rates. Other net finance expense movements included interest receivable from group undertakings increased to £1,424 million (2021: £813 million), interest payable on external borrowings increased to £793 million (2021: £642 million) and net interest on derivative financial instruments increased to £634 million (2021: £208 million). The increase in net interest on derivative financial instruments was in part due to accretion on index-linked swaps, which was affected by the increase in inflation of 14.0% during 2022 (2021: 7.1%) as the company pays RPI on its inflation-linked swaps.

The mark-to-market value of cross-currency swaps was negatively impacted during the period mainly due to higher CAD, EUR and CHF overnight index rates, together with the impact of OIS discounting.

The settlement of £534 million (2021: £69 million) of accretion on index-linked swaps and the appreciation of Sterling against the hedged currencies, impacted the carrying value of all derivatives which changed from a net asset of £71 million at 31 December 2022 to a net liability of £12 million at 31 December 2022 as shown in Note 6.

Heathrow Funding Limited continues to focus on maintaining a strong liquidity position and optimising its long-term cost of debt as well as ensuring duration, diversification and resilience in its debt financing.

In the year ended 31 December 2022, the company raised £196 million of new debt.

Class A financing activities included:

- The scheduled repayment of a £180 million RPI-linked bond in April.
- A return to the CHF market in May, raising £136 million equivalent maturing in 2027.
- The scheduled repayment of a €600 million public bond in May.
- In August, we priced £60 million of new debt in the private placement market with a maturity of 2047.

No significant changes to the activities of the Company are expected in the foreseeable future.

Heathrow Funding Limited

Directors' report *continued*

Results and dividends
The loss after taxation for the financial year amounted to £294 million (2021: £177 million). The Company's net liabilities as at 31 December 2022 were £284 million (2021: net assets £10 million). No ordinary dividends were proposed or paid during the year (2021: £nil). The statutory results for the year are set out on page 19.

Directors
The directors who served during the year and since the year end, are as follows:

Yuanyuan Ding
Javier Echave
Nicholas Golding – Resigned 31 March 2022
Martin Bailey – Appointed 1 April 2022
Lisa Aune – Resigned 6 June 2022

Employment policies
The Company has no direct employees (2021: none).

Key performance indicators
Given the straightforward nature of the business, the Company's directors are of the opinion that analysis using key performance indicators is not necessary for an understanding of the financial performance and financial position of the Company.

Going Concern
The financial information presented within these financial statements has been prepared on a going concern basis. More detail can be found in the going concern statement on page 23.

Internal controls and risk management
Internal controls and risk management are key elements of the Company's corporate operations. The functions of the Heathrow Airport Holdings Limited Board (the 'HAHL Board') and its committees are applied equally to all subsidiaries of the HAHL Group, including the Company, further information on the governance structure and composition of the HAHL Board and its committees can be found in the HAHL Group annual report and financial statements at www.heathrow.com/company/investor-centre.

Internal controls
The directors are responsible for the system of internal controls designed to mitigate the risks faced by the Company and for reviewing the effectiveness of the system. This is implemented by applying the HAHL Group internal control procedures, supported by a Code of Professional Conduct Policy, appropriate segregation of duties controls, organisational design and documented procedures. These internal controls and processes are designed to manage rather than eliminate the risk of failure to achieve business objectives and can only provide reasonable, and not absolute, assurance against material misstatements or loss.

The key features of the HAHL Group's internal control and risk management systems in relation to the financial reporting process include:

- a company-wide comprehensive system of financial reporting and financial planning and analysis;
- documented procedures and policies;
- defined and documented levels of delegated financial authority;
- an organisational structure with clearly defined and delegated authority thresholds and segregation of duties;
- a formal risk management process that includes the identification of financial risks;
- detailed reviews by the Executive Committee and the Board of monthly management accounts measuring actual performance against both budgets and forecasts on key metrics;
- Audit Committee review of press releases and key interim and annual financial statements, before submission to the Board, scrutinising amongst other items;
  - compliance with accounting, legal, regulatory and lending requirements;
  - critical accounting policies and the going concern assumption;
  - significant areas of judgement and estimates;
  - key financial statement risk areas;
- independent review of controls by the Internal Audit function, reporting to the Audit Committee; and
- a confidential whistleblowing process.

Directors' report *continued*

Risk management

The Heathrow Risk and Assurance Management framework is an enterprise risk management system that is embedded Group-wide with the principal aim of providing oversight and governance of the key risks that Heathrow faces, and to monitor current, upcoming and emerging risks.

The framework provides guidance on how risks should be identified, mitigated, reviewed and reported within Heathrow. During 2022, we have continued to improve our risk processes, building on the current risk-management structure, to enhance the data quality, completeness of risk information and control measurement in addition to improving the overall reporting integrity.

The HAHL Board has overall responsibility for the framework and for reviewing the effectiveness of the risk-response system. There are two HAHL Board sub-committees which are responsible for risk: the Audit Committee, which reviews the effectiveness of systems for internal financial and operational control, and the Sustainability and Operational Risk Committee, which reviews the effectiveness of operational reporting and performs an oversight review of the performance against sustainability goals and operational targets.

To achieve a balanced view of our risk landscape in line with wider company objectives, all our risks are evaluated against defined risk appetite levels, which are captured in a formal risk appetite statement which is consolidated and reviewed on an annual basis.

The most significant risks are collated and reported to the Risk and Assurance Committee, a sub-committee of the Executive Committee, which meets every six weeks. The risks are then reviewed by the Executive Committee before being submitted to the Audit Committee and Sustainability and Operational Risk Committee for independent review and challenge. The final Heathrow Risk Outlook Report is then reviewed and approved by the HAHL Board on a quarterly basis.

Principal risks have been identified at an Executive level ensuring a comprehensive top-down approach to risk identification and management. A Principal Risk is a risk that has been identified by the HAHL Board, its formal committees, the Executive Committee, or the Risk and Assurance Committee, as an important risk that fundamentally affects the business's ability to deliver on its overarching objectives. A Principal Risk is assessed according to the likelihood, consequence and velocity by which the risk may impact Heathrow.

Principal risks

The risks outlined below are the principal strategic, corporate and operational risks identified. This is a current point-in-time assessment of the risk profile that the HAHL Group faces, as the risk environment evolves these risks are being constantly reviewed and updated.

A Safe and Secure Operating Environment

Principal risk

An airport as large and complex as Heathrow has a multitude of fire, safety, health and wellbeing risks and with the pace and rate of our growth as we build back capacity these risks increase. Nationally, COVID-19 has resulted in a worsening of physical and mental health and external pressures including the war in Ukraine and cost of living crisis are adding to people's anxiety.

If we do not set and strive for the highest standards of fire, safety, health and wellbeing, we risk causing harm to our colleagues and stakeholders, compromising our service to passengers, and damaging our reputation and ultimately our business performance.

We therefore value, above all else, the health and safety of colleagues, passengers and anyone else affected by the airport's activities. Our focus on health and safety is not just the right thing to do, it is the foundation of an efficient operation, a secure airport and a sustainable business.

The UK security threat level is substantial, meaning an attack is likely. We are responsible for ensuring that our assets, infrastructure, human and electronic systems and processes meet requirements to protect aviation security, deliver high security standards and build confidence with regulators, airlines and passengers.

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Directors' report *continued*

Principal risks *continued*

A Safe and Secure Operating Environment *continued*

Risk mitigation strategy

Our risk mitigation strategy is built from our fire, safety, health and wellbeing framework of safe and healthy 'place', 'work', 'team' and 'decisions'.

Place – We ensure our physical environment and assets are designed, built, used, and maintained so that they don't cause harm. Our change control processes are designed to ensure that new equipment, technology, and processes are introduced safely.

Work – Our, fire, health and safety management systems are designed to ensure a planned and controlled way of working. We set Fire Health and Safety ('FHS') standards for the airport community and influence industry standards working with UK and international regulators and industry bodies. Our risk assessment processes adopt the hierarchy of controls and we set FHS standards for the airport community. Governance and assurance processes are used to ensure that controls around health-and-safety risks remain effective, and continuous improvement is encouraged.

Team – Consultation, engagement and collaboration are key to a safe and healthy team. We work closely with our Trade Union partners on health and safety matters and engage colleague views through our engagement surveys. Our leaders, managers and colleagues receive the training they need to understand and manage risks associated with their roles. We collaborate across Team Heathrow through a range of mechanisms, including the Team Heathrow Safety Council and Network, to drive standards and performance. We held our first Heathrow Airport Safety Summit with Team Heathrow in June 2022 and started to measure safety culture across organisations operating at the airport.

Decisions – In the last 12 months our focus has been on 'healthy minds' to ensure safe and healthy decision making. Our extensive range of health and wellbeing products and services has been further promoted this year resulting in increased utilisation, supplemented by the provision of mental fitness training for line managers and support for financial wellbeing. Over 60% of line managers within our Security function have received mental fitness training, providing practical tools so that line managers prioritise their own mental fitness and develop confidence in holding wellbeing conversations and signposting colleagues to appropriate support. Support for financial wellbeing includes practical support and access to one-to-one financial coaching.

We also have a confidential reporting line through which concerns of wrongdoing at work can be reported (Safecall).

We work with law enforcement and government agencies to ensure security procedures are appropriate and mitigate evolving threats. Procedures are subject to review through the internal controls mechanism and via independent scrutiny from the Civil Aviation Authority ('CAA') and other domestic/international agencies.

Information Security

Principal risk

Information security, which refers primarily to our systems and information and the data contained in them, continues to be a risk for Heathrow. Malicious cyber-attack is a continued risk given the size and breadth of our network and operating environment. Attacks continue to be more sophisticated, especially around phishing and ransomware which are now a persistent challenge for all industries. In addition, new ways of working following the COVID-19 crisis have also resulted in an increased risk profile.

Risk mitigation strategy

Heathrow is a Critical National Infrastructure ('CNI') and therefore complies with The CAA "Cyber Security Oversight Process for Aviation" (CAP 1753) based on the National Cyber Security Centre's "Cyber Assessment Framework" and in turn is broadly aligned to the NIST Cyber Security Framework. The Regulator (CAA/DfT) requires that Heathrow achieve compliance with CAP1753, through the CAA ASSURE audit process.

Heathrow has top-down support for Cyber Security. It is an active topic at the Executive Committee and briefings are provided as required or requested. Regular reporting is also performed through reports at Executive/Board/Non-Executive risk committees. Cyber risk assessment is performed at a system, supplier, and departmental level, and rolled up into overall corporate risk management processes. Mandatory cyber and data privacy training is rolled out to colleagues annually. Monthly phishing awareness campaigns are run and tracked. Execution of Business Continuity Plans is managed through the Heathrow

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Directors' report *continued*

Principal risks *continued*

Information Security *continued*

Resilience "Command and Control" process. We work with Strategic Security in partnership with governing bodies as part of our CNI status.

Regulation Requirements

Principal risk

We are subject to economic regulatory review. Changes to economic regulation could materially impact the performance of the business. Failure to comply with laws and regulations could result in loss of licence, penalties, claims and litigation, reputational damage and loss of stakeholder confidence.

Risk mitigation strategy

The risk of an adverse outcome from economic regulatory reviews is mitigated as far as possible by a dedicated regulatory team. This team ensures full compliance with regulatory requirements, establishes a sound relationship with the regulator and advises the Executive Committee and HAHL Board on regulatory matters. Beyond engagement with the regulator, these risks are somewhat further mitigated by our right of appeal to the Competition and Markets Authority. In addition, we engage closely with internal and external legal advisors to ensure that relevant and appropriate advice is received and that our response to reviews and our actions to ensure compliance with regulatory requirements reflect such advice.

Legal status of Airports National Policy Statement ('ANPS')

Principal risk

In June 2018 Parliament approved the Airports National Policy Statement ('ANPS') which sets out the policy framework for expansion at Heathrow Airport and is the primary basis for decision making on any development consent application for a new north-west runway. Heathrow was making considerable progress towards developing its Development Consent Order ('DCO') application to deliver a sustainable, affordable and financeable expanded Heathrow, including holding multiple consultations to seek feedback on its proposals. However, on 27 February 2020, the Court of Appeal concluded that the UK Government was required but had failed to take into account the Paris Climate Agreement when preparing the ANPS. The Court declared that the ANPS had no legal effect unless and until the UK Government carried out a review of the policy. Heathrow appealed against this decision and in December 2020, the Supreme Court unanimously held that the UK Government had acted lawfully when making the ANPS, overturning the Court of Appeal's decision. The judgment confirmed that the UK Government had properly exercised its discretion and had taken into account the Paris Climate agreement by having regard to the Climate Change Act 2008 in the ANPS. On 6 September 2021, the Secretary of State for Transport decided that it was not appropriate to review the ANPS at this time. Further confirmation of the status of the ANPS has been made through the May 2022 publication of "Flightpath to the Future" and the July 2022 publication of "Jet Zero Strategy". While work to expand Heathrow during COVID-19 was paused, the post pandemic period has shown the demand from airlines to fly from Heathrow, as well as how critical Heathrow is for the UK's trade routes. The Government's ANPS continues to provide policy support for Heathrow's plans for a third runway and the related infrastructure required to support an expanded airport and we are reviewing our options.

Risk mitigation strategy

In 2020 we appealed the Court of Appeal's judgment on legal grounds with a view to reinstating the ANPS. Having won the appeal and restored the ANPS, we have positively reiterated the case for expanding Heathrow in line with Government policy and we are continuing to engage with the Government, the CAA and other stakeholders on the next steps to progress our plans.

Heathrow remains committed to a long-term sustainable expansion. When demand returns to pre COVID levels, meeting that demand as the UK's hub airport will be essential to a country with global and levelling up ambitions.

Reduction in global demand and revenues

Principal risk

Operational ecosystem challenges impacting capacity rebuilding and revenue growth.

COVID-19 has led to an unprecedented reduction in passenger volumes and revenues, which the industry was forced to respond to with workforce reductions and temporary closure of two terminals to weather the pandemic. The lack of targeted industry support and unstable travel policies (quarantines, testing requirements) by the government exacerbated the industry's ability to plan for recovery. Brexit has impacted on worker availability, particularly in relation to ground handling staff.

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Directors' report *continued*

Principal risks *continued*

Reduction in global demand and revenues *continued*

Continued policy inconsistency on VAT Free shopping provides significant revenue uncertainty and lack of competitive parity with EU airports. The Next Generation Security Project is expected to have a negative impact on aviation capacity and retail revenue from 2023 onwards.

Significant potential revenue impacts are expected relating to workforce challenges requiring capacity restrictions and removal of VAT Free shopping.

Revenue growth may be inhibited by the lack of certainty over consumer demand recovery in 2023-2024, driven by high inflation, a slowdown in economic growth, impact of a recession and pressure on consumer spending. A limited capacity for growth dependent on slot trading combined with the highest aviation taxes in Europe ('APD') continue to put pressure on airports and hub airlines.

Risk mitigation strategy

Aviation

Our strategic response to protect revenues and drive passenger volumes has been:

1. Slot Strategy in place to secure desired slot recommendation for winter 22, summer 23 and for the future, with advocacy plan also in place to influence Department for Transport, Airport Council International ('ACI') (World and Europe), International Air Transport Association ('IATA') and other stakeholders to align to Heathrow's position.
2. 2022 – 2026 Network Strategy in place to target new routes, grow market share and competition in key markets and protect weaker performing routes.
3. Senior engagement and account plans in place with key airlines to rebuild relations and accelerate collaboration, post COVID-19.
4. 2022 – 2026 Aviation Strategy in place to optimise revenues generated from Aviation with the goal of delivering sustainable growth, increased hub connectivity both globally and domestically and diversifying revenue.
5. Worked with Airport Coordination Limited ('ACL') (and Ops Planning on pre-season schedule optimisation to maximise capacity where resources are limited.
6. Industry monitoring via daily updates from CAPA (market intelligence for the aviation and travel industry), media cuts and other industry events, as well as attendance at Routes (network) and IATA (slots and cargo) conferences.
7. Close alignment internally with Space, Retail and Property teams to optimise commercial opportunities while maintaining alignment with Security Project.

Retail

Key measures implemented to contain the impact on retail income include:

1. Close monitoring and balance of assessed debt and contractual fixed income guarantees to maximise overall retail revenue.
2. Targeted scouting of the market to identify potential new entrants with the ability to enter into a commercial deal with minimal level of disruption and delays (e.g., lending locations to businesses that could make immediate use of the structure 'as is').
3. Continued dialogue with officials in the Treasury (HMT) around the impact and pitching an alternative solution for the reintroduction of VAT free shopping for departing passengers and the opportunity to introduce duty free shopping for arriving passengers.

Liquidity and ability to access finance

Principal risk

We need to continue to be able to access finance to fund our current operations.

Risk mitigation strategy

We produce long-term forecasts which include consideration of significant downside risk to enable our management to conclude that covenant terms are likely to be met, and that we have the ability to access additional future finance as required. We have invested in a suitably skilled Business Planning and Treasury team who have robust procedures in place to ensure that the best quality investment decisions are made, and that investments can be appropriately financed.

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Directors' report *continued*

Principal risks *continued*

Resilience of Team Heathrow

Principal risk

The COVID-19 pandemic has had a significant impact on the aviation industry, as well as on the wider eco-system of key customers and stakeholders that support the supply of services and facilities to passengers and airlines. There is a risk that the level of passengers and Air Traffic Movement growth exposes the gaps in operational resilience across the wider Team Heathrow, impacting on our collective ability to provide the safety, resilience, service levels and passenger experience our passengers expect.

Following the removal of government restrictions, both in the UK and globally, Heathrow and the wider aviation sector has experienced a rapid increase in passenger demand. Airports, including Heathrow, and their partners and suppliers, have experienced significant challenges in ensuring sufficient resources are available to support rapidly increasing demand, placing particular challenges on key parts of the passenger journey at peak times – security, airline ground-handling and immigration.

Risk mitigation strategy

We continue to monitor and build on our operational insight and data to ensure we have capacity and resource ready ahead of demand with planned responses. We have developed a build back capacity programme led by our Chief Solutions Officer to specifically address pain points and risk areas around resilience. This programme reviews resourcing capacity across Heathrow's ecosystem and measures short and medium-term forecasting to enable capacity planning. We work closely with our stakeholders and airlines undertaking regular reviews via the capacity sub-group. This includes seasonal peaks and flying schedules.

We continue to work closely with our airline customers, retailers and wider stakeholders. We monitor the financial health of our key Team Heathrow partners to ensure we have early warning of any concerns so that where possible we can work together to find a solution or provide alternative facilities where this proves to be the more viable option. Regular engagement takes place at both management and operative level across key members of Team Heathrow to discuss future plans and strategies.

Across our supply chain, our Supplier Management function monitors the real-time financial risks associated with our critical suppliers (e.g., financial strength, likelihood of insolvency, liquidity, credit worthiness, compliance with payment terms). This monitoring enables early sight of potential insolvency risks, which are initially investigated by Supplier Management and highlighted immediately to relevant Commercial Managers, allowing risks to be managed by all relevant stakeholders and mitigated.

Ineffective Organisation – Systems and People

Principal risk

Systems – Technology is evolving rapidly. To meet the needs of our business we must constantly adapt to our internal and external requirements. Existing systems and processes become unsuitable, outdated and need to evolve so that we can remain competitive, effective and efficient.

People – Our people ensure that we operate effectively and efficiently. External and internal requirements put pressure on colleagues. This pressure has increased as a result of growth and associated workload, cost of living and the challenging external resourcing market. Recruitment demand remains high with vacancies in the UK at over 1.2 million (Oct 2022). Labour market supply is low, combined with economic inactivity being at the highest level in at least 30 years (2.49 million – Oct 2022).

Risk mitigation strategy

Systems – We continuously review systems and processes to ensure they meet the needs of our business. Where benefits exceed the cost, we invest in new systems. In October 2021 we launched our new cloud financial and people ERP system to enable working in a simpler, more agile and cost-effective way. Moving to a cloud-based system enables us to receive quarterly upgrades to ensure it remains modern and relevant and provides the opportunity for continuous improvement and benefits.

People – We continue to invest in our people and have a strategy to ensure the development of talent and careers at Heathrow. Policies are in place to engage and motivate our colleagues; as well as maintain accountability and compliance with internal governance, policies and procedures. We provide career opportunities, development and training. In September 2022, we launched our new leadership development programme. It has been designed to help leaders address the needs of our colleagues in light of the changing landscape; and enable them to better understand the impact of their leadership style. Talent and criticality of roles and individuals are reviewed regularly. This supports the retention of talent, skills and business knowledge thus preventing single points of failure.

Heathrow Funding Limited

Directors' report *continued*

Principal risks *continued*
Political environment
Principal risk
Our ability to meet passenger and cargo demand is reliant on political support. Changes to the Government, and therefore to government priorities, can impact material decisions that are taken by us. Political stability has become more uncertain with any change in either the current Prime Minister and Cabinet or a new Government having the potential to impact the environment in which Heathrow operates.
Risk mitigation strategy
We continue to make a strong case for our place in the wider economy and the part we play in a successful Global Britain, and we explain the benefits that our ability to meet the UK's demand for long-haul travel brings. Whilst a change in the Government and their focus cannot be controlled, risk is monitored and proposed mitigating actions agreed in advance where necessary. We have a cross functional Policy Coordination Group, reporting to the Executive Committee and HAHL Board, which has implemented a structured approach to the identification and management of all risks related to changing Government policy.

Competition
Principal risk
We compete against other airports both within the UK and across the world for passengers; some make marginal choices, particularly connecting passengers, about which route to fly. The impact of COVID-19 has disrupted aviation and lower passenger numbers means that rival airports have more capacity and therefore greater potential to compete with Heathrow. In addition, Heathrow's charges increased significantly in 2022, potentially reducing our competitive advantage compared to other airports in the London system and our European hub competitors. Heathrow will need to continue to deliver great value to our airlines in order to retain them at these higher charges.

Risk mitigation strategy
Our primary focus is to ensure the continuity of safe, secure and efficient airport operations in the interests of all air transport users and build back capacity so that we can deliver the throughput and service levels that we did before COVID-19. Maintaining commercial strategies that enable us to deliver great value to airlines and consumers is key to improving competitiveness and retaining key passenger groups and partners.

Climate change and net zero carbon
Principal risk
Climate change remains the most significant mid to long-term risk facing the aviation sector and Heathrow, working with the wider industry must demonstrate real progress towards achieving the sector's net zero goal in this decade. Heathrow has implemented the Task Force for Climate related Financial Disclosures ('TCFD') recommendations and climate related risk is therefore considered under the following categories:

- Transitional risks – Transitional risks relate to the decarbonisation of Heathrow and the aviation sector to achieve net zero carbon emissions. Political, consumer and investor attitudes to aviation's climate impacts will become more negative without tangible progress to cut emissions and deliver the sector's net zero plan, threatening our ability to recover, operate and grow.
- Physical risks – Physical risks relate to the resilience of our assets, operations and network to the negative impacts of climate change including more extreme weather events.

These risks are presented in greater detail in the TCFD section of the HAHL Group annual report and financial statements which can be found at www.heathrow.com/company/investor-centre.

Risk mitigation strategy
Policy and global alignment to transition the aviation sector to net zero carbon emissions by 2050. We have been working with relevant aviation stakeholders to promote policies to scale up sustainable aviation fuel ('SAF'), to increase aircraft efficiency, and to support the development of zero emissions aircraft.

In November 2022, ICAO, the International Civil Aviation Organisation, formed by 193 member states, committed to net zero carbon emissions for international civil aviation by 2050. The building blocks of this commitment were the development of the required technical feasibility assessment combined with a robust consensus-driven approach for a global framework led by some member states, particularly the UK that developed an international aviation coalition climate ambition during its COP26 presidency. In 2021, the entire aviation industry had already committed to net zero carbon emissions by 2050, including IATA, the international industry airline body. Heathrow has committed to net zero carbon and, in February 2022, published our Net Zero Plan which guides our approach to decarbonisation. Our plan is aligned to the broader UK sector roadmap and sets clear goals and targets to cut emissions by 2030 and beyond.

Heathrow Funding Limited

Directors' report *continued*

Principal risks *continued*

Climate change and net zero carbon *continued*

The significant priority is accelerating net zero flying in the 2020s by securing the right policies for sustainable aviation fuel ('SAF') production at scale in the UK and building a high ambition coalition globally for net zero aviation and SAF. We have established net zero as a strategic programme in our H7 regulatory settlement period which ends in 2026. The programme, which includes over £200m of capital investment, will deliver the carbon emissions reductions we included in our plan, during this period. To ensure and support the delivery of our Net Zero Plan, climate change has been embedded into our governance structures, business planning development and operational processes and is supported by employee training and targets. We operate ISO 140001 and 50001 management systems which commit us to continuous improvement.

Financial stability

The HAHL Board approves prudent treasury policies and delegates certain responsibilities including changes to treasury policies, the approval of funding and the implementation of funding and risk strategy to the HAHL Group Finance Committee. Senior management directly control day-to-day treasury operations on a centralised basis.

The treasury function is not permitted to speculate in financial instruments. Its purpose is to identify, mitigate and hedge treasury-related financial risks inherent in the HAHL Group's business operations and funding. To achieve this, the Group enters into interest rate swaps, index-linked swaps, cross-currency swaps and foreign exchange contracts to protect against interest rate, inflation and currency risks.

The primary treasury-related financial risks faced by the HAHL Group are:

a. Interest rates

   The HAHL Group maintains a mix of fixed and floating rate debt. Interest rate swaps are entered by the Group to mitigate to interest rate risk for the Group.

b. Inflation

   The HAHL Group mitigates the risk of mismatch between Heathrow's aeronautical income and regulatory asset base, which are directly linked to changes in the retail prices index, and nominal debt and interest payments, by the issuance of index-linked instruments.

c. Foreign currency

   The HAHL Group uses cross-currency swaps to hedge all interest and principal payments on its foreign currency debt. The HAHL Group uses foreign exchange contracts to hedge material capital expenditure in foreign currencies once a project is certain to proceed.

d. Funding and liquidity

   The Group has established both investment grade and sub-investment grade financing platforms for Heathrow. The platforms support term loans, various revolving loan facilities including revolving credit facilities, working capital facilities and liquidity facilities, and Sterling and foreign currency capital markets issuance. All debt is secured and can be issued in either senior or junior format. Covenants are standardised wherever possible and are monitored on an ongoing basis with formal testing reported to the HAHL Group Audit Committee, the Board and Executive Committee. Although there can be no certainty that financing markets will remain open for issuance at all times, debt maturities are spread over a range of dates, thereby ensuring that the Group is not exposed to excessive refinancing risk in any one year.

   HAHL Group expects to have sufficient liquidity to meet all its obligations in full, including capital investment, debt service costs, debt maturities and distributions, for at least 12 months from the approved date of these consolidated financial statements. As at 31 December 2022, the HAHL Group had cash and cash equivalents and term deposits of £3,012 million.

e. Counterparty credit

   The Group's exposure to credit related losses, in the event of non-performance by counterparties to financial instruments, is mitigated by limiting exposure to any one party or instrument.

Heathrow Funding Limited

Directors' report *continued*

Directors' indemnity

The Company's Articles of Association provide that, subject to the provisions of the Companies (Jersey) Law 1991, but without prejudice to any protection from liability which might otherwise apply, every Director of the Company shall be indemnified out of the assets of the Company against any loss or liability incurred by them in defending any proceedings in which judgement is given in their favour, or in which they are acquitted or in connection with any application in which relief is granted to them by the court for any negligence, default, breach of duty or breach of trust by them in relation to the Company or otherwise in connection with their duties or powers or office. This indemnity also applies to the Directors who are Directors of other companies within the Group. The third-party indemnity provisions (which are qualifying third-party indemnity under the Companies (Jersey) Law 1991) are in place during the 2022 financial year and at the date of approving the Financial Statements.

Auditor

The auditors, PricewaterhouseCoopers LLP, have indicated their willingness to continue in office, and a resolution that they be re-appointed will be proposed within the period set out in section 485 of the Companies Act 2006.

Statement of disclosure of information to the Auditor

Each of the persons who is a director at the date of approval of this Annual report confirms that:

- so far as the director is aware, there is no relevant audit information of which the Company's auditor is unaware; and
- the director has taken all the steps that he ought to have taken as a director in order to make himself aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

This confirmation is given and should be interpreted in accordance with the Companies (Jersey) Law 1991.

Subsequent events

Subsequent events are disclosed in note 11.

The Directors' report was approved and authorised by the Board and issued on behalf of the Board by:

Javier Echave
Director

29 June 2023

Heathrow Funding Limited

Statement of directors' responsibilities in respect of the financial statements

The directors are responsible for preparing the financial statements in accordance with applicable Jersey law and United Kingdom Accounting Standards.

The directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period. In preparing the financial statements, the directors are responsible for:

- selecting suitable accounting policies and then applying them consistently;
- stating whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements;
- making judgements and accounting estimates that are reasonable and prudent; and
- preparing the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors confirm that they have complied with the above requirements in preparing the financial statements.

The directors are responsible for ensuring that the financial statements comply with The Companies (Jersey) Law, 1991 and safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities. So far as the directors are aware, there is no relevant audit information of which the company's auditors are unaware, and each director has taken all the steps that he or she ought to have taken as a director in order to make himself or herself aware of any relevant audit information and to establish that the company's auditors are aware of that information.

The directors are also responsible for keeping adequate accounting records that are sufficient to show and explain the company's transactions and disclose with reasonable accuracy at any time the financial position of the company.

The Directors' report was approved and authorised by the Board and issued on behalf of the Board by:

Javier Echave
Director

29 June 2023

Independent auditors' report to the members of Heathrow Funding Limited

Report on the audit of the financial statements

Opinion

In our opinion, Heathrow Funding Limited's financial statements:

- give a true and fair view of the state of the company's affairs as at 31 December 2022 and of its loss for the year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards, including FRS 102 "The Financial Reporting Standard applicable in the UK and Republic of Ireland", and applicable law); and
- have been prepared in accordance with the requirements of the Companies (Jersey) Law 1991.

We have audited the financial statements, included within the Annual report and financial statements (the "Annual Report"), which comprise: the statement of financial position as at 31 December 2022; the statement of comprehensive income and the statement of changes in equity for the year then ended; the accounting policies; the significant estimates and judgements; and the notes to the financial statements.

Our opinion is consistent with our reporting to the Audit Committee of Heathrow Airport Holdings Limited.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities under ISAs (UK) are further described in the Auditors' responsibilities for the audit of the financial statements section of our report. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence

We remained independent of the company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, which includes the FRC's Ethical Standard, as applicable to listed entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

To the best of our knowledge and belief, we declare that non-audit services prohibited by the FRC's Ethical Standard were not provided.

We have provided no non-audit services to the company in the period under audit.

Our audit approach

Overview

Audit scope

- Our audit scope includes a full scope audit of the company.

Key audit matters

- Valuation of derivative financial instruments - inflation linked swaps including day 1 fair valuation and credit risk adjustment
- Going concern basis of preparation

Heathrow Funding Limited

Independent auditor's report to members of Heathrow Funding Limited for the year ended 31 December 2022 *continued*

Materiality

- Overall materiality: £72.85m (2021: £73m) based on 0.5% of external borrowings.
- Performance materiality: £54m (2021: £55m).

The scope of our audit

As part of designing our audit, we determined materiality and assessed the risks of material misstatement in the financial statements.

Key audit matters

Key audit matters are those matters that, in the auditors' professional judgement, were of most significance in the audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) identified by the auditors, including those which had the greatest effect on: the overall audit strategy; the allocation of resources in the audit; and directing the efforts of the engagement team. These matters, and any comments we make on the results of our procedures thereon, were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

This is not a complete list of all risks identified by our audit.

Going concern basis of preparation is a new key audit matter this year. Impact of Covid, which was a key audit matter last year, is no longer included because of the factors leading to increased uncertainty are not relevant for current year. Otherwise, the key audit matters below are consistent with last year.

Key audit matter	How our audit addressed the key audit matter
Valuation of derivative financial instruments - inflation linked swaps including day 1 fair valuation and credit risk adjustment Refer to the Accounting Policies, significant estimates and judgements and to note 7 in the financial statements. As at 31 December 2022, the Company held derivative assets of £1,146m and derivative liabilities of £2,476m on the balance sheet. These are held to mitigate interest rate and foreign exchange risk arising on debts of £2.3bn. Included in these derivative balances were inflation linked swaps totalling £146m assets and £1,241m liabilities. IFRS 9 "Financial Instruments" requires derivatives to be accounted for at fair value with movements recognised in profit or loss, unless designated in a hedge relationship. Due to the nature and complexity in the valuations involved, we identified a significant risk that the fair value of inflation linked swaps may be misstated. The risk is mainly driven by: the valuation process (being manual in nature) of valuation differences between the consideration paid or received and the system derived fair value on inception or restructuring ('day-1 fair value'); and the estimation of the valuation of credit risk of the swaps (in particular the assumed loss given default percentage) to the valuation due to these derivatives ranking as super senior in the priority of payments.	We, with the support of our Treasury specialists, performed the following audit procedures: • Assessed the design and implementation of key controls relating to the valuation of derivatives; On a sample basis, performed independent valuation testing on the derivatives, including the credit risk adjustment and the new day-1 fair value at 31 December 2022. • Recalculated and assessed the accounting treatment for the day-1 fair value of derivatives in line with IFRS9 - Financial Instruments and IFRS 13 - Fair Value Measurement; Inspected the documentation supporting the super senior nature of interest rate swaps and inflation linked swaps where a higher recovery rate than the currency swaps is used in the valuation and evaluated whether the rate used is in line with the expected market rate. • Obtained third party confirmations from the financial institutions with which the group holds derivative instruments to assess the completeness of the instruments. • Tested the estimation of the credit risk and quantum of the recovery rate applied to the super senior derivatives. • Assessed management's derivative fair value disclosures in the financial statements. The results of our procedures above did not identify any material exceptions. We consider management's derivative fair value disclosures in the financial statements to be adequate.

Independent auditor's report to the members of Heathrow Funding Limited for the year ended 31 December 2022 *continued*

Going concern basis of preparation In the context of the 2021 Heathrow Funding accounts and the 2022 quarterly press releases relating to the wider Heathrow Group, the Group and Company previously prepared its financial statements on a basis of going concern with material uncertainty. Since then, the wider Heathrow Group has experienced strong passenger number growth in Q4 2022, and Q1 2023 experiencing 95% of pre-covid levels. It is with this growth and the significantly increased certainly that it provided over debt covenant compliance in future periods that the Directors made the decision to prepare the 2022 Heathrow Funding accounts on a going concern basis with the absence of material uncertainty. In assessing the going concern position, the Directors have considered the cash flow, liquidity and debt covenant compliance over the next 12 months of the group and also considered the period beyond 12 months to December 2024, as well as on an entity only basis reviewed the net asset position and cash flows of the company.	We, with the support of our Business Recovery Services experts, performed the following audit procedures: • Assessed the design and implementation of key controls relating to forecasting; • Assessed management's forecasts including consideration of the impact of COVID-19 on cash flows; • Reviewed the group's compliance with bank covenants; • Ensured the forecasts and calculations are mathematically accurate; • Assessed the reasonableness of assumptions used in management's base case forecasts, and challenged the judgements underpinning those forecasts, for example by obtaining independent third party evidence of market forecasts for passenger forecast of 74 million for 2023 and assessing the extent to which these assumptions are consistent with those used to support other financial statement estimates; • Assessed the reasonableness of management's severe but plausible downside case, and challenged the judgements regarding the low end of Heathrow's passenger forecast of 71 million for 2023; • Tested the underlying data in management's going concern model; • Assessed the entity only net asset position and cash flows in understanding the standalone basis; • Assessed the adequacy of disclosures in relation to going concern in the financial statements; The results of our procedures above did not identify any material exceptions. We consider the disclosures in the financial statements to be adequate and we concur with management's view that the Group and Company's 2022 financial statements are prepared on the basis of going concern with the absence of material uncertainty.

How we tailored the audit scope

We tailored the scope of our audit to ensure that we performed enough work to be able to give an opinion on the financial statements as a whole, taking into account the structure of the company, the accounting processes and controls, and the industry in which it operates.

Our audit effort included substantive testing of material financial statement line items.

Materiality

The scope of our audit was influenced by our application of materiality. We set certain quantitative thresholds for materiality. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures on the individual financial statement line items and disclosures and in evaluating the effect of misstatements, both individually and in aggregate on the financial statements as a whole.

Based on our professional judgement, we determined materiality for the financial statements as a whole as follows:

Independent auditor's report to the members of Heathrow Funding Limited for the year ended 31 December 2022 *continued*

Overall company materiality	72.85m (2021: 73m)
How we determined it	0.5% of external borrowings
Rationale for benchmark applied	The primary purpose of the Company is to raise debt instruments from external sources and provide funding to Heathrow (SP) Limited and its subsidiaries. We have therefore used total external borrowings as the benchmark.

We use performance materiality to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements exceeds overall materiality. Specifically, we use performance materiality in determining the scope of our audit and the nature and extent of our testing of account balances, classes of transactions and disclosures, for example in determining sample sizes. Our performance materiality was 75% (2021: 75%) of overall materiality, amounting to £54m (2021: £55m) for the company financial statements.

In determining the performance materiality, we considered a number of factors - the history of misstatements, risk assessment and aggregation risk and the effectiveness of controls - and concluded that an amount at the upper end of our normal range was appropriate.

We agreed with the Audit Committee that we would report to them misstatements identified during our audit above £3.6m (2021: £1.4m) as well as misstatements below that amount that, in our view, warranted reporting for qualitative reasons.

Conclusions relating to going concern

Based on the work we have performed, we have not identified any material uncertainties relating to events or conditions that, individually or collectively, may cast significant doubt on the company's ability to continue as a going concern for a period of at least twelve months from when the financial statements are authorised for issue.

In auditing the financial statements, we have concluded that the directors' use of the going concern basis of accounting in the preparation of the financial statements is appropriate.

However, because not all future events or conditions can be predicted, this conclusion is not a guarantee as to the company's ability to continue as a going concern.

Our responsibilities and the responsibilities of the directors with respect to going concern are described in the relevant sections of this report.

Reporting on other information

The other information comprises all of the information in the Annual Report other than the financial statements and our auditors' report thereon. The directors are responsible for the other information. Our opinion on the financial statements does not cover the other information and, accordingly, we do not express an audit opinion or, any form of assurance thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If we identify an apparent material inconsistency or material misstatement, we are required to perform procedures to conclude whether there is a material misstatement of the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report based on these responsibilities.

Independent auditor's report to the members of Heathrow Funding Limited for the year ended 31 December 2022 *continued*

Responsibilities for the financial statements and the audit

Responsibilities of the directors for the financial statements

As explained more fully in the Statement of directors' responsibilities in respect of the financial statements, the directors are responsible for the preparation of the financial statements in accordance with the applicable framework and for being satisfied that they give a true and fair view. The directors are also responsible for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the company or to cease operations, or have no realistic alternative but to do so.

Auditors' responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

Irregularities, including fraud, are instances of non-compliance with laws and regulations. We design procedures in line with our responsibilities, outlined above, to detect material misstatements in respect of irregularities, including fraud. The extent to which our procedures are capable of detecting irregularities, including fraud, is detailed below.

Based on our understanding of the company and industry, we identified that the principal risks of non-compliance with laws and regulations related to Heathrow Airport's CAA operating licence being revoked, breaches of environmental regulations, adherence to data protection requirements, UK tax legislation not being adhered to and non-compliance with employment regulations in the UK, and we considered the extent to which non-compliance might have a material effect on the financial statements. We also considered those laws and regulations that have a direct impact on the financial statements such as Companies (Jersey) Law 1991. We evaluated management's incentives and opportunities for fraudulent manipulation of the financial statements (including the risk of override of controls), and determined that the principal risks were related to posting inappropriate journal entries, and management bias in accounting estimates. Audit procedures performed by the engagement team included:

- Discussions with; management, including representatives outside of the finance function; representatives from Business Assurance and Internal Audit; and members of the group's General Counsel team. Those discussions included consideration of known or suspected instances of non-compliance with laws and regulations and fraud.
- Reading the Board minutes to identify any issues which could indicate non-compliance with laws and regulations.
- Challenging assumptions and judgements made by management in its significant accounting estimates in relation to the valuation of derivative financial instruments (see related key audit matter above).
- Identifying and testing journal entries, in particular any journal entries posted with unusual account combinations or those posted with unexpected words.

There are inherent limitations in the audit procedures described above. We are less likely to become aware of instances of non-compliance with laws and regulations that are not closely related to events and transactions reflected in the financial statements. Also, the risk of not detecting a material misstatement due to fraud is higher than the risk of not detecting one resulting from error, as fraud may involve deliberate concealment by, for example, forgery or intentional misrepresentations, or through collusion.

Our audit testing might include testing complete populations of certain transactions and balances, possibly using data auditing techniques. However, it typically involves selecting a limited number of items for testing, rather than testing complete populations. We will often seek to target particular items for testing based on their size or risk characteristics. In other cases, we will use audit sampling to enable us to draw a conclusion about the population from which the sample is selected.

A further description of our responsibilities for the audit of the financial statements is located on the FRC's website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditors' report.

Independent auditor's report to the members of Heathrow Funding Limited for the year ended 31 December 2022 *continued*

Use of this report

This report, including the opinions, has been prepared for and only for the company's members as a body in accordance with Article 113A of the Companies (Jersey) Law 1991 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

Other required reporting

Companies (Jersey) Law 1991 exception reporting

Under the Companies (Jersey) Law 1991 we are required to report to you if, in our opinion:

- we have not obtained all the information and explanations we require for our audit; or
- proper accounting records have not been kept by the company, or proper returns for our audit have not been received from branches not visited by us; or
- the financial statements are not in agreement with the accounting records and returns.

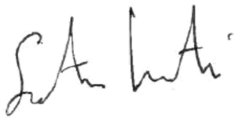
We have no exceptions to report arising from this responsibility.

Appointment

Following the recommendation of the Audit Committee, we were appointed by the members on 22 January 2019 to audit the financial statements for the year ended 31 December 2020 and subsequent financial periods. The period of total uninterrupted engagement is two years, covering the years ended 31 December 2020 to 31 December 2022.

Other matter

As required by the Financial Conduct Authority Disclosure Guidance and Transparency Rule 4.1.14R, these financial statements form part of the ESEF-prepared annual financial report filed on the National Storage Mechanism of the Financial Conduct Authority in accordance with the ESEF Regulatory Technical Standard ('ESEF RTS'). This auditors' report provides no assurance over whether the annual financial report has been prepared using the single electronic format specified in the ESEF RTS.



Sotiris Kroustis
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants
Watford
29 June 2023

Heathrow Funding Limited

Statement of comprehensive income for the year ended 31 December 2022

	Note	**Year ended 31 December 2022 £m**	Year ended 31 December 2021 £m
Financing			
Finance income	*2*	**1,424**	813
Finance cost	*2*	**(1,427)**	(850)
Fair value loss on financial instruments	*2*	**(291)**	(140)
Operating loss before taxation	*1*	**(294)**	(177)
Taxation	*3*	**-**	-
Loss after taxation for the financial year		**(294)**	(177)
Total comprehensive loss for the year		**(294)**	(177)

The statement of comprehensive income has been prepared on the basis that all operations are continuing operations.

The notes on pages 29 to 38 form part of these financial statements.

Heathrow Funding Limited

Statement of financial position as at 31 December 2022

	Note	31 December 2022 £m	31 December 2021 £m
Assets			
Non-current assets			
Trade and other receivables	*4*	**13,223**	13,583
Derivative financial instruments	*6*	**3,220**	2,385
		16,443	15,968
Current assets			
Trade and other receivables	*4*	**1,076**	886
Derivative financial instruments	*6*	**21**	41
		1,097	927
Total assets		**17,540**	16,895
Liabilities			
Non-current liabilities			
Borrowings	*5*	**(13,634)**	(13,596)
Derivative financial instruments	*6*	**(3,214)**	(2,338)
		(16,848)	(15,934)
Current liabilities			
Borrowings	*5*	**(936)**	(933)
Derivative financial instruments	*6*	**(39)**	(17)
Trade and other payables	*8*	**(1)**	(1)
		(976)	(951)
Total liabilities		**(17,824)**	(16,885)
Net (liabilities)/assets[1]		**(284)**	10
Capital and reserves			
Share capital	*9*	**-**	-
Retained earnings		**(284)**	10
Total shareholders' (deficit)/funds		**(284)**	10

[1] Net assets reflect the different measurement bases used for certain financial instruments: Borrower Loan Agreements and bonds are recorded at amortised cost but derivatives are re-measured to fair value at each reporting date.

The notes on pages 29 to 38 form part of these financial statements.

The financial statements on pages 19 to 38 were approved by the Board of Directors on 29 June 2023 and signed on its behalf by

Javier Echave
Director

Martin Bailey

Martin Bailey
Director

Heathrow Funding Limited

Statement of changes in equity for the year ended 31 December 2022

	Share capital £m	Retained earnings £m	Total £m
At 1 January 2021	-	187	187
Total comprehensive loss for the financial year	-	(177)	(177)
At 31 December 2021	**-**	**10**	**10**
Total comprehensive loss for the financial year	**-**	**(294)**	**(294)**
At 31 December 2022	**-**	**(284)**	**(284)**

The notes on pages 29 to 38 form part of these financial statements.

Heathrow Funding Limited

Statement of cash flows for the year ended 31 December 2022

	Year ended 31 December 2022 £m	Year ended 31 December 2021 £m
Operating activities		
Loss before tax	**(294)**	(177)
Adjustments for:		
Net finance costs	**294**	177
Working capital changes:		
Net decrease/(increase) in amounts owed by group undertakings – interest bearing[1]	**1,070**	(394)
Net cash generated from/(used in) operating activities	**1,070**	(394)
Cash flows from financing activities		
Proceeds from issuance of bonds	**196**	1,582
Repayment of bonds	**(732)**	(1,119)
Settlement of accretion on index-linked swaps	**(44)**	(69)
Early settlement of accretion on index-linked swaps	**(490)**	-
Net cash (used in)/generated from financing activities	**(1,070)**	394
Net change in cash and cash equivalents	**-**	-
Cash and cash equivalents at beginning of year	**-**	-
Cash and cash equivalents at end of year	**-**	-

[1]This movement excludes non-cash movements in amounts owed by group undertakings – interest bearing.

Accounting policies for the year ended 31 December 2022

The principal accounting policies applied in the preparation of the financial statements of Heathrow Funding Limited (the 'Company') are set out below. These policies have been applied consistently to all the years presented, unless otherwise stated.

Statement of compliance

These financial statements have been prepared in accordance with Financial Reporting Standards 102 – 'The Financial Reporting Standard applicable in the United Kingdom and Republic of Ireland' (FRS 102) and with the Companies (Jersey) Law 1991. This provides for the Company to follow statements of accounting practice issued by the relevant accounting bodies in the United Kingdom. Consequently, the Company follows Financial Reporting Standard 100 ('FRS100') and in accordance with FRS 100 the Company has chosen to apply FRS 102.

The Company

The Company is a limited liability company registered and incorporated in Jersey. The registered office is IFC 5, St Helier, Jersey, JE1 1ST.

Basis of preparation

The Company financial statements are prepared in accordance with FRS 102 and are presented on the basis of the historical cost convention, except for derivative financial instruments under fair value hedge accounting. These exceptions to the historical cost convention have been measured at fair value in accordance with FRS 102 and as permitted by the Fair Value Directive as implemented in the Companies Act 2006.

The financial statements are presented in Sterling and are rounded to the nearest million pounds (£m), except when otherwise noted.

The Company has adopted the following standard that is relevant to these financial statements:

- IAS 39 'Financial Instruments: Recognition and Measurement', in compliance with FRS 102. As a result, the accounting requirements of IAS 39 have been applied to all financial instruments instead of those of FRS 102 (s.11 and s.12)

The individual financial statements of the Company have been prepared in compliance with United Kingdom Accounting Standards, including Financial Reporting Standard 102, 'The Financial Reporting Standard applicable in the United Kingdom and the Republic of Ireland' ('FRS 102') and the Companies Act 2006.

The Company has taken advantage of the exemption provided by Section 400 of the Companies Act 2006 from the requirement to prepare consolidated financial statements as it is a wholly-owned subsidiary of FGP Topco Limited and its subsidiary undertakings are included in the consolidated financial statements of that company for the year ended 31 December 2021. Its registered office is The Compass Centre, Nelson Road, Hounslow, Middlesex, TW6 2GW. The financial statements present information about the Company as an individual entity only and not as a group.

FRS 102 allows a qualifying entity certain disclosure exemptions, subject to conditions, therefore, the company has taken advantage of the following exemptions in its individual financial statements:

- the requirement from disclosing related party transactions with entities that are wholly- owned subsidiaries of the FGP Topco Limited Group
- from providing certain other disclosures regarding key management personnel

Going concern

The Directors have prepared the financial information presented within the annual report and financial statements on a going concern basis as they have a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future.

Background

The company is part of the wider Heathrow Group of companies. In considering the going concern assessment, the Directors have considered both the individual circumstances of the company but also the wider Group given the corporate structure, which involves activities and cash generation across the Group including within the main operating company, Heathrow Airport Limited. Heathrow is economically regulated by the CAA which controls Heathrow's maximum airport charges. On 1 January 2022 the H7 price control period commenced, running to 31 December 2026. Due to its delays in making a final decision, the CAA put in place an interim tariff (the "2023 Interim Tariff") from 1 January 2023 to 31 December 2023 of £31.57 in nominal terms, ahead of a Final Decision which was subsequently published on 8th March 2023. This Final Decision provides an average H7 tariff of £23.06 in 2020 CPI real terms and has been arrived at based on a set of assumptions such as higher passenger numbers, lower operating costs and higher commercial revenues versus those forecast by the wider Heathrow Group, which

Accounting policies for the year ended 31 December 2022 *continued*

Going concern *continued*
has led to a lower tariff than the Group believes is appropriate. Whilst the H7 Final decision contains a new traffic risk sharing mechanism and other mechanisms to deal with asymmetric risk and cost uncertainty, they do not fully protect against lost cash flows and would lead to partial recovery of lost revenue over time.

This critical relationship between H7 prices and forecast passenger numbers, as well as the potential resultant impact to liquidity and debt covenant compliance have been considered in assessing the appropriateness of preparing this annual report and financial statements on a going concern basis.

The wider Heathrow Group is bound by two types of debt covenants, tested on 31 December each year: the Regulatory Asset Ratio ("RAR"), a measure of the ratio of consolidated nominal net debt to the Regulatory Asset Base ("RAB"); and Interest Cover Ratios ("ICR"), a measure of operating cashflows to debt interest charge. These covenants exist at different levels within the Group's Class A and Class B debt.

Base case
The Directors have considered the wider Heathrow Group when assessing going concern. In assessing the going concern position, the Directors have considered the regulatory uncertainty described above, as well as the potential impact of any further COVID-19 impacts on cash flow, liquidity and debt covenant compliance over the next 12 months.

- Forecast revenue and operating cash flows from the underlying operations, based on 2023 traffic forecasts.
- Forecast level of capital expenditure based on the CAA's H7 Final Decision.
- The overall Group liquidity position including cash resources, the remaining committed and uncommitted facilities available to it, its scheduled debt maturities, its forecast financial ratios, projected covenant requirements, and its ability to access the debt markets.

Base case passenger forecast
In modelling passenger number recovery from COVID-19, there remains a degree of uncertainty given the wide range of potential traffic forecasts being formed by various stakeholders in the global aviation industry, including the CAA. Therefore, there is inherent subjectivity in our forecasting. Nevertheless, passenger numbers have increased significantly in the first 5 months of 2023; with total passengers to 31 May being 95% of 2019 levels. Despite a high-inflationary economic environment, impacting the cost-of-living of passengers, demand has remained strong.

Base case tariffs
The base case uses the CAA's Interim Tariff for the entirety of 2023, with a 2024 nominal tariff of £25.43 based on the tariff set out in the CAA's Final Decision. Under the base case, the Group will meet all covenants associated with its financial arrangements.

Base case cash flow and liquidity
The wider Heathrow Group can raise finance at both Heathrow SP Limited ("Heathrow SP") and Heathrow Finance plc ("Heathrow Finance"). Despite a continued challenging market, there continues to be confidence and support for the Group's credit with £546 million of new debt raised in FY22 in addition to the successful refinancing of the group's £1.38bn revolving credit facility in Q4 2022. No additional debt was raised in Q1. Consequently, Heathrow SP held cash of £1.1 billion as at 31 March 2023. Total debt maturity within Heathrow SP for the next 12 months from 31 March 2023 is £0.6 billion. The wider Heathrow Group (which includes Heathrow Finance and the cash held at Heathrow SP) has cash of £2.3bn available at 31 March 2023. Taking this into account, the Group has sufficient liquidity to meet its base case cash flow needs for the going concern period. This includes forecast operational costs, capital investment, debt service costs, scheduled debt maturities and repayments.

Severe but plausible downside case
The Directors are required to consider severe but plausible downside scenarios in the preparation of the annual report and financial statements. In considering a severe but plausible downside, the Directors have considered the inherent judgement in forecasting future passenger numbers, particularly in a highly inflationary economic environment impacting the disposable income of passengers on cash flow generation, liquidity and debt covenant compliance.

Under the Group's downside scenario, the Directors have considered passenger numbers at the low end of Heathrow's 2023 and 2024 passenger forecast to be a severe but plausible outcome. This considers the Group's views of plausible impacts caused by reduced passenger confidence and other economic factors. The low range of passengers represents a 5% reduction against the base case. The tariff assumptions remain the same as in the base case.

Going concern *continued*

Conclusion

Having had regard to both liquidity and debt covenants, and considering severe but plausible downsides, the Directors have concluded that there will be funds available to meet the Group and Company's funding requirements for at least 12 months from the date of the annual report and financial statements and that it is accordingly appropriate to adopt a going concern basis with no material uncertainty for the preparation of these results.

Foreign currency

The Company financial statements are presented in Sterling, which is the Company's functional currency.

Transactions denominated in foreign currencies are initially recorded in the entity's functional currency applying the spot exchange rate using the exchange rates prevailing at the dates of transactions. Monetary assets and liabilities denominated in foreign currencies are retranslated into Sterling at the rates of exchange ruling at the reporting date. Differences arising on translation are charged or credited to the statement of comprehensive income. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

Finance income

Finance income is recognised when it is probable that the economic benefits will flow to the Company and the amount of revenue can be measured reliably. Finance income is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset to the asset's net carrying amount on initial recognition.

Taxation

Whilst the Company is incorporated outside the UK, it is treated as a UK resident company for tax purposes. The Company qualifies as a 'securitisation company' within the scope of the Taxation of Securitisation Companies Regulations 2006 under UK tax law. Therefore its annual results are not subject to Corporation tax and instead a nominal fixed amount of £20,000 is taxed every year.

Borrowings

Borrowings are recognised initially at fair value, net of transaction costs incurred and are subsequently stated at amortised cost. Any difference between the amount initially recognised (net of transaction costs) and the redemption value is recognised in the statement of comprehensive income over the period of the borrowings using the effective interest method. Borrowings being novated or cancelled and re-issued, with a substantial modification of the terms, are accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability, with any resulting gain or loss recognised in the statement of comprehensive income.

Borrowings from Company undertakings include the balance of the Borrower Loan Agreements ('BLAs') payable by the Company to Heathrow Funding Limited. Advances under the BLAs are secured and are issued on substantially the same terms as the bonds issued by Heathrow Funding Limited. The advances are carried at amortised cost with the interest expense recognised using the effective interest method. The nominal amount of the index-linked borrowings is accreted for inflation component recognised within interest payable in the statement of comprehensive income.

Debt issue costs

Prepaid fees in relation to the future issuance of debt are held on the statement of financial position on the basis that such issuance is considered probable. If issues do not occur, or are deemed not to be probable, such fees are recognised in the statement of comprehensive income.

Derivative financial instruments

Derivative instruments not designated in hedge accounting relationships and are accounted for at fair value and recognised immediately in the (statement of comprehensive income) profit and loss.

Derivatives are not in a hedge relationship, the fair value changes on these derivatives are recognised within fair value gains/(losses) on financial instruments in the statement of comprehensive income. The interest payable and receivable on those derivatives are recorded at their net amount in finance costs in the statement of comprehensive income.

Derivative financial instruments *continued*
Derivatives are initially recognised at fair value on the date a derivative contract is entered into and are subsequently re-measured at their fair value at each reporting period. The Company does not designate derivatives held by the Company in a hedge relationship.
Certain derivatives, as indicated by their fair value at inception or immediately prior to the restructuring, could not be supported by observable inputs alone. These "Day1" fair values are supported by unobservable factors including the counterparty's credit, capital, funding and trading charges. Therefore, such movement was deferred on the balance sheet in compliance with IFRS 9 and will be recognised in the statement of comprehensive income on a straight-line basis over the life of the underlying derivative instrument.

Accounting for changes in credit risk
Accounting standards require that the fair value of financial instruments reflects their credit quality, and also changes in credit quality where there is evidence that this has occurred. The credit risk associated with the Company's derivatives is updated monthly based on current market data.

Classification of financial instruments issued by the Company
In accordance with FRS 102, Section 22: *Liabilities and Equity*, financial instruments issued by the Company are treated as a liability only to the extent that they meet the following two conditions:

- they include contractual obligation to deliver cash or another financial asset; or
- they include a contract that will or may be settled in the entity's own equity instruments and:
  - under which the entity is or may be obliged to deliver a variable number of the entity's own equity instruments; or
  - will or may be settled other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of the entity's own equity instruments.

The Company's financial liabilities include borrowings, trade and other payables and derivative financial instruments.

To the extent that this definition is met, the proceeds of issue are classified as a financial liability. Where the instrument so classified takes the legal form of the Company's own shares, the amounts presented in these financial statements for share capital and share premium reserve exclude amounts in relation to those shares. Finance payments associated with financial liabilities are dealt with as part of interest payable and similar charges.

Finance payments associated with financial instruments that are classified as part of shareholders' funds are dealt with as appropriations in the reconciliation of movements in shareholders' funds.

As permitted by FRS 102, the Company has chosen to apply the classification provisions of International Accounting Standard ('IAS') 39 'Financial Instruments: Classification of financial assets and Classification of financial liabilities'. As a result, the accounting requirements of IAS 39 have been applied to all financial instruments instead of those of FRS 102.

Amounts owed to/by group undertakings
Amounts owed to/by Group undertakings are recognised initially at fair value, net of transaction costs incurred and are subsequently stated at amortised cost. Any difference between the amount initially recognised (net of transaction costs) and the redemption value is recognised in the statement of comprehensive income over the period of the borrowings using the effective interest method.

Share capital
Ordinary shares are classified as equity and are recorded at the par value of proceeds received, net of direct issue costs allowing for any reductions in the par value. Where shares are issued above par value, the proceeds in excess of par value are recorded in the share premium reserve.

Issue costs and arrangement fees
Immediately after issue, debt is stated at the fair value of the consideration received on the issue of the capital instrument after deduction of issue costs. The finance cost of the debt is allocated to periods over the term of the debt at an effective interest rate on the carrying amount.

Accounting policies for the year ended 31 December 2022 *continued*

Issue costs and arrangement fees *continued*
Issue costs are those that are incurred directly in connection with the issue of a capital instrument, that would not have been incurred had the instrument not been issued. These are accounted for as a deduction from the fair value of consideration received and amortised using the effective interest method.

Facility and arrangement fees resulting from the negotiation of finance that do not qualify as issue costs are written off to the profit and loss account as incurred.

Heathrow Funding Limited

Significant estimates and judgements for the year ended 31 December 2022

In applying the Company's accounting policies, management have made judgements and estimates in a number of key areas. Actual results may, however, differ from the estimates calculated and management believe that the following areas present the greatest level of uncertainty.

Critical judgements in applying the Company's accounting policies

Going concern
The impact of post pandemic recovery and regulatory uncertainty on going concern was considered in some detail. Further information can be found within the 'accounting policies' section.

Key sources of estimation uncertainty

Loss given default and assumed recovery rates
Accounting standards require that the fair value of financial instruments reflects their credit quality, and also the assumed recovery rate which then implies a loss given default rate. The credit risk associated with the Company's derivatives is updated monthly based on current market data, and industry standard default rates. However certain derivatives are ranked higher in the waterfall priority payments schedule such as interest rate swaps and inflation-linked swaps and therefore apply a super senior recovery rate.

On a semi-annual basis, the Group reviews any material changes to the valuation techniques and market data inputs used.

As all derivative and associated risks are passed to Heathrow Airport Limited there is no sensitivity applicable to the Company's super senior derivatives.

Heathrow Funding Limited

Notes to the financial statements for the year ended 31 December 2022

1 Operating loss before taxation

Auditor's fee
Audit fees are recharged in accordance with the Shared Service Agreement ('SSA') into the operating entities. The Company is not an operating entity and is therefore not party to the SSA and receives no recharge of the audit cost. However, the Company's auditor received £173,000 (2021: £165,000) as remuneration for the audit of the Company's financial statements the cost of which is borne by Heathrow Airport Limited.

Employee information
The Company has no employees (2021: nil).

Directors' remuneration
A total amount of £5,000 was paid to Apex Group Fiduciary Services Limited (formerly Sanne Fiduciary Services Limited) in relation to Director services for the year ended the 31 December 2022 (2021: £5,000). This service was provided by Lisa Aune, a Jersey resident employee of Apex Group Fiduciary Services Limited who was appointed on the board of Heathrow Funding Limited, in line with the Directorship Engagement Letter dated 27 June 2008 and the Directorship Novation Agreement dated 15 July 2013. In addition to this, a total of £40,829 (2021: £33,334) was paid to Apex Group Fiduciary Services Limited by various entities in the Heathrow Airport Holdings Group for registered office and company secretarial services in line with the Letter of Engagement between the Companies dated 29 September 2021.

Javier Echave is a director of a number of companies within the Heathrow Airport Holdings Group during the year. His remuneration for the year ended 31 December 2022 was disclosed in the financial statements of Heathrow Airport Holdings Limited. The directors do not believe it is possible to accurately apportion their remuneration to individual companies based on services provided. Yuanyuan Ding, Nicholas Golding and Martin Bailey were directors of a number of companies within the HAHL Group during the year. They were paid by, but are not directors of, Heathrow Airport Limited. The directors do not believe it is possible to accurately apportion their remuneration to individual companies within the HAHL Group based on services provided.

During the year, one of the directors (2021: one) had retirement benefits accruing to them under a defined benefit scheme and one of the directors (2021: one) had retirement benefits accruing to them under a defined contribution scheme.

2 Financing

	Year ended 31 December 2022 £m	Year ended 31 December 2021 £m
Net finance costs before certain re-measurements		
Finance income		
Interest receivable from group undertakings	**1,424**	813
Total finance income	**1,424**	813
Finance costs		
Interest payable on external borrowings	**(793)**	(642)
Net interest payable on derivatives	**(634)**	(208)
Total finance costs	**(1,427)**	(850)
Net finance costs before certain re-measurements	**(3)**	(37)
Certain re-measurements		
Fair value loss on financial instruments		
Index-linked swaps with external counterparties	**661**	(529)
Index-linked swaps as internal derivatives with Heathrow Airport Limited	**(658)**	527
Cross-currency swaps with external counterparties and retranslation of foreign currency debt[1]	**(294)**	(132)
Interest rate swaps with external counterparties	**267**	(102)
Interest rate swaps as internal derivatives with Heathrow Airport Limited	**(267)**	96
Fair value loss on financial instruments	**(291)**	(140)
Net finance costs including certain re-measurements	**(294)**	(177)

[1] Includes foreign exchange retranslation on the currency bonds of £285 million (2021: £318 million) which has moved systematically in the opposite direction to that of the cross currency swaps which economically hedge the related currency.

Heathrow Funding Limited

Notes to the financial statements for the year ended 31 December 2022

2 Financing *continued*

Certain re-measurements relates to the derivative financial instruments, which are subject to external financial market fluctuations.

3 Taxation

	Year ended 31 December 2022 £m	Year ended 31 December 2021 £m
UK corporation tax		
Current tax at 19% (2021: 19%)	**-**	-
Group relief payable	**-**	-
(Under)/Over provision in respect of prior years	**-**	-
Taxation for the year	**-**	-

Reconciliation of tax charge

The actual tax charge for the current and prior year differs from the theoretical amount that would arise by applying the UK statutory tax rate to the accounting profits of the company for the reasons set out in the following reconciliation:

	Year ended 31 December 2022 £m	Year ended 31 December 2021 £m
Loss on ordinary activities before tax	**(294)**	(177)
Tax credit /(charge) on ordinary activities at 19% (2021: 19%)	**56**	34
Effect of:		
Non-taxable income	**(56)**	(34)
Taxation for the year	**-**	-

Whilst the Company is incorporated outside the UK, it is treated as a UK resident company for tax purposes. As the Company qualifies as a 'securitisation company' within the scope of the Taxation of Securitisation Companies Regulations 2006, it is subject to UK corporation tax on a small margin rather than the profit shown in the statement of comprehensive income.

For the year ended 31 December 2022, the profits subject to corporation tax were £20,000 (2021: £20,000) which gave rise to a tax liability of £3,800 (2021: £3,800).

Finance Act 2021 substantively enacted the increase in corporation tax from 19% to 25% to take effect from 1 April 2023.

Other than these changes, there are no items which would materially affect the future tax charge.

4 Trade and other receivables

	31 December 2022 £m	31 December 2021 £m
Current		
Interest receivable from group undertakings[1]	**180**	163
Amounts owed by group undertakings – interest bearing[2]	**896**	723
	1,076	886
Non-current		
Amount owed by group undertakings – interest bearing[2]	**13,223**	13,583
	13,223	13,583
Total trade and other receivables	**14,299**	14,469

[1] Interest receivable from group undertakings' relates to interest accrued on the BLAs receivable from Heathrow Airport Limited ('Heathrow').

[2] Amounts owed by group undertakings - interest bearing' largely represent the balance of the BLAs receivable from Heathrow. The advances under the BLAs are secured and are issued on substantially the same terms as the bonds issued by the Company, taking into consideration the related hedging instruments. Heathrow (SP) Limited, Heathrow (AH) Limited, Heathrow Airport Limited and Heathrow Express Operating Company Limited are joint guarantors in respect of principal, indexation, interest, fees and hedging arrangements in relation to the borrowings of Heathrow under the BLAs.

Heathrow Funding Limited

Notes to the financial statements for the year ended 31 December 2022 *continued*

5 Borrowings

	31 December 2022 £m	31 December 2021 £m
Current		
Secured		
Bonds		
1.650%+RPI £180 million due 2022	-	234
1.875% €600 million due 2022	-	504
5.225% £750 million due 2023	747	-
	747	738
Interest payable on borrowings	189	195
Total current	936	933
Non-current		
Secured		
Bonds		
5.225% £750 million due 2023	-	732
7.125% £600 million due 2024	598	597
0.500% CHF400 million due 2024	358	325
3.250% C$500 million due 2025	304	290
1.500% €750 million due 2025	660	625
4.221% £155 million due 2026	155	155
6.750% £700 million due 2026	696	695
0.450% CHF210 million due 2026	189	171
2.650% NOK1,000 million due 2027	84	84
2.694% C$650 million due 2027	395	379
1.810% CHF165 million due 2027	147	-
2.625% £350 million due 2028	347	346
3.400% C$400 million due 2028	243	233
7.075% £200 million due 2028	199	199
4.150% A$175 million due 2028	98	93
2.500% NOK1,000 million due 2029	84	84
2.750% £450 million due 2029	446	445
3.782% C$400 million due 2030	243	233
1.125% €500 million due 2030	438	415
1.500% €750 million due 2030	660	625
3.661% C$500 million due 2031	304	291
6.450% £900 million due 2031	863	860
Zero-coupon €50 million due January 2032	70	63
1.366%+RPI £75 million due 2032	104	92
Zero-coupon €50 million due April 2032	68	62
0.101%+RPI £181.75 million due 2032	218	192
1.875% €500 million due 2032	441	418
3.726% C$625 million due 2033	386	371
4.171% £50 million due 2034	50	50
Zero-coupon €50 million due 2034	57	52
1.875% €650 million due 2034	567	538
0.347%+RPI £75 million due 2035	91	80
0.337%+RPI £75 million due 2036	91	80
1.061%+RPI £180 million due 2036	245	216
0.419%+RPI £51 million due 2038	61	54
3.460% £105 million due 2038	105	105
1.382%+RPI £50 million due 2039	69	61
3.334%+RPI £460 million due 2039	765	679
Zero coupon €86 million due 2039	84	78
0.800% JPY1,000 million due 2039	64	65

Heathrow Funding Limited

Notes to the financial statements for the year ended 31 December 2022 *continued*

5 Borrowings *continued*

	31 December 2022	31 December 2021
	£m	£m
Non current *continued*		
Secured *continued*		
1.238%+RPI £100 million due 2040	**137**	121
0.362%+RPI £75 million due 2041	**91**	80
3.500% A$125 million due 2041	**70**	67
5.875% £750 million due 2041	**739**	739
2.926% £55 million due 2043	**54**	54
4.625% £750 million due 2046	**742**	742
4.702% £60 million due 2047	**60**	-
1.372%+RPI £75 million due 2049	**104**	92
2.750% £400 million due 2049	**393**	393
0.147%+RPI £160 million due 2058	**197**	175
Total non-current	**13,634**	13,596
Total borrowings	**14,570**	14,529
Total borrowings (excluding interest payable)	**14,381**	14,334

The maturity dates of the Heathrow Funding Limited bonds listed above reflect their scheduled redemption dates that correspond to the maturity dates of the loans between Heathrow Airport Limited and Heathrow Funding Limited. The bonds are not callable in nature and are expected to be repaid on their scheduled redemption date. However, to meet rating agency requirements the bonds have a legal maturity that is two years later, except for the 7.125% £600 million due 2024, 4.221% £155 million due 2026, 2.625% £350 million due 2028, 0.101%+RPI £182 million due 2032, 0.347%+RPI £75 million due 2035, 0.337%+RPI £75 million due 2036, 1.061%+RPI £180 million due 2036, 3.460% £105 million due 2038, 0.419%+RPI £51 million due 2038 and 0.362%+RPI £75 million due 2041 bonds wherein the redemption dates coincide with their legal maturity dates.

Fair value of borrowings

	31 December 2022		31 December 2021	
	Book value	**Fair value[1]**	Book value	Fair value[1]
	£m	**£m**	£m	£m
Current				
Bonds	**747**	**749**	738	691
Non-current				
Bonds	**13,634**	**12,040**	13,596	15,397
	14,381	**12,789**	14,334	16,088

[1] Fair values of borrowings are for disclosure purposes only.

Accrued interest is included as a current borrowings balance and not in the carrying amount of non-current borrowings. The fair value of listed borrowings are based on quoted prices (thereby classified as Level 1) at balance sheet date. For unlisted borrowings, the Company establishes fair values by using discounted cash flow analysis utilising yield curves derived from observable market data, which are adjusted to allow for any relevant credit risk (Level 2). The fair value of borrowings which have floating rate interest are assumed to materially equate to their nominal value. At 31 December 2022, the fair value of debt classified as Level 1 and Level 2 was £12,171 million and £618 million respectively (2021: £15,137 million and £951 million respectively). The RPI growth rate in the period reflected by a 12-month annualised increase of 14.0% in 2022 compared to an annualised increase of 7.1% in 2021.

Securities and guarantees

The Company has given Deutsche Trustee Company Limited (the 'Bond Trustee') a covenant to pay and discharge, when due, to each of the Issuer Secured Creditors (including Bondholders) all Issuer Secured Liabilities (including all amounts due under the Bonds). The Bond Trustee holds the benefit of that covenant on trust for itself and the Issuer Secured Creditors. The Company has also granted security to the Bond Trustee (for itself and as trustee for the Issuer Secured Creditors) over its property, assets, undertakings and rights to secure the covenant to pay and discharge the Issuer Secured Liabilities.

Heathrow Funding Limited

Notes to the financial statements for the year ended 31 December 2022 *continued*

5 Borrowings *continued*

All borrowings issued by the Company are on-lent to Heathrow Airport Limited under the BLA. The advances under the BLA are issued on substantially the same terms as the new bonds issued by the Company, taking into consideration the related hedging instruments. Foreign currency bonds and the related cross-currency swaps are packaged together and on-lent to Heathrow Airport Limited.

6 Derivative financial instruments

	Notional £m	Assets £m	Liabilities £m	Total £m
31 December 2022				
Current				
Cross-currency swaps	-	-	-	-
Interest rate swaps:	-	-	-	-
with counterparties external to the SP Group				
with fellow subsidiary Heathrow Airport Limited	-	-	-	-
Index-linked swaps:				
with counterparties external to the SP Group	160	-	(39)	(39)
with fellow subsidiary Heathrow Airport Limited	100	21	-	21
Total current	**260**	**21**	**(39)**	**(18)**
Non-current				
Cross currency swaps	5,533	336	(186)	150
Interest rate swaps:				
with counterparties external to the SP Group	7,378	662	(1,010)	(348)
with fellow subsidiary Heathrow Airport Limited	7,378	1,009	(662)	347
Index-linked swaps:				
with counterparties external to the SP Group	5,547	146	(1,241)	(1,095)
with fellow subsidiary Heathrow Airport Limited	5,401	1,067	(115)	952
Total non-current	**31,237**	**3,220**	**(3,214)**	**6**
Total	**31,497**	**3,241**	**(3,253)**	**(12)**

	Notional £m	Assets £m	Liabilities £m	Total £m
31 December 2021				
Current				
Cross-currency swaps	490	24	-	24
Interest rate swaps:	-	-	-	-
with counterparties external to the SP Group				
with fellow subsidiary Heathrow Airport Limited	-	-	-	-
Index-linked swaps:				
with counterparties external to the SP Group	100	-	(17)	(17)
with fellow subsidiary Heathrow Airport Limited	100	17	-	17
Total current	690	41	(17)	24
Non-current				
Cross currency swaps	5,398	255	(98)	157
Interest rate swaps:				
with counterparties external to the SP Group	7,500	113	(665)	(552)
with fellow subsidiary Heathrow Airport Limited	7,500	665	(113)	552
Index-linked swaps:				
with counterparties external to the SP Group	5,707	53	(1,462)	(1,409)
with fellow subsidiary Heathrow Airport Limited	5,501	1,299	-	1,299
Total non-current	31,606	2,385	(2,338)	47
Total	32,296	2,426	(2,355)	71

Heathrow Funding Limited

6 Derivative financial instruments *continued*

A full disclosure of derivative financial instruments can be found in the consolidated financial statements of Heathrow (SP) Limited (external derivative financial instruments) and in the financial statements of Heathrow Airport Limited (internal derivative financial instruments).

The Company does not apply hedge accounting in relation to any of its derivative financial instruments.

Cross-currency swaps
Cross-currency swaps have been entered into by the Company to hedge currency risk on interest and principal payments on its foreign currency-denominated bond issues.

Index-linked swaps
Index-linked swaps have been entered into by the Company to economically hedge RPI linked revenue and regulatory asset base of Heathrow Airport Limited.

Interest rate swaps
Interest rate swaps have been entered into by the Company to hedge against variability in interest cash flows on current and future debt issuances.

During the year, new interest rate swaps with a notional of £0.5 billion were executed in continuation of the theme where the SP Group will receive fixed coupon and pay SONIA with a spread close to zero during 2022, where possible to maintain hedging ratio compliance.

This resulted in a fair value of £2 million (cost) at initial recognition and deferred on the balance sheet.

As at 31 December 2022, £246 million (31 December 2021: £276 million) remained deferred on the balance sheet and £32 million had been recognised in the statement of comprehensive income for the period (2021: £30 million).

In relation to the internal swaps with Heathrow Airport Limited, £232 million remained deferred on the balance sheet as at 31 December 2022 (31 December 2021: £261 million) and £31 million had been recognised in the statement of comprehensive income for the period (2021: £30 million).

The Company has index-linked derivative financial instruments where changes in RPI are capitalised to the carrying value of the derivative instrument over its life, with scheduled payments usually every 5 years. Swap accretion payments of the accrued accretion of £490 million in advance of the schedule repayment dates were made during the period, which has had the effect of reducing future accretion payments by £541 million.

7 Financial instruments

Financial risk management objectives and policies
The SP Group's principal financial instruments (other than derivatives) comprise of loans, term notes, listed bonds, cash and short-term deposits; the main purpose of these instruments is to raise finance for the SP Group's operations; and additionally include trade and other receivables, trade and other payables and lease liabilities.

The SP Group also enters into derivative transactions, principally interest rate swaps, index-linked swaps, cross-currency swaps and foreign exchange contracts. The purpose of these transactions is to manage the interest rate and currency risks arising from the SP Group's operations and its sources of finance.

The SP Group mitigates the risk of mismatch between Heathrow's aeronautical income and its regulatory asset base, which are directly linked to changes in the retail prices index, and nominal debt and interest payments by the use of index-linked instruments.

The SP Group's policy does not permit use of derivatives for speculative purposes. However, some derivatives do not qualify for hedge accounting, or are specifically not designated as a hedge where gains and losses on the hedging instrument and the hedged item naturally offset in the SP Group's statement of comprehensive income. These instruments include index-linked contracts and foreign exchange forward contracts. The treasury function operates on a centralised basis, where Derivatives are only used for economic hedging purposes and not as speculative investments and are classified as 'held for trading', other than

Heathrow Funding Limited

Notes to the financial statements for the year ended 31 December 2022 *continued*

7 Financial instruments *continued*

designated and effective hedging instruments, and are presented as current assets or liabilities if they are expected to be settled within 12 months after the end of the reporting period, otherwise they are classified as non-current.

The main risks arising from the SP Group's financial instruments are market risk (including fair value interest rate, foreign currency, cash flow interest rate and price risks), credit risk and liquidity risk. The Board approves prudent treasury policies for managing each of the risks which are summarised below.

Interest rate risk

The HAHL Group's policy is to maintain a mix of fixed and floating rate debt within Board approved parameters such that a minimum of 75% of existing and forecast debt is at a fixed rate. It manages its cash flow interest rate risk by using floating or fixed interest rate swaps, where at three or six-month intervals the difference between fixed contract rates and floating rate interest amounts calculated by reference to the agreed notional principal amounts are exchanged.

Financial instruments by category

The company's financial instruments as classified in the financial statements can be analysed under the following categories:

31 December 2022	**Financial assets at amortised cost and cash equivalents £m**	**Assets at fair value through statement of comprehensive income £m**	**Total £m**
Derivative financial instruments	**-**	**3,241**	**3,241**
BLA Intercompany receivables	**14,299**	**-**	**14,299**
Total financial assets	**14,299**	**3,241**	**17,540**

31 December 2022	**Liabilities at fair value through statement of comprehensive income £m**	**Other financial liabilities at amortised cost £m**	**Total £m**
Borrowings	**-**	**(14,570)**	**(14,570)**
Derivative financial instruments	**(3,253)**	**-**	**(3,253)**
Trade payables	**-**	**(1)**	**(1)**
Total financial liabilities	**(3,253)**	**(14,571)**	**(17,824)**

31 December 2021	Financial assets at amortised cost and cash equivalents £m	Assets at fair value through statement of comprehensive income £m	Total £m
Derivative financial instruments	-	2,426	2,426
BLA Intercompany receivables	14,469	-	14,469
Total financial assets	14,469	2,426	16,895

31 December 2021	Liabilities at fair value through statement of comprehensive income £m	Other financial liabilities at amortised cost £m	Total £m
Borrowings	-	(14,529)	(14,529)
Derivative financial instruments	(2,355)	-	(2,355)
Trade payables	-	(1)	(1)
Total financial liabilities	(2,355)	(14,530)	(16,885)

Heathrow Funding Limited

Notes to the financial statements for the year ended 31 December 2022 *continued*

7 Financial instruments *continued*

Fair value estimation

Financial instruments that are measured in the statement of financial position at fair value are classified by the following fair value measurement hierarchy:

- Level 1 - quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2 - inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices); and
- Level 3 - inputs for the asset or liability that are not based on observable market data (that is, unobservable inputs).

At 31 December 2022 and 2021, all fair value estimates on derivative financial instruments are included in level 2.

The fair value of financial instruments traded in active markets is based on quoted market prices at the reporting date. A market is regarded as active if quoted prices are readily and regularly available from an exchange, dealer, broker, industry group, pricing service, or regulatory agency, and those prices represent actual and regularly occurring market transactions on an arm's length basis. The quoted market price used for financial assets held by the SP Group is the current bid price. These instruments are included in level 1.

The fair value of financial instruments that are not traded in an active market (such as derivatives) is determined by using valuation techniques. These valuation techniques maximise the use of observable market data where it is available. If all significant inputs required to fair value an instrument are observable, the instrument is included in level 2.

If one or more of the significant inputs is not based on observable market data, the instrument is included in level 3.

Specific valuation techniques and inputs used to value financial instruments include:

- quoted market prices or dealer quotes for similar instruments;
- applicable market-quoted swap yield curves adjusted for relevant basis and credit default spreads;
- the recovery rate and associated reduction in credit risk of super senior ranking derivatives (interest rate and index-linked swaps);
- the fair value of derivatives and certain financial instruments are calculated as the present value of the estimated future cash flows based on observable market inputs such as RPI and CDS curves; and
- other techniques, such as discounted cash flow analysis, are used to determine fair value for the remaining financial instruments.

At the restructuring date or initial date of recognition of index-linked swaps, the fair value of these instruments, as indicated by their fair value immediately prior to the restructuring or at initial recognition, could not be supported by observable inputs alone. These fair values are supported by unobservable factors including the counterparty's credit, capital, funding and trading charges. Therefore, such movement was deferred on the balance sheet in compliance with IFRS.

As at 31 December 2022, £13 million (2021: £15 million) remained capitalised and £2 million (2021: £2 million) had been recognised in the statement of comprehensive income for the period.

On a semi-annual basis, the SP Group reviews any material changes to the valuation techniques and market data inputs used. The potential impact to the fair value hierarchy is assessed if it is deemed a transfer. Significant transfers between levels are considered effective at the end of the reporting period. During the year there were no transfers between the levels in the fair value hierarchy.

Heathrow Funding Limited

Notes to the financial statements for the year ended 31 December 2022 *continued*

7 Financial instruments *continued*

Fair value estimation *continued*

The tables below present the company's assets and liabilities that are measured at fair value as at 31 December:

31 December 2022	**Level 1 £m**	**Level 2 £m**	**Level 3 £m**	**Total £m**
Assets				
Assets at fair value through statement of comprehensive income	**-**	**3,241**	**-**	**3,241**
Total assets	**-**	**3,241**	**-**	**3,241**
Liabilities				
Liabilities at fair value through statement of comprehensive income	**-**	**(3,253)**	**-**	**(3,253)**
Total liabilities	**-**	**(3,253)**	**-**	**(3,253)**

31 December 2021	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Assets				
Assets at fair value through statement of comprehensive income	-	2,426	-	2,426
Total assets	-	2,426	-	2,426
Liabilities				
Liabilities at fair value through statement of comprehensive income	-	(2,355)	-	(2,355)
Total liabilities	-	(2,355)	-	(2,355)

8 Trade and other payables

	31 December 2022 £m	31 December 2021 £m
Current		
Amounts owed to group undertakings – non interest bearing	**1**	1
Trade and other payables	**1**	1

9 Share capital

	£
Authorised	
At 1 January and 31 December 2022	
Unlimited number of shares with no par value of one class, designated as ordinary shares	-
Called up, allotted and fully paid	
At 1 January and 31 December 2022	
2 no par value ordinary shares of £1 each	**2**

10 Ultimate parent undertaking

The immediate parent undertaking of the Company is Heathrow (SP) Limited, a company registered in England and Wales.

The ultimate parent entity is FGP Topco Limited, which is the parent undertaking of the largest group to consolidate these financial statements. The shareholders of FGP Topco Limited all hold ordinary shares in the following proportion; Hubco Netherlands B.V. (25.00%) (an indirect subsidiary of Ferrovial, S.A., Spain), Qatar Holding Aviation (20.00%) (a wholly-owned subsidiary of Qatar Holding LLC), Caisse de dépôt et placement du Québec (12.62%), Baker Street Investment Pte Ltd (11.20%) (an investment vehicle of GIC), QS Airports UK,L.P (11.18%) (through its general partner, ART Asset Operations Limited)*, Stable Investment Corporation (10.00%) (an investment vehicle of the China Investment Corporation) and USS Buzzard Limited (10.00%) (wholly-owned by the Universities Superannuation Scheme).

* The general partner of QS Airports UK, LP changed from Eagle Airports General Partner 2, Limited, an entity controlled by Alinda Capital Partners, to ART Asset Operations Limited with effect from 27 May 2023.

The Company's results are also included in the audited consolidated financial statements of Heathrow (SP) Limited for the year ended 31 December 2022, which is the parent undertaking of the smallest group to consolidate these financial statements. They are also included in the audited consolidated financial statements of Heathrow Finance plc, Heathrow Airport Holdings Limited and FGP Topco Limited for the year ended 31 December 2022.

Copies of the financial statements of FGP Topco Limited, Heathrow Airport Holdings Limited, Heathrow Finance plc and Heathrow (SP) Limited may be obtained by writing to the Company Secretarial Department at The Compass Centre, Nelson Road, Hounslow, Middlesex, TW6 2GW. This is the registered office for the smallest and the largest undertaking to consolidate these financial statements.

11 Subsequent events

In March 2023, both Fitch and Standard and Poor ('S&P') affirmed Heathrow Fundings' Class A and Class B debt ratings from negative to stable.