

Heathrow Airport – Property Rents 2020/21 and proposal for immediate years following Covid 19 crisis

Decision Document

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Prepared by: Heathrow Airport Limited

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1.0 Introduction and Consultation Programme

Purpose

- 1.1 Heathrow Airport Limited (Heathrow) has reviewed Property Rental Guide Prices in respect of the following which have been the subject of recent consultation.
- 1.2 **Part 1** - Heathrow Property Rents 2020/21
- 1.3 **Part 2** – Approach for determining Heathrow Property rents in years subsequent to 2020/21 where impacted by the continuing effect of the Covid 19 pandemic.
- 1.4 The purpose of this document is to set out Heathrow's decision.

Background

- 1.5 Since 1996 Heathrow has had a list of published Guide Prices. The Guide Prices are either a band or spot rent for most standard property products.
- 1.6 Since 1996, Guide Prices have been adjusted by the percentage change in a rental formula applied annually to the Guide Prices which was previously consulted upon. In further consultation with the AOC Rents Group the tariff rents were simplified in 2008 and the formula has evolved since it was first introduced.
- 1.7 The components of the current formula, revised in 2002 using data as at December in the year prior, are as follows:
 - Passenger Numbers.
 - Retail Price Index.
 - Investment Property Databank (IPD) Annual Property Index – the average of Central, Outer and West of London Office Indices.
- 1.8 The formula gives equal weighting to each component.
- 1.9 The formula seeks to provide consistent growth flattening the peaks and troughs associated with the external property market.
- 1.10 The 2020/21 consultation sought views on the 2 separate parts identified in section 1 above.

Consultation Programme

- 1.11 The consultation was launched on 22 February 2021 with the publication of the Consultation Document. An open consultation meeting was held via a Microsoft Teams call on 24 March 2021 to seek feedback on the proposals.
- 1.12 The consultation document has been available on the Heathrow website. Heathrow communicated the consultation document and an invitation to a consultation meeting to property users and the AOC via an e-mail communication sent out on 22nd February 2021.

1.13 The Consultation programme followed by Heathrow was:

Date	Milestone
22nd February 2021	Heathrow publish consultation document on 2020/21 rental proposals and approach to be adopted to deal with the effects of the Covid 19 crisis
24th March 2021	Consultation meeting via Microsoft Teams call
26 th April 2021	Property customer written responses due
Week commencing 3 rd May 2021	Heathrow target to publish - Part 1 - 2020/21 rents effective from 1 st April 2020 and Part 2 - Rental approach for the years that follow where impacted by Covid 19

Further Information

1.14 This document informs all users of Heathrow's decision and concludes this Consultation on Heathrow Property Guide Price Rents 2020/21 and proposal for immediate years following Covid 19 crisis.

1.15 If you have any questions on the decision, please contact:

E-mail: property@heathrow.com

2.0 Review of Responses and Decision

2.1 The comments received during the consultation meeting held on 24 March 2021 are set out in the minutes, including a list of attendees, attached at Appendix 1. The comments/representations received into the property mailbox constituted 2 responses – one from Nigel Wicking Chief Executive Heathrow AOC Limited providing the response of the AOC/AOC Property Board formally confirming the issues and request made at the consultation meeting and providing further explanation on the rationale; and a further mail from Clive Redding Director Lambert Smith Hampton confirming on behalf of himself and Sarah Kelley that the proposal put forward via the AOC letter were also supported by dnata and Virgin Atlantic, Menzies Aviation, Global Baggage Solutions and Rushlift.

2.2 The comments received focussed on Part 1 of the proposals in respect of the implementation of the formula driven increase of 1.33% for 2020/21 which would have been effective from 1st April 2020. The requests were for Guide Price rates to be held at the existing level set and established previously for 2019/20.

2.3 Other than the fact that Rent Guide Prices should be held at 2019/20 rates [as opposed to formula calculated 2020/21 rates] no further representations were received in having any direct bearing on proposals made under Part 2 for holding Guide Prices and banking any initial formulaic fall pending a net increase based on the cumulative level of guide prices (off a 2001 base).

- 2.4 On consideration of these representations and in taking into account both Parts 1 and 2 of the proposals, the detrimental effect on the airport community of the Covid 19 crisis and the overall need for stability and an equitable solution during the initial downturn and recovery Heathrow's decision is to leave Guide prices at existing levels established and set for the year 2019/20. Guide prices will be frozen/held at these levels pending an increase becoming due as determined by an increase in the cumulative rent levels off a 2001 base being apparent.

3.0 Summary of Decision

- 3.1 **Part 1** - The decision is to retain Guide Price Rents at 2019/20 levels effective from 1 April 2020. Following consultation Heathrow will not implement the formula generated increased in Guide Price Rents initially proposed for 2020/21 and will hold Guide price rents at 2019/20 levels.
- 3.2 A full schedule of the rents is attached at Appendix 2.
- 3.3 **Part 2** - The decision is to hold Guide Price Rents at 2019/20 levels banking an anticipated formulaic reduction caused largely by the Covid 19 pandemic effect on passenger numbers at the Airport until such a time as the formula produces a net increase based on the cumulative level of guide prices (off a 2001 base) above these rates.

4.0 Implementation Timescale

- 4.1 The 2019/20 Guide Prices are already in effect having previously been applied from 1st April 2019 and will continue to be implemented for any property rental transactions effective from this date.
- 4.2 Whilst Guide prices remain held at 2019/20 levels Heathrow will keep the Property AOC advised on an annual basis of the output of the cumulative formula calculation based on the established input data set into the Guide price formula. When a net increase above 2019/20 Guide Price levels is proposed in line with above Heathrow will at that point again consult as usual with the wider airport tenant community on the proposals.

5.0 List of Respondents

- 5.1 Responses were made during the consultation meeting, specific comments came from, or on behalf of:

Heathrow Property AOC also authorised to represent Virgin, British Airways, United Airlines, Cathay Pacific, SAS, Emirates and DNATA & Menzies

British Airways

Lambert Smith Hampton

Appendix 1 – Guide Price Rents 2020/21 Consultation Meeting Minutes

Meeting subject: Heathrow Guide Price Rents 2020/21 Consultation Meeting

Meeting location: Online Microsoft teams meeting

Date/Time: 24 March 2021 10:00 – 11:30 hours

Present:

Gavin Wilson (GW)	Heathrow Airport Ltd
Chris Fenwick (CF)	Heathrow Airport Ltd
Clive Redding (CR)	LSH - Heathrow Property AOC
Steve Barnes (SB)	British Airways/Heathrow Property AOC
Nigel Wicking (NW)	Heathrow AOC
Sarah Kelley (SK)	LSH – Menzies, GBS
Annabel Oakley (AO)	Cushman & Wakefield for British Airways
Hugo Watts (HW)	Knight Frank for Metropolitan Police Service
Joanne Thomas (JT)	ICM Technics
Mario Bergonzi (MB)	Alitalia
Kristina Panayotova (KP)	Bulgaria Air
Robert Baker (RB)	Cobalt

GW opened the meeting and welcomed everyone to the 2020/21 Rents Consultation and provided a general introduction and overview of meeting format

All attendees gave a brief introduction of themselves

CR as chair of the Heathrow Property AOC confirmed that he, NW & SB where authorised to speak on behalf of Virgin, BA, United, Cathay, SAS and Emirates as well as handling agent clients DNATA & Menzies.

CF presented a slide deck as a summary of the main issues under consultation which (at request of SB) was circulated by E Mail to attendees after the meeting.

AGENDA ITEMS:

- Overview
- Consultation Timetable
- **Part 1** - 2020/21 - application of Guide price Formula
- Guide Price Change
- **Part 2** - Covid 19 effect and anticipated issues with formula application.
- Issues posed by existing formula

- Proposal for approach to determining Heathrow Property rents

1. Overview

CF gave an overview of the consultation, outlining that owing to the unprecedented circumstances posed by Covid 19 and the effect on the Airport the consultation would this time be in 2 distinct parts –

Part 1 being the usual annual Guide Price review in line with the established agreed formula for 2020/21 to set rents effective 01/04/2020 and

Part 2 to address the dramatic effects of the initial Impact of Covid 19 in 2020 and anticipated ongoing effect of the pandemic and recovery, particularly in respect of passenger numbers (being one of the three data set inputs) creating the potential for disruption, instability and further unanticipated anomalies. The aim was to agree the basis and mechanism for reviewing Guide Price Rents during this period to give certainty of approach and stability to rents at the Airport.

2. Timetable

CF confirmed the consultation started on 22nd February 2021 with Heathrow Property publishing on the Heathrow website and circulating the Consultation Document. The closing date for any written customer responses is 26th April 2021 with the aim of the outcome to be confirmed and published week commencing 3rd May 2021 effective from 1st April 2020.

3. Part 1 - 2020/21 - application of Guide price Formula

CF presented the formula that has been used to calculate the 2020/21 guide price rents using Passenger numbers (Year to December 2019), RPI (December 2019) and the Investment Property Databank (IPD) indices for Central, Outer and West London (December 2019) all to create a 'smoothed' average index increment.

The formula calculation for 2020/21 generated a +1.33% change to 2019/20 rents.

The change in guide prices over the last few years would mean the following increases for tenants on 1, 2 and 3 year rental uplift patterns:

- 1 year increase: +1.33%
- 2 year increase: +3.31%
- 3 year increase: +6.34%

It was confirmed that the 4% allowance for rents in Terminal 2 relating to the future delivery of various specific areas of infrastructure would continue to be applied for 2020/21.

A graph was presented plotting the changes in passenger numbers, RPI, IPD and the Guide Price since 2002 which illustrated the effect of the formula in plotting a steady change in rents avoiding the peaks and troughs of the off-airport property market.

4. Part 2 – Covid 19 effect and anticipated issues with formula application

CF presented a table and graph to show the potential effects on Guide Price Rents using the current established formula with forecast data assumptions. Whilst the formula was intended to smooth the effects of peaks and troughs of for example the external property market it does throw up unintended anomalies in times of significant and abrupt swings particularly when 1 of the data sets is involved – in this case the initial major decline and forecast recovery in passenger numbers.

Using Terminal 3 CIP Lounge rent levels as an example, the forecast data shows an initial fall in guide price rents of over 24% in 2021 followed by over 22% increase the following year, 14% the year after etc. culminating in Guide price rents being above 2020/21 levels by 2023/24 when the passenger number forecast (for 2022 being the input data for the formula) remain relatively low at circa 55 Million.

These swings in Guide price has the potential for major disruption to property leasing at Heathrow, potential for 2 tier markets for similar accommodation depending on when tenants/Heathrow can renew agreements and general instability.

A proposed solution was presented by way of using the same forecast data again in table and graph form but by introducing a hold/freeze in guide price levels at the proposed 2020/21 rates and banking the initial formulaic reduction until such a time as the formula produces a net increase based on the cumulative level of guide prices as compared to 2020/21 rates (off a 2001 base).

It was noted that the forecast data used in the illustrations was just that ie a forecast and in practice actual data would be used and the formula run to determine the cumulative effect on an annual basis and length during which rates would be held.

It was further noted that on 2 previous occasions in 2002/3 and 2008/9 when the formula would have produced a reduction in guide price rents (albeit a much smaller impact) a similar approach was taken to bank the reduction/hold rents at the previously established level pending a net increase.

It was proposed that this approach be agreed and implemented to provide an equitable solution and give certainty to approach for the next few years during the continued effects of the pandemic until the cumulative assessment basis provides a net increase.

5. Q & A

GW gave a brief overview/summary of the proposals and re-iterated that the issues posed by the formula for the coming years is addressed up front for clarity and aim was to find a solution that was equitable and fair for both Heathrow and tenants to enable us to move forward with stability and certainty of approach for property rents at the Airport.

GW confirmed Heathrow were happy to hear views and comments to the presentation proposals and opened up the meeting to all attendees to express views and ask any questions etc.

CR opened up the main response on behalf of AOC Property and those for whom they had authority to represent.

CR recalled that the exiting formula and approach to setting Guide Price Rents at Heathrow dates back to 1996 implemented at the request of tenants to establish a consistent and known basis of rent assessment to replace previous practice of directly linking rents to the property market and property related rental evidence.

CR advised that there was no specific mechanism to specifically diverge from the formula or deal with circumstances such as the current situation posed by the pandemic however felt that impact was being felt at the time of the effective date for the current Guide Price review (01/04/2020) and that a further increase on the current established rents (2019/20 Guide Price rates) was not a fair approach in the current climate.

CR advised that on his analysis, over the six or so years of the banking of the decrease the impact would be more fairly spread if rents were capped at 2019 levels rather than 2020. In other words there would be a more level playing field. As the proposal is to vary the process to reflect the current situation, the opportunity should be taken to make the change fairer.

CR acknowledged that tenant's agreements which provided for rent reviews/uplifts where existing rents where set prior to 2019/20 rental levels would still be subject to an increase at the relevant time where provided under such contracts to that level whilst the freezing of the rental rates is in place.

A variation to the proposals in the consultation document was therefore proposed in not implementing the 2020/21 formula uplift but retaining the level at exiting 2019/20 rates. This is the level at which they should be held pending a calculated uplift on the lines of the basis proposed.

This was the counter proposal made and one the AOC property board where happy to see implemented.

NW confirmed that he had consulted both the AOC and Airlines who were also in agreement and where supportive of the proposals subject to this counter-proposed amendment.

GW & CF thanked the CR & NW for the feedback and revision to the proposals.

Closing

GW asked for any further contributions and or proposals/comments from the remainder of the attendees when it was confirmed there where none to add.

GW thanked all for attendance and reminded participants to please submit any comments in response to the consultation in writing to the Property Mailbox by 26th April 2021

The meeting relating to the Guide price consultation was closed

END

Appendix 2 – Heathrow Rental Guide Prices 2020/21 held at existing 2019/20 levels

Heathrow Airport Rental Guide Prices - 2019/20 (Effective 1st April 2020)	2019/20			
	Rent £ sq ft per annum		Rent £ sq M per annum	
	Min	Max	Min	Max
Terminal 1				
Piers - standard ramp	£43.35	£51.32	£466.58	£552.41
Terminal 2				
CIP - T2A		£91.55		£985.41
CIP - T2B		£86.98		£936.23
T2A - Landside offices/support accom		£80.25		£863.79
T2A - Airside offices/support accom		£65.99		£710.28
T2A - Airside apron level support accom (Ramp)		£51.74		£556.90
T2B - Apron level support accom (Ramp)		£51.32		£552.41
Terminal 3				
North Wing		£69.35		£746.52
South Wing		£77.05		£829.31
East Wing		£74.56		£802.59
Departures ground floor R/O check-in		£58.96		£634.65
Departures ground floor off back corridor		£52.02		£559.89
Infill Offices		£77.05		£829.31
CIP - Departures		£86.71		£933.35
CIP - Arrivals	£82.35	£86.71	£886.36	£933.35
Piers - standard ramp	£43.35	£51.32	£466.58	£552.41
Building 820				
First and Second Floor		£61.68		£663.87
Ground Floor		£65.02		£699.86
Bays		£40.43		£435.15
D'Albiac House				
Bays		£36.39		£391.67
Offices (Outer offices)		£55.84		£601.09
Offices (Inner offices)		£54.28		£584.24
Terminal 4				
NE Extension, Balcony		£77.05		£829.31
Departures rear of check in		£58.96		£634.65
Mezzanine airside		£55.50		£597.41
Standard ramp	£43.35	£51.32	£466.58	£552.41
CIP		£86.71		£933.35
Terminal 5				
CIP - T5A		£95.36		£1,026.47
CIP - T5B/C		£90.60		£975.24
T5A - Landside offices/support accom		£83.59		£899.79
T5A - Airside offices/support accom		£68.74		£739.88
T5A - Airside apron level support accom (Ramp)		£53.89		£580.10
T5B/C - Airside offices/support accom		£65.47		£704.71
T5B/C - Apron level support accom (Ramp)		£52.61		£566.26
Desk Frontage Rates - All Terminals				
Check-in		£603.83		£1,981.03
Sales and Reservation		£1,250.20		£4,101.64
Transfer		£603.83		£1,981.03
Information		£927.03		£3,041.39
Unless otherwise stated:				
The rents are exclusive of Maintenance Rent and Heating Rent or Service Charge.				
All rents (except CIP) assume measurement based on net internal area.				
A discount of 10% is given for No Natural Light, unless all the accommodation in the category has no natural light.				
Where there is a price range, actual charge will be based on the overall quality and location of accommodation.				
Typically, new build will be at the top of range.				