

Merrill Lynch European Transport Conference 2004

Speech by Mike Clasper, Chief Executive, BAA plc 10 March 2004

Good Morning,

It's a pleasure to join you at this important and timely gathering. It's nearly a year since I took over from Mike Hodgkinson as Chief Executive. A lot has happened and it's a good moment to take stock.

But I'm going to avoid the temptation to cover the whole BAA waterfront this morning. I would chiefly like to talk about the White Paper agenda and to pick up some of the points raised by Roy in his remarks.

Let me first just take a minute to set out the overall framework within which we're working at BAA.

Some of you will have heard me say before, that a great airports company does three things. This is the Holy Trinity. You need:

- To be a brilliant, day-to-day operator, 24/7.
- To select the right capital projects and manage them superbly.
- And to work constantly at refreshing the licence to grow.

The company I inherited from Mike was well set up to achieve this focus. Mike dumped the things we should never have got into and recognised that we're an airports company.

Very largely, we're a UK airports company, though over time, where we can find opportunities overseas in airport operation and airport retail, and where we can earn good returns from our expertise, without making significant capital commitments, we'll play. We'll grow international, but it will remain very modest in scale against the rest of the group.

In the last year, I've been hard at work in the three core zones. I'm not going to say any more now about day to day operations, but we have an agenda for change across retail, security, maintenance and customer service which will, over time, manage our cost base more tightly and, through innovation, grow our revenues.

On existing capital projects, we've been vigorous managers of the programme. Terminal 5 is on budget and nicely ahead of schedule. And we've agreed with BA the accelerated, one-stage occupation of the terminal in 2008.

At the same time, we've also developed a more effective plan to refresh and re-organise the Central Terminal Area at Heathrow.

Taken together, these initiatives promise real benefits for BAA, in terms of greater operational efficiency, accelerated passenger growth and diminished congestion, which is good for net retail income per passenger.

The hallmark of our approach is to combine innovation with discipline and drive. This is how we'll approach the capital programme which arises out of December's White Paper.

Before I talk about the development programmes for Stansted and Heathrow in more detail, let me just say, since this is the first speech I've given since the publication of the White Paper, that I believe the Government did a very good job.

Alistair Darling has given us a balanced policy framework, which takes a realistic view of the next two to three decades and gives the UK aviation industry an opportunity to build on its strengths.

But it's wrong to say, as some have, that this White Paper simply gave in to industry demands and ignored environmental and social imperatives.

The policy sets unyielding standards on air quality, which at Heathrow present a major challenge. But that's as it should be. No-one in our industry should accept that our future depends upon having people breathe air which is not safe to breathe.

Equally, in specifying emissions trading as the route through which aviation can pay for its contribution to climate change, the Government has chosen the right path.

But following it will take real determination and imagination, by airlines, airport operators and governments all over the world, including the United States.

It's only in this context that we will be allowed to plan and deliver additional airport infrastructure in South East England. We have to keep public and parliamentary opinion on our side.

Our intention, on the basis of the White Paper, is to get on and build a second runway at Stansted, with the aim of meeting the Government's target to complete the first phase of the project inside a decade.

At the same time, we're at work with the Government, airlines and others on addressing the air quality issues at Heathrow. I expect this work to lead, in due course, to the construction of a third runway at Heathrow.

But first Stansted. We have called this project Stansted Generation 2 because we think that it will take what is already Europe's fastest growing major airport into a quite different league.

Our starting point is that we will abide by the underlying principles set out by the Government, after extensive consultation, in the White Paper. Our reading of the White Paper suggests the following key principles:

- The first new runway in the South East will be at Stansted

- It will be delivered as soon as possible, against a very challenging target set by the Government.
- The runway will be wide-spaced, as set out in the White Paper. Page 117 to be precise.
- The enlarged airport will be designed for point-to-point operation, not as a hub.
- We will, as the White Paper demands, work to safeguard the character of the area around the airport to the maximum extent possible. This is consistent with our vision of a sustainable UK aviation industry.
- We will make a proportionate and fair contribution to surface access schemes which support the airport's expansion and which themselves represent good value for money.

In getting from these underlying principles set out by the Government to a detailed plan, BAA will talk in detail to the many stakeholders involved, including the Stansted airlines, most of which are low-cost carriers. In the light of conversations which have already taken place, with airlines and other stakeholders, I would expect the following principles to be reflected in our planning brief:

- The new terminal will be designed to achieve the best balance between functionality and cost, therefore leading to best value for money for the airport's users.
- It will be designed in modules, to allow phased construction and so enabling capacity to match demand as closely as possible.
- It will be configured to allow quick turnarounds. This means keeping coaching to a minimum, but may, as a result, involve significant walking distances.
- The layout of the new facilities will offer quick access between runways and stands.
- We will design the lay-out on scenarios which reflect Stansted's position as a base primarily for low-cost carriers. But we will also need to cater for likely future traffic mix. For example, we will wish to safeguard for the possible emergence of low-cost long-haul services, such as those which may be feasible using the Boeing 7E7 or the new generation Airbus, the A330.
- There will be minimal back office accommodation and privileged access lounges.
- Retail will be provided at a level to support the financial case for airport development, but not to add net cost to aeronautical charges.

These are principles, not statements of hard detail. Our dialogue with the Stansted airlines will intensify as the planning process unfolds. These airlines are not known to be shy about telling us what they think. I sometimes think I can hear Michael (O'Leary) when he's in Dublin, I'm in London and neither of us is on the phone.

The business case for Stansted Generation 2 rests upon three assumptions:

- That traffic at the airport will continue to grow, broadly as envisaged in the Government's own projections.
- That, as a result, Stansted will be able to raise its charges to the level permitted by the regulatory ceiling set for the present five-year period, 2003-2008. Existing discounts are being unwound and this process will be complete by March 2007.
- And that, in the next five-year settlement, 2008-2013, the CAA and the Competition Commission will agree to remunerate satisfactorily the first phase of the Stansted G2 project, which could just be operational at the back end of that period.

I am personally confident that these assumptions are well-based and that the first phase of the runway project will proceed broadly on the time-scale the Government envisages. That is why we are pushing on vigorously with the Stansted project today.

However, if circumstances turn out very differently, we will have to adjust our plans. BAA will not ask its shareholders and lenders to support any project for which there is no sound business case.

Just after the White Paper, there was much comment in the press and elsewhere about whether the Stansted runway project would require “system pricing” or “cross subsidy” by users of other BAA airports in the South East.

The CAA’s policy, as you’ve heard from Roy, is that our South East airports should be run and regulated on a stand-alone basis. I accept that we must work within the CAA’s policy framework, as we must also operate within the broader policy framework of the more recent Air Transport White Paper.

And, as Roy has acknowledged, the CAA’s 2003 price settlement stated that BAA has the right to contest the the standalone approach if “compelling reasons” arise.

It is far too early to say whether such compelling reasons exist or are likely to exist. We will not know the answer to that for some years.

If we think the reasons are compelling, it will be BAA’s duty to argue the case. For the present, there really isn’t anything to add.

At Stansted, we’ve made a good start to a demanding work programme. We hope to appoint architects and other consultants within the next couple of months. We have already set out for the local community our approach to dealing with blight.

At Heathrow, we are busy with a number of tasks. The Government is leading a work programme on air quality, in which we will play a central role. I believe that with the right level of co-operation across Government, the aviation industry and the motor industry, we have a good chance of solving the air quality issue at Heathrow.

The White Paper also gave us the opportunity to explore the potential for greater use of our two existing runways at Heathrow: for example, by introducing mixed mode operation.

This will require close dialogue with airlines, NATS and local stakeholders to understand the benefits and impacts involved, both within the existing air traffic movement limit and beyond it.

If the case is made for an increase in the air traffic movement limit, it would require planning approval, not to mention compliance with air quality thresholds.

In these circumstances, it is too early to start thinking about detailed design work for a third runway at Heathrow.

But we will, in the context of drawing up master plans for all our airports (as required by the White Paper) be moving in the course of the next year to define in outline the land-take of a third runway and associated facilities. Again, we're doing all this on the basis of close consultation with airlines and with our local stakeholders.

There are many other challenges: not least ensuring that we get the right rate of progress on surface access issues.

The White Paper represents a large work programme for BAA, but one which by extending our licence to grow underpins the future growth and success of the company.

Are we biting off more than we can chew? I don't think so. The Government has given those of us who hold leadership positions in the aviation industry the chance to deliver what we've spent so many years saying we must have.

And as I said at the beginning, BAA today is a well focused organisation, fully capable of delivering what is needed.

This is a historic opportunity and we intend to take it.

Thank you.