



Governance, Privatization and Impacts

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- ❑ Objective: Review the evolution of airport governance arrangements with emphasis on the privatization trend and its impacts
- ❑ Outline
 - Changing governance practices
 - Trend toward privatization
 - Reasons for privatizing
 - Resultant “models” of ownership and management
 - Advantages and disadvantages of privatization
 - Government regulation
 - Elements of privatization agreements
 - Quality of service regulation

The Past (to the 1990s)

- ❑ Airports were owned by national, regional or local government and managed either by government organizations or by independent, government-owned Airport Authorities
- ❑ Often heavily subsidized by national governments, especially with respect to capital costs
- ❑ Essentially not-for-profit organizations, with principal aim to provide infrastructure for air travel
- ❑ Change began in the 1980s
 - Growing commercialization of some airports
 - BAA privatization (1986)

The Present

❑ Dramatic restructuring of airports as an “industry” in 25 years

1. **Commercialization**: Emphasis on commercial activities that greatly increase airport revenues; from “public utility” to “commercial enterprise”.

2. **Privatization**: Transfer of ownership (or management) to private sector.

- Share flotations
- Private management contracts
- Outright sales to private or public-private partnerships

3. **Diversification of ownership**

- Financial institutions and investors
- Construction/infrastructure companies
- Operators of other airports
- Pension funds, airlines, various others

Factors Contributing to Privatization Trend

- ❑ The economic results of some publicly-owned airports that emphasized commercialization in the 1980s indicated that the airport industry held great potential for private investors
- ❑ Need for airport management to react quickly and flexibly to rapid change in the airline industry (privatization, mergers)
- ❑ Airports became “mature” as economic entities and no longer required government subsidies to survive
- ❑ For several reasons, governments have become increasingly reluctant to allocate large amounts of public funds to capital expenditures at busy airports

What is “Privatization”?

- ❑ **Privatization**: the transfer of partial or full **ownership** to private organizations
- ❑ A more “liberal” definition includes “transfer of **management** to private organizations”
- ❑ The term “**corporatization**” is often used to refer to a restructuring of public organizations into corporate entities that introduce business management techniques to their administration.
- ❑ The typical result of corporatization is the creation of state-owned corporations where the **government retains a majority ownership** of the corporation's stock.

Airport Privatization Trend

- ❑ Natural evolution from earlier commercialization trend
- ❑ Growing private participation in airport ownership [about 300 privatized airports world-wide as of 2014]
- ❑ Equally important, private-sector management practices are replacing traditional government-style management in an environment demanding economic self-sufficiency
- ❑ Trend toward “outsourcing” of airport activities, lean airport organizations (“US model”)
- ❑ *Accompanied by improved understanding of need for regulatory safeguards to protect public interest and prevent monopolistic practices*

Types of Privatization

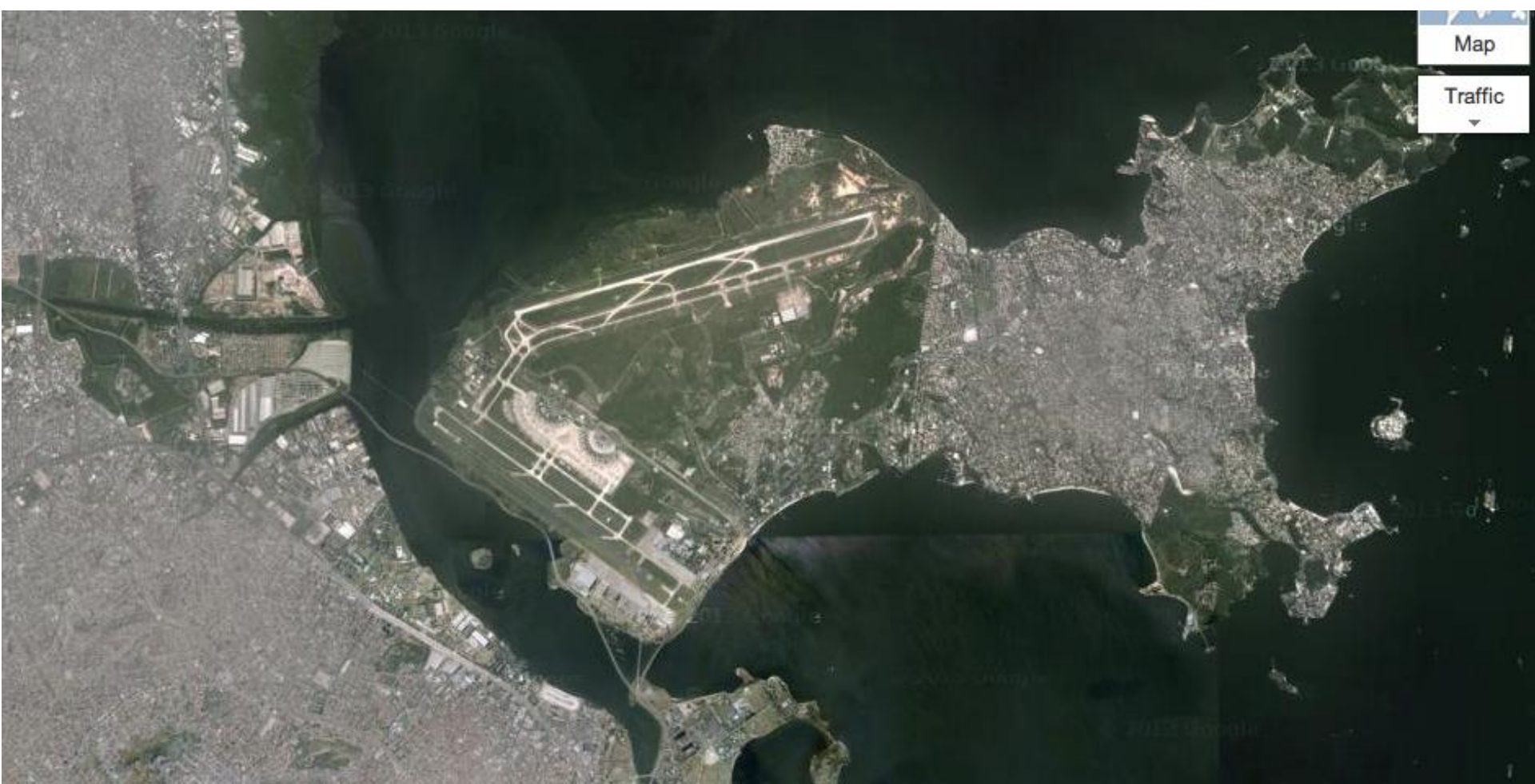
- ❑ **Share flotation:** initial public offering (IPO) with shares issued and traded on stock exchanges (BAA - 100%, Vienna - 27, Zurich - 22, Auckland - 52, AdP - 28, etc.)
- ❑ **Trade sale:** Sale of all or part of the airport through a public tender (many UK airports – 51-100%, Dusseldorf – 50, Australia excluding Sydney – 100, Hanover – 30, etc.)
- ❑ **Concession:** Sale of lease to operate airport for a defined period (20 – 40 yrs), usually through public tender, ROT-rehabilitate-operate-transfer (Argentinean Airport System, Santo Domingo, Antalya, Izmir, St. Petersburg, Zagreb)
- ❑ **Project finance:** BOT – build-operate-transfer agreement (20 – 40 yrs) with private group or PPP (public-private-partnership) (Athens, Izmir, Manila, Amman, Tirana)
- ❑ **Management contract:** Assign responsibility for operating airport (Cairo, Riyadh, Bahamas, Algeria)

Brazilian Privatization (2012)

	Pax (mio) 2011	Cargo (000) Tonne s 2011	Revenue (\$ mio) 2011	Concession conditions	Winning bid
Sao Paulo Guarulhos	27	431	\$450	20 yrs; Min bid: \$2 billion; 10% of gross revenue per yr; Investment req'd: \$2.7 billion	ACSA (S. Africa) + Invepar (Brazil) + OAS (Brazil) \$9.4 billion
Sao Paulo Viracopos Campinas	5	258	\$150	30 yrs; \$870 million; 5%; \$5 billion	Egis (France) + Triunfo (Br) \$2.2 billion
Brasilia	14	3	\$75	25 yrs; \$340 million 2%; \$1.6 billion	Corporacion America (Arg) + Engevix (Br) \$2.6 billion

Source: Graham (2014)

Rio de Janeiro/Galeão–Antonio Carlos Jobim (GIG)



2013: 25-year concession to consortium of Oderbrecht (Br, 60%) and Changi Airport (Sin, 40%); ~\$8 billion for 51% share; forecast: 175% growth in 15 yrs (~7.5/year); ~17.5 mio pax in 2012

Forms of Ownership and Management

- A. Government-owned; operated by Department or Agency of national government
- B. Government-owned; operated by a municipal or regional Department or Agency
- C. Government-owned, possibly with some private participation; operated and managed by a contractor
- D. Operated by an autonomous Airport Authority, fully owned by municipal and/or regional and/or national government
- E. As in 'D' but with minority private shareholders (some shares may be publicly traded)
- F. Privately-owned (fully or in majority, possibly with some or all shares publicly traded); operated as autonomous airport authority

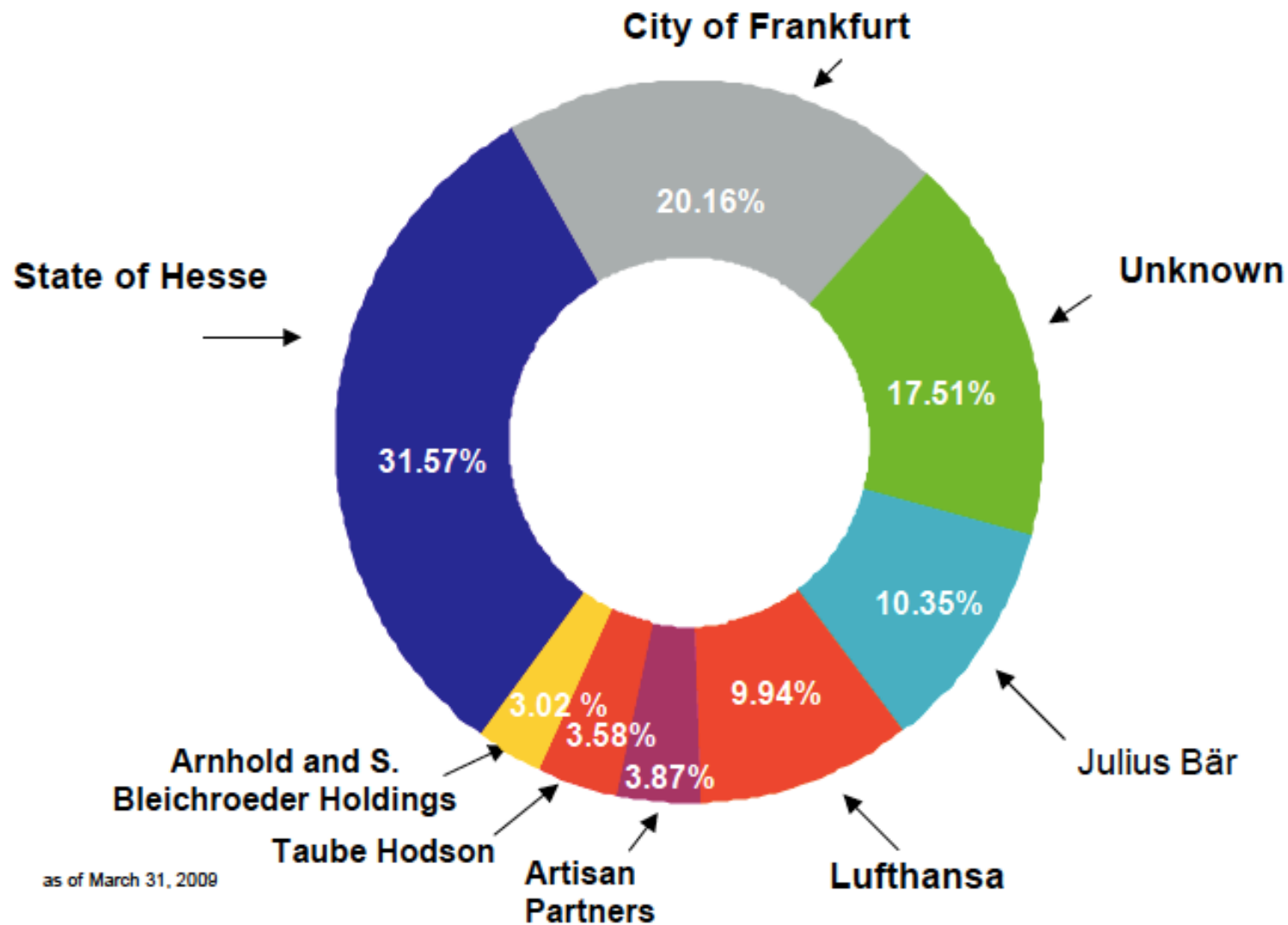
Typical Provisions for Type D Airports in US

- ❑ Board of Directors appointed by shareholders
- ❑ Often tax exempt or privileged tax status
- ❑ Authorized to acquire land via “eminent domain”
- ❑ Authorized to undertake construction, manage the airport, and be responsible for all services
- ❑ Authorized to issue tax-exempt revenue bonds
- ❑ Typically expected to be economically self-supporting; authorized to adjust user charges to this effect
- ❑ Can make “contributions” to owner in lieu of taxes
- ❑ Possibly also operate other infrastructure (e.g., seaports, bridges, tunnels, etc.)
- ❑ All property reverts to owner if Authority is dissolved

Ownership and Management of Airports: Comments

- ❑ Tendency toward D - F as airports become busier and critical to local and national economies [40 of top 100 are in F; \$41 billion revenue in 2013]
- ❑ Many variations within categories
- ❑ “Build, operate and transfer” (BOT) or “rehabilitate, operate and transfer” (ROT) agreements are often associated with E and F
- ❑ BOT arrangements may also be made for individual facilities within an airport (e.g., terminals, car parks, etc.)
- ❑ Airport privatization decisions (E and F) are often the subject of significant political controversy

Shareholders of Fraport AG, 2009



Sample European Airports: Ownership + Operator

Airport	Type	Operator	Ownership
Amsterdam	D	Schiphol Group	Dutch Govt. 69.77%, City of Amsterdam 20.3%, City of Rotterdam 20.3%, ADP 8%
Berlin	D	Flughafen Berlin Schönefeld, GmbH	German Govt. 26%, State of Brandenburg 37%, State of Berlin 37%
Brussels	F	Brussels Airport Co.	Ontario Teachers 39%, Macquarie Fund 36%, Belgian Govt. 25%
Copenhagen	F	Copenhagen Airport	CAD ApS 57.7%, Danish Govt. 39.2%, free float 3.1%
Dublin	D	Dublin Airport Authority	Irish Govt. 100%
Frankfurt	E	Fraport AG	State of Hessen 31.5%, City of Frankfurt 20.1%, Lufthansa 9.9%, Artio Global Investors 10%, free float 28.5%
Greece (except Athens)	A	Ministry of Transport	Greek Govt. 100% [may change to F in 2015, Fraport]

Sample European Airports: Ownership + Operator

Airport	Type	Operator	Ownership
Lisbon	F	ANA	Vinci Group 100%
London Heathrow	F	Heathrow Airport Holdings, Ltd.	Ferrovial Consortium 62%, Cdp du Quebec 28%, Baker Street Investment 10%
London Gatwick	F	Gatwick Airport, Ltd.	Global Infrastructure Partners (GIP) 100%
Madrid	D	AENA	Spanish Govt. 100% [may change]
Manchester	D	Manchester Airport Group	Council of City of Manchester 55%, 9 Borough Councils 45%
Milan (Malpensa+Linate)	E	SEA	City of Milan 54.8%, F2i investment fund 44.3%, various 1%
Moscow Domodedovo	F	East Line Group	East Line Group 100%
Moscow Sheremetyevo	D	Joint Stock Company	Russian Govt. 100%
Munich	D	Flughafen München, GmbH	German Govt. 26%, State of Bavaria 51%, City of Munich 23%
Paris (Charles de Gaulle + Orly)	E	Aéroports de Paris (ADP)	French Govt. 52.4%, various institutional investors 29.1%, Schiphol Group 8%, free float 8.5%, ADP employees 2%
Prague	D	Joint Stock Company	Czech Govt. 100%

Commercialization and Away-from-Home Ventures

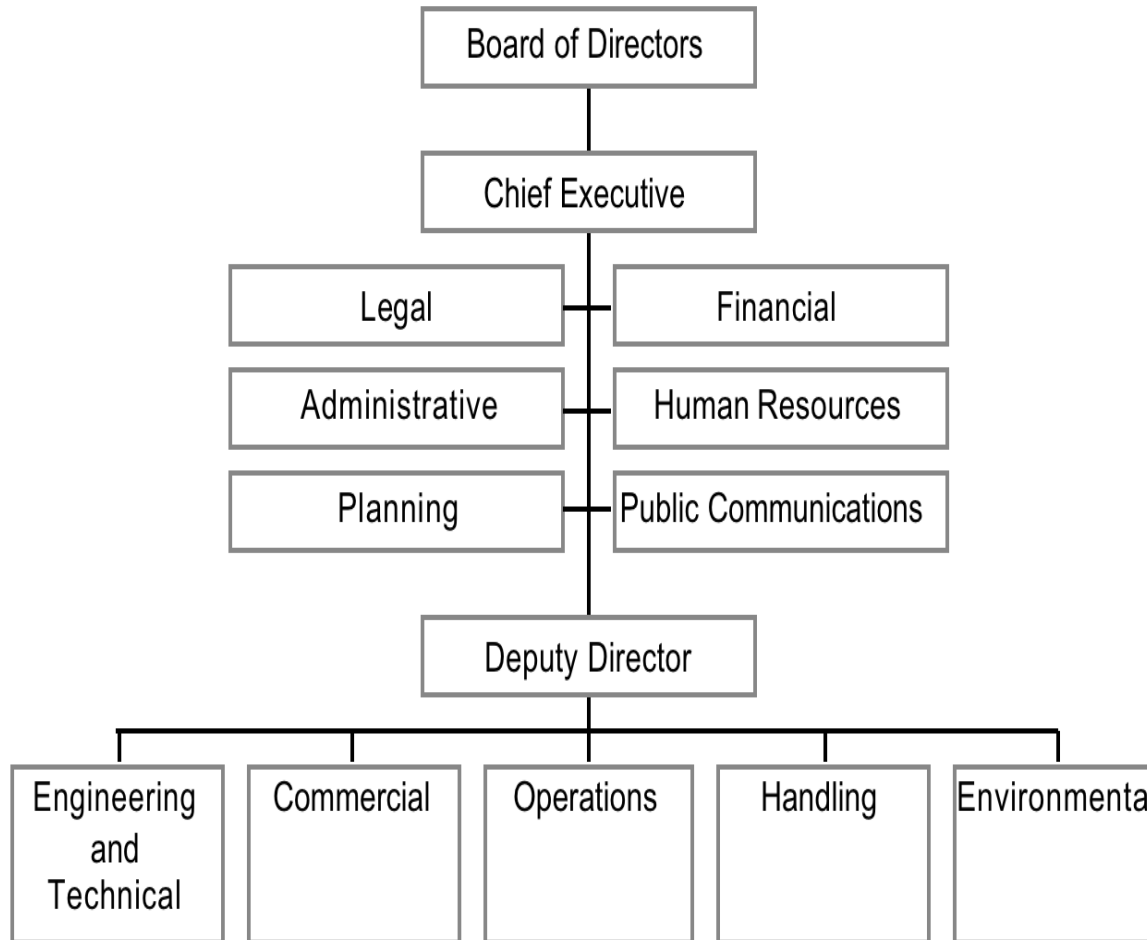
- ❑ Fast-growing non-aeronautical revenues as a result of emphasis on commercial activities and other landside services (due to growing traffic and to numbers and longer dwell times of connecting and departing passengers)
- ❑ Ventures away from home, sometimes in activities not directly related to airports (e.g., real estate)
- ❑ "Global airport operators" (Fraport -- \$500 million revenue from airports elsewhere in 2011, Vinci, TAV, Vantage, GMR, etc.)
- ❑ Evolving organizational structures reflecting these trends

Fraport's International Holdings

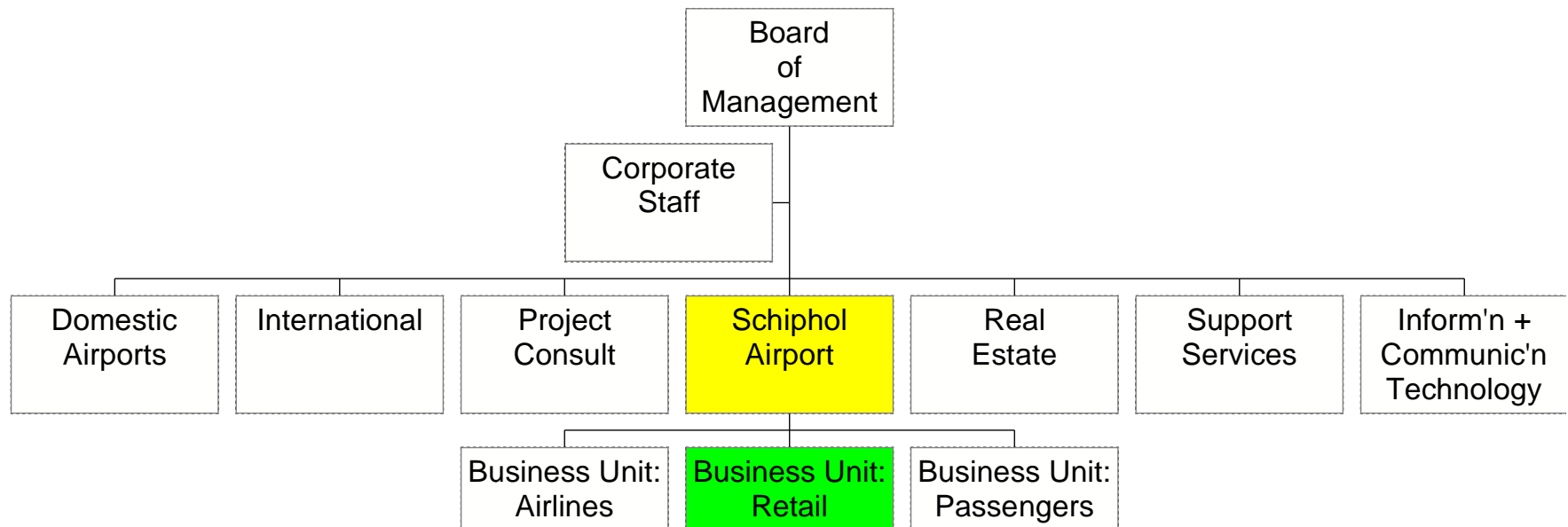
	% Share of Airport's Operator	Date of Initial Involvement	No. of pax in 2011 (millions)
Delhi	10	2006	35
Hanover	30	1998	5
Antalya	51	2007	25
Varna and Burgas	60	2006	3
Lima	100	2001	12
St. Petersburg, Pulkova	35.5	2010	10
Xi'an	24.5	2007	21

Source: Graham (2014)

Traditional 2-Tier Organizational Chart



Organizational Structure: The Amsterdam Schiphol Group



Perceived Advantages of Privatization

- q Reduced need for public investment
- q Access to commercial capital markets
- q More flexibility in tailoring financing schemes
- q Less government control and political interference
- q Private sector management may improve efficiency, increase competitiveness
- q Incentives for management and employees to perform well
- q Governments may gain financially from converting public assets and from company taxes
- q More responsiveness to change
- q Timely investments at right scale

Criticisms of Privatization

- ❑ May create a private monopoly with
 - Excessive focus on “bottom line”, overcharging for services
 - Little concern for externalities
 - Reluctance to make additional investments, especially near expiration of concession period
 - Insufficient attention to quality, level of service
- ❑ Less emphasis on public interest, overall economic effects (e.g., “high user charges” vs. “attractiveness to low-cost carriers”)
- ❑ Poor employment conditions, “extra-lean” organization
- ❑ Ownership and management teams may change during concession period, often several times

London Heathrow Holdings Ltd: History

- q 1965-86: British Airports Authority, publicly owned; owner and operator of Heathrow, Gatwick, Stansted plus Glasgow, Edinburgh, Southampton, Aberdeen
- q 1986-2006: BAA plc, 100% privately held shares, London Stock Exchange (~\$2.5 billion initial capitalization)
- q 2006: BAA Ltd, 100% of shares acquired by consortium led by Ferrovial S.A., a Spanish construction and infrastructure conglomerate (~\$20 billion); delisted from London Exchange
- q 2009: UK Competition Commission requires that BAA sell Gatwick, Stansted and either Edinburgh or Glasgow citing monopoly concerns

London Heathrow Holdings Ltd: History [2]

- ❑ 2009+: Gatwick (2009) and Edinburgh (2012) sold to Global Infrastructure Partners (GIP) and Stansted (2013) to Manchester Airports Group
- ❑ 2012: BAA → Heathrow Airport Holdings Ltd
- ❑ 2014: Announcement of intent to sell Glasgow, Southampton and Aberdeen

Shareholders: Ferrovial S.A. (25.00%), Qatar Holding LLC (20.00%), Caisse de dépôt et placement du Québec (12.62%), the Government of Singapore Investment Corporation (11.20%), Alinda Capital Partners (11.18%), China Investment Corporation (10.00%) and Universities Superannuation Scheme (10.00%)

Initial Contract: Setting the Rules

- ❑ Initial contract with (fully or partially) private Airport Operator is extremely important in setting the framework for airport development and operation and in avoiding future problems
- ❑ Typically specifies:
 - Facilities to be built, if any (what? when?)
 - Constraints on charge increases or return on investment
 - Timeline for future investments (often tied to traffic growth)
 - Quality of service (LOS) requirements
 - Management appointments
 - Reporting requirements
 - Length of concession period, conditions on renewal
 - Conditions for share trades, rights of shareholders
- ❑ Regulatory environment, monitoring mechanisms during concession period are also critical

A Recent Example (December 2015)

- ❑ 14 airports in Greece were privatized (all the main ones except Athens, which has been privatized since 1996)
- ❑ ~25 million passengers in 2015
- ❑ Fraport plus a Greek energy firm (Copelouzos)
- ❑ 40 year concession
- ❑ \$1.3 billion initial payment; annual rental fee of \$25 million; must invest \$350 million in first 4 years of concession period; consortium plans to invest \$1.4 billion during the concession period
- ❑ Some legal challenges are still pending

Government Regulation

- ❑ Because of the perceived risks associated with privatization and corporatization of airports, governments exercise:
 - Economic regulation (to be discussed in Module 20)
 - Quality of service regulation
- ❑ Practices vary widely from country to country
- ❑ Interest in quality-of-service regulation is growing
- ❑ In addition, all countries regulate and monitor compliance with safety and security requirements

Example: Regulation of Quality of Service at LHR

- ❑ Until a few years ago, London Heathrow was widely considered as one of the worst in the world, in terms of level of service
- ❑ The government regulator (Civil Aviation Authority) imposed the Service Quality Rebate Scheme (SQRS) to force LHR to achieve acceptable service standards – penalties when standards are not met
- ❑ The airport operator (Heathrow Holdings) adopted a service philosophy that emphasizes a “passenger perspective”
- ❑ The airport operator is also monitoring its progress through the ACI Airport Service Quality (ASQ) Monitoring system

LHR: Quality Control Program

- ❑ The Service Quality Rebate Scheme (SQRS) imposed on LHR by the UK's Civil Aviation Authority:
 - Identifies the service standards that airlines and passengers should expect from Heathrow in return for the regulatory charges they paid
 - If performance falls below a certain level, Heathrow must repay a proportion of charges levied back to the airlines
- ❑ SQRS provides an incentive to the airport operator to meet the specified standards of service quality
- ❑ Rebate payments are made monthly to airlines
- ❑ Maximum amount of rebates is 7% of airport charges
- ❑ Rebates are paid on performance in each individual terminal

LHR: Coverage of Quality Control Program

- q Queuing at the departures security search area, transfers security search, staff search, and security search for catering, flight crews and maintenance equipment
- q Availability of stand service for aircraft.
- q Passenger perception of availability of seating in the departures lounge, the quality of flight information systems, how easy it is to find their way around, the cleanliness of toilets and concourse areas, ease of use of wi-fi service.
- q Passenger Sensitive Equipment (PSE), which includes lifts, escalators, conveyors (moving walkways).
- q Arrivals baggage reclaim belts, fixed electrical ground power (for aircraft on stands), pre-conditioned air (for aircraft), and stand entry guidance (to assist aircraft parking).

LHR: Example of SQRS Report (T5, Jan 2015)

Heathrow Terminal 5	Jan-15				Year to date *	
	Actual	Target	Target achieved	Rebate £	Rebate £	Number of failures
Departure lounge seat availability	4.02	3.80	Yes	0	0	0
Cleanliness	4.24	4.00	Yes	0	0	0
Wayfinding	4.17	4.10	Yes	0	0	0
Flight information	4.29	4.30	No	394,470	394,470	1
Security	4.05	n/a	n/a	n/a	n/a	n/a
Wi-fi	3.89	n/a	n/a	n/a	n/a	n/a
Central security queues - Times queue <5 minutes	96.54%	95.00%	Yes	0	0	0
Central security queues - Times queue < 10 minutes	99.88%	99.00%	Yes	0	0	0
Passenger sensitive equipment (general)	99.62%	99.00%	Yes	0	0	0
Passenger sensitive equipment (priority)	99.61%	99.00%	Yes	0	0	0
Arrivals reclaim (baggage carousels)	99.86%	99.00%	Yes	0	0	0
Stands	99.88%	99.00%	Yes	0	0	0
Jetties	99.53%	99.00%	Yes	0	0	0
FEGP	99.89%	99.00%	Yes	0	0	0
Pre-conditioned air	99.88%	98.00%	Yes	0	0	0
Stand entry guidance	99.98%	99.00%	Yes	0	0	0
Transfer search	96.17%	95.00%	Yes	0	0	0
Staff search	96.16%	95.00%	Yes	0	0	0
Control posts search	97.83%	95.00%	Yes	0	0	0
Transit system - % time one car available	99.94%	99.00%	Yes	0	0	0
Transit system - % time two cars available	99.24%	97.00%	Yes	0	0	0
Total				394,470	394,470	1

The “Passenger’s Perspective”



Figure 1 What airports think about



Figure 2 What passengers think about

Source: Article by Nick Adderley (Heathrow Airport, Ltd.) in *Airport Management*, Jan-March 2012.

Current Situation re. Privatizations

- q Focus on promising primary airports
- q Secondary / regional airports typically sold/leased in groups
- q Weak prospects for sale of individual secondary/regional airports
- q Huge international investment funds (private equity/venture capital/hedge funds) increasingly dominate
- q Investors increasingly focus on airports in emerging markets where growth forecasts are significantly higher
- q Wide fluctuations in what investors will pay (many surprises)

References

- q de Neufville, R. and A. Odoni (2013) *Airport Systems: Planning, Design and Management*, 2nd Edition, McGraw-Hill Education. [Chapters 7 and 8]
- q Graham, Anne (2014) *Managing Airports: An International Perspective*, 4th Edition, Routledge Publishers. [Chapters 2 and 4]

Questions? Comments?