Airport Revenues and Charges

Objective:
– Review briefly international practices concerning airport ownership and management

Topics:
– Alternative “models” of airport ownership and management
– The privatization trend
– Examples of privatization
– Advantages and disadvantages of privatization
– Organizational structures

Reference: Chapter 7 of de Neufville and Odoni
Governance, Privatization and Impacts

Objective: Review the evolution of airport governance arrangements and the main features of the relationship between airports and airlines

Outline

– Changing governance practices, the trend toward privatization and related impacts
– Reasons for privatizing
– Resultant “models” of ownership and management
– Advantages and disadvantages
– The airline-airport relationship
– Some areas of contention between airports and airlines
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 the airports as an “industry” during the past 25 years


2. Privatization: Transfer of management and, often, of ownership 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 government and 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%, Hannover – 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)
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
- 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
<table>
<thead>
<tr>
<th>Airport (except Athens)</th>
<th>Type</th>
<th>Operator</th>
<th>Ownership</th>
</tr>
</thead>
<tbody>
<tr>
<td>Amsterdam</td>
<td>D</td>
<td>Schiphol Group</td>
<td>Dutch Govt. 69.77%, City of Amsterdam 20.3%, City of Rotterdam 20.3%, ADP 8%</td>
</tr>
<tr>
<td>Berlin</td>
<td>D</td>
<td>Flughafen Berlin Schöenefeld, GmbH</td>
<td>German Govt. 26%, State of Brandenburg 37%, State of Berlin 37%</td>
</tr>
<tr>
<td>Brussels</td>
<td>F</td>
<td>Brussels Airport Co.</td>
<td>Ontario Teachers 39%, Macquarie Fund 36%, Belgian Govt. 25%</td>
</tr>
<tr>
<td>Copenhagen</td>
<td>F</td>
<td>Copenhagen Airport</td>
<td>CAD ApS 57.7%, Danish Govt. 39.2%, free float 3.1%</td>
</tr>
<tr>
<td>Dublin</td>
<td>D</td>
<td>Dublin Airport Authority</td>
<td>Irish Govt. 100%</td>
</tr>
<tr>
<td>Frankfurt</td>
<td>E</td>
<td>Fraport AG</td>
<td>State of Hessen 31.5%, City of Frankfurt 20.1%, Lufthansa 9.9%, Artio Global Investors 10%, free float 28.5%</td>
</tr>
<tr>
<td>Greece (except Athens)</td>
<td>A</td>
<td>Ministry of Transport</td>
<td>Greek Govt. 100% [may change to F in 2015, Fraport]</td>
</tr>
</tbody>
</table>
## Sample European Airports: Ownership + Operator

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

<table>
<thead>
<tr>
<th>% Share of Airport’s Operator</th>
<th>Date of Initial Involvement</th>
<th>No. of pax in 2011 (millions)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Delhi</td>
<td>2006</td>
<td>35</td>
</tr>
<tr>
<td>Hanover</td>
<td>1998</td>
<td>5</td>
</tr>
<tr>
<td>Antalya</td>
<td>2007</td>
<td>25</td>
</tr>
<tr>
<td>Varna and Burgas</td>
<td>2006</td>
<td>3</td>
</tr>
<tr>
<td>Lima</td>
<td>2001</td>
<td>12</td>
</tr>
<tr>
<td>St. Petersburg, Pulkova</td>
<td>2010</td>
<td>10</td>
</tr>
<tr>
<td>Xi’an</td>
<td>2007</td>
<td>21</td>
</tr>
</tbody>
</table>

Source: Graham (2014)
Organizational Structure: The Amsterdam Schiphol Group

Board of Management

Corporate Staff

Domestic Airports
International
Project Consult
Schiphol Airport
Real Estate
Support Services
Inform'n + Communic'n Technology

Business Unit: Airlines
Business Unit: Retail
Business Unit: Passengers
Perceived Advantages of Privatization

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

- May create a private monopoly with
  - Excessive focus on “bottom line”, overcharging for services
  - Less 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
Setting the Rules

- Initial contract with (fully or partially) privatized Airport Operator is extremely important in setting framework for airport development and operation.

- 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.
Current Situation re. Privatizations

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