

AERO CLUB OF WASHINGTON
U.S. AVIATION POLICY: OLD SCHOOL INSTEAD OF NEW NORMAL

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Thank you... for that kind introduction.

I want to take a few minutes today to give a global perspective on some of the issues facing U.S. airports these days. It is a curious thing that the U.S., which is an aviation leader in so many ways, seems to be mired in some old-fashioned policy debates about airport governance and financing.

But, let me start by telling you a little bit about ACI, Airports Council International. We are the worldwide representative of airports, created in 1991 through the merger of two worldwide airport associations, one based in the US since 1948, one based in Europe since 1950. Our mission is to promote the collective interests of the world's airports and the communities they serve, and promote professional excellence in airport operations and management. We have 573 members operating 1751 airports in 174 countries, representing 95% of the world's passenger traffic.

ACI is comprised of six units: the World Office in Montreal, which is where I hail from and five regional offices: Africa, Asia-Pacific, which includes the Middle East, Europe, Latin-America/Caribbean and North America.

Each ACI regional office has a governing board that deals directly with the issues and regulatory bodies specific to that region, while ACI World deals with global issues and global regulatory bodies, like the International Civil Aviation Organization (ICAO) and the World Health Organization and with other international associations like the

International Air Transport Association (IATA) and the Civil Air Navigation Service Organization (CANSO). So we deal with international alphabet soups and ACI-North America deals with U.S. and Canadian alphabet soups.

Well, what's up with airports? I think most in this room appreciate that there have been and continue to be major shifts in the air transportation industry in general but I'm not sure there has been a lot of recognition about the impact of those shifts on the airport side of the industry.

Until the mid-1980s almost all international airports were owned and operated by governments, often the national government. Airports were - and still are - seen as important national assets that provide efficient access to the country and facilitate economic growth. In some instances airports were seen as facilities that operated primarily for the benefit of the government-run airline and this was often reflected in the underlying economics of the relationship between the airport and the airline.

It is only comparatively recently that airports have come to be seen as viable businesses in their own right. Marked particularly by the 1986 privatization of BAA where it was demonstrated that airports could generate value through non-aeronautical activities, airports are evolving from being simply public-sector infrastructure providers into business-oriented service providers.

What's behind this? A few key drivers.

One: the liberalization of airline markets, which started in the United States with deregulation, spread to Europe with privatization of airlines and liberalization of routes and continues to evolve as Open Skies reach more markets. As a result, airlines are more agile, in fact, downright footloose and fancy free in many parts of the world. As a result, communities compete against each other for air service and they do that through

their airports, whether the airport is publicly or privately governed. We now have airports chasing airlines for their business, and the mega-hubs competing with each other to become gateways to entire continents.

Along with liberalization, the rise of the emerging economies of the world has increased the sheer volume of the traffic. In 2012, worldwide passenger numbers reached 5.7 billion passengers.

Looking at passenger traffic by region, we see strong growth in the Middle East, Latin America, Africa and Asia while the mature markets of North America and Western Europe grew more slowly. The change in the distribution patterns is staggering.

Only ten years ago Beijing was the 33rd busiest passenger airport in the world. Today it is the second largest and on track to surpass Atlanta by 2020. The main airport serving Jakarta, Indonesia, went from 85th position in 2001 to 12th in 2012.

Eight of the world's 20 largest airports are now in emerging markets. And cargo?

Hong Kong has already unseated Memphis as the largest cargo airport in the world and four of the ten largest cargo airports are in emerging markets.

And then there is that small and sparsely populated part of the planet - the Middle East.

For years one of the quietest aviation markets in the world, this region is transforming the world aviation landscape. The driving force behind that performance is not only the new and aggressive intercontinental airlines from the Gulf countries which are truly making a mark in the international aviation scene, but also the vision of literally connecting the world through mega airport infrastructures. During the first half of last year, passenger traffic in the Middle East grew at double the rate of the second and third fastest growing markets, Africa and Asia.

This is an age where access to air transportation has become fundamental for social and economic development.

In many countries, public budgets are stretched and they have gotten creative about how to assure this access, adopting a quintessential American approach – they've turned to private investors to both raise capital to meet their airport capacity requirements as well as to participate in management and governance to improve efficiency and quality of service.

Let me be clear: ACI does not promote a specific ownership model, but it is essential to find a model that provides the ability to run an efficient, competitive business that can accommodate and drive the community's economic vitality. That includes financing airport capacity and modernization. The airport takes great risk as it tries to respond to market-driven airline demands with facilities that take years to bring into being, take even more years to pay for, cannot be moved and cannot be put to higher and better use. The airport has to get it right but yet has to design facilities that are flexible enough to respond to changes in market conditions.

All of these trends together are putting great stress on the traditional airport decision-making chain stretching up into public institutions at both local and national levels.

Unfortunately, the links with government have a tendency to **hinder** airport developments rather than help them. A variety of alternate airport ownership and governance models have emerged and proven to be successful. In many countries, governments have decided that, under the right economic conditions, they can successfully turn to the private sector for the financing and operation of airport infrastructure.

According to ACI's latest count, worldwide, 450 airports have some form of private sector participation in airport management and/or ownership.

It is in Europe where the privatization of airports has most advanced, with the UK having the highest proportion of privately owned airports worldwide. Indeed, most of the airports in Western Europe operate under some form of privatized or corporatized governance, the latter somewhat akin to the "Airport Authority" form of governance in the U.S. but without the federal legislative involvement that I will talk about in a bit.

The second most active region in terms of airport privatization is the Latin America-Caribbean region. There, airports are often operated under a concession model where, for the duration of the concession contract, typically twenty to thirty-five years, the concessionaire manages and develops the airport and tries to generate a return on its investment. From Argentina to Mexico to the Bahamas, 16 countries have adopted the airport concession model for their airports. In the Asia Pacific Region, airports are predominantly run by government entities albeit often corporatized like in the U.S and Canada.

However, it is worth pointing out that Asia, and China in particular, has the highest number of airport companies under partial private ownership through stock market listings, including Beijing and Shanghai Airports. It also has direct foreign investment, with Frankfurt Airport for example holding a 24.5% stake in the management company that runs Xi'an Airport. Currently, twenty-five airport companies are listed on stock exchanges worldwide, of which five companies are Chinese, three are Mexican and two are from Southeast Asia, with the balance of airport companies being in Australasia and Europe.

Of course there are good reasons for this, but it is also a reflection of the fact that we live in a globalized economy where new paradigms are the order of the day and almost anything is possible. Indeed, the airport world is a global business, where teacher pension funds from Canada own airports in Australia and Australian companies own airports in the United Kingdom, while Indian and South African companies bid for airports in Brazil. This is the state of play.

When you look at the United States, despite its public sector facing considerable financial difficulties, the way of funding airport infrastructure has not changed for decades, and the role of the Federal Government has not changed either. In other parts of the world airports have more flexibility and freedom to finance their expansion. In particular, worldwide most airports are heavily dependent on mechanisms like the passenger facility charge. Indeed, passenger facility charges represent the largest proportion of revenue for world airports. Even just looking at charges for aeronautical services, airports derive a higher proportion of their revenue from passenger facility charges than from landing fees on airlines, and the rates are generally set on the basis of the actual funding requirements.

The airports that are consistently ranked by passengers as the best in the world: Singapore, Beijing, Hong Kong, all use the passenger facility charge to finance airport development.

Earlier, we made reference to international airlines reshaping the world aviation map. Their success is not only due to government policy but to those countries being open to the use of modern financing approaches to fund investment in their airports. What Emirates is doing in Dubai or what Turkish Airlines is doing in Istanbul, would not be

possible if their hub was LAX or JFK. The massive expansion of service and market reach of these airlines is enabled by the expansion of airport capacity.

In North America, airports have an annual payroll of \$365 billion a year and are responsible for more than 10 million jobs. Industry connected activity represents 7% of overall employment and 8.0% of GDP per annum. Airports are responsible for \$1.2 trillion dollars of economic activity; if airports were a single company, they would be the nation's second largest employer, just behind Wal-Mart.

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For years, the US has led the aviation world in terms of innovation and infrastructure investment. Where is the grand plan for building the airport capacity that the US will need to keep connected to growing economies such as China, India, Brazil? The US needs to think much bigger and more strategically about how to provide this country's airports the ability to make the investments necessary to compete in a global industry.

I would urge the U.S. not to blow its lead. Thank you.
