ACI EUROPE ECONOMICS REPORT 2015

ACI EUROPE
AIRPORTS COUNCIL INTERNATIONAL



CONTENTS

Business Context
Revenues
Costs
Revenues & Costs
Investment
Profitability

BUSINESS CONTEXT: Strong passenger growth in 2014, in spite of weaker underlying economic conditions and continued cautious deployment of airline capacity.

REVENUES: Minor increases in revenues from airport charges in 2014 undermined by stagnant revenues from non-aeronautical activities, with decreases in revenues from advertising, property rental and car hire concessions.

COSTS: Reduced total costs in 2014 reflected a minor decrease in capital costs and the continued reduction of operating costs.

REVENUES & COSTS: Airports continued to cover their cost base with a diverse range of revenues in 2014. Revenues from airport charges covering only approximately two thirds of overall costs, leaving a shortfall of circa €10 billion which had to be covered by other means.

INVESTMENT: Actual capital expenditure below what was initially forecast for 2014 – however airports forecast higher investment in the medium term.

PROFITABILITY: Solid EBIDTA & net profits allowed the European airport industry to cover its cost of capital in 2014 – however returns were lower than in other global regions and in Europe only around half of all airports were profitable.

1

Business Context
Revenues
Costs
Revenues & Costs
Investment
Profitability

BUSINESS CONTEXT

Europe's airports recorded solid traffic growth of **+5.4%** in passenger traffic in 2014, with growth of +7.3% at non-EU airports surpassing growth of +4.9% within the EU.

Overall, aviation growth in 2014 outperformed the general economy, with European GDP expansion remaining sluggish, in spite of a depreciated euro, additional action from the European Central Bank and the arrival of lower oil prices in the last months of the year. 2014 was the first time since 2011 that airlines did not reduce overall capacity on the market, with aircraft movements increasing by **+2.6%**. This was a minor increase after years of retrenchment, and airlines remained very cautious in their deployment of capacity.

Freight traffic grew by **+3.6%** in 2014 – a healthy increase compared to previous years, signalling the continued slow recovery in underlying economic growth in the EU.

TABLE 1

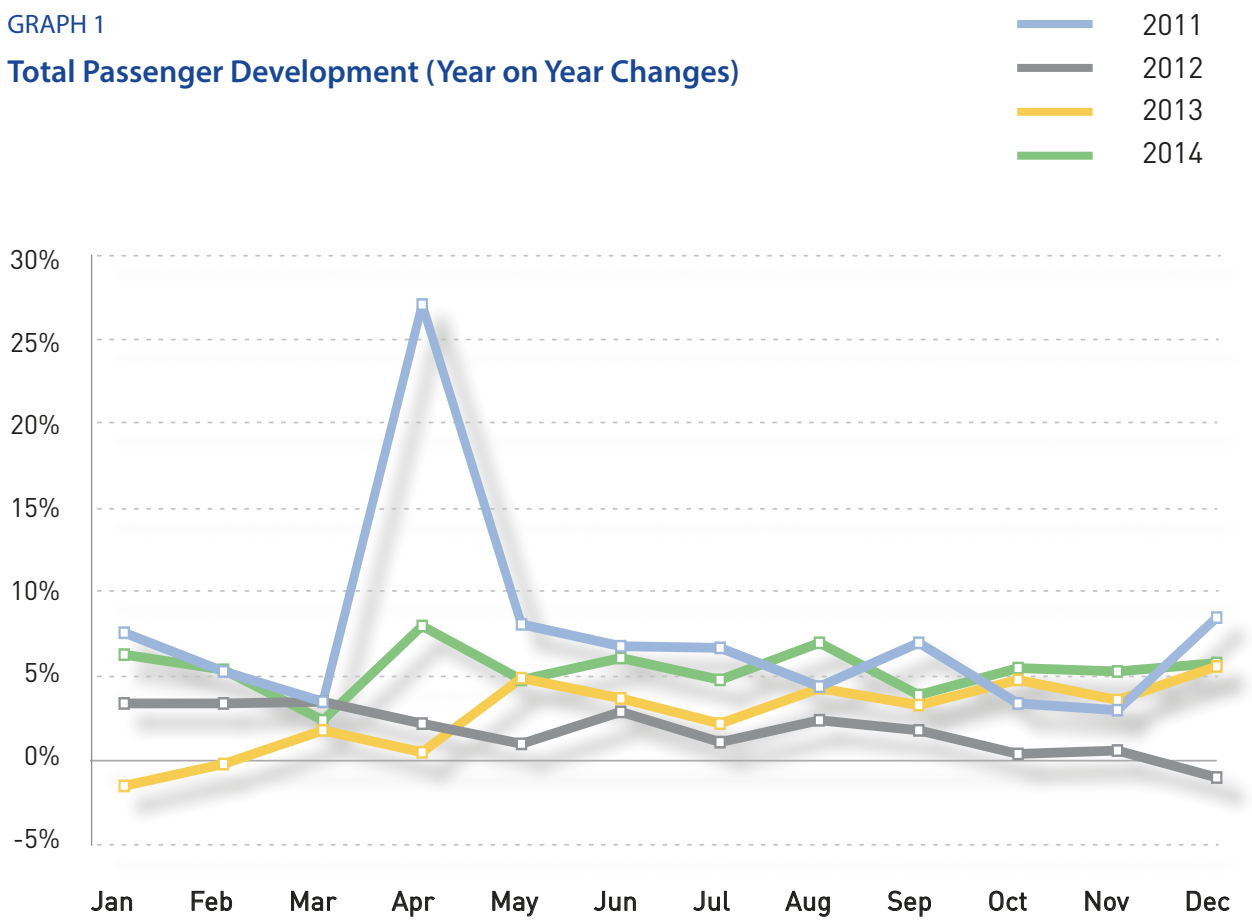
Year-on-year % change	EU	Non-EU	Overall Europe
Passengers	+4.9%	+7.3%	+5.4%
Aircraft Movements	+1.5%	+5.6%	+2.6%
Freight	+3.6%	+3.3%	+3.6%

1

Business Context
Revenues
Costs
Revenues & Costs
Investment
Profitability

GRAPH 1

Total Passenger Development (Year on Year Changes)



2

Business Context
Revenues
Costs
Revenues & Costs
Investment
Profitability

REVENUES

In 2014 total airport revenues in Europe reached **€39.7bn**. This was a real per-passenger increase of **+1.2%** on 2013 levels, and **only just above pre-crisis levels in 2008**.

Airport revenues are derived from a number of sources:

- **Aeronautical revenues:** Revenues earned primarily for charges levied upon airlines for use of the runway and aircraft parking, and upon passengers for use of the terminal services and facilities.
- **Non-aeronautical revenues:** Revenues earned primarily from activities which are not directly related to the core aeronautical business of the airport, such as retail, car parking, property rental and advertising.
- **Ground handling:** Revenues earned by those airport operators which still provide ground handling services (fuelling aircraft, loading baggage, checking in passengers, etc.). Few larger airports in Europe now provide ground handling services to airlines. Since the liberalisation of the European ground handling market in 1996, it is increasingly large pan-European specialised companies which provide such services. These companies are separate from both airlines and airports. Their pan-European networks and the accompanying economies of scale are major competitive advantages.
- **Other:** Revenues from a wide range of disparate activities, including non-operating income such as interest on reserves, the divestment of assets and – for some smaller airports – a degree of public funding.

2

Business Context
Revenues
Costs
Revenues & Costs
Investment
Profitability

TABLE 2

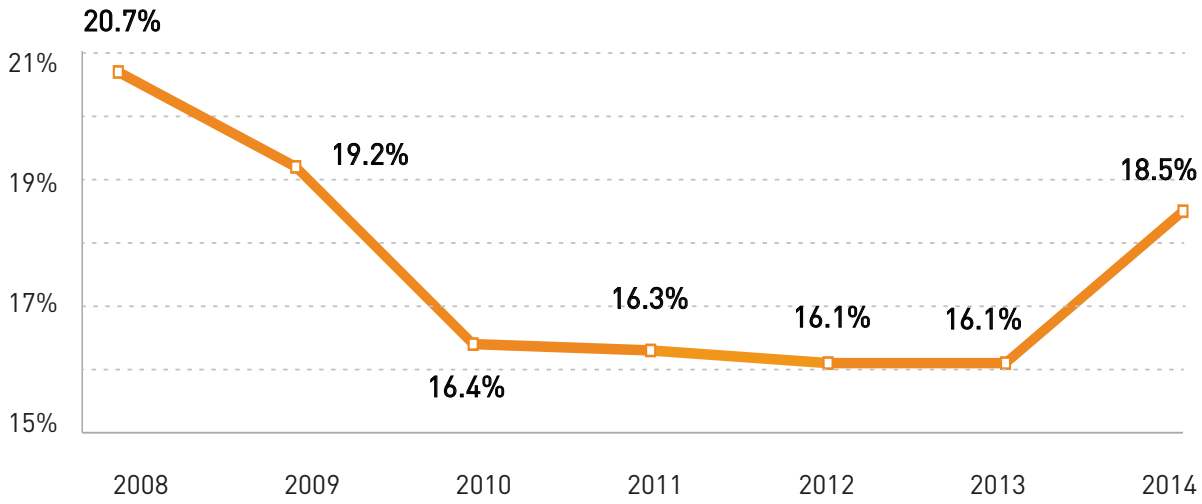
Distribution of Total Revenues	€39.7bn	100%	Excl GH and Other
Aeronautical Revenue	€21.9bn	55.2%	63.1%
Non-Aeronautical Revenue*	€12.8bn	32.3%	36.9%
Ground Handling Revenue	€1.7bn	4.3%	--
Other**	€3.3bn	8.3%	--

**Including non operating revenue.*

***Terminal navigation charges (if applicable), facility management, special guest services, other operating income.*

GRAPH 2

Airline-Related Revenues as % of Total Airport Revenues, 2008-2014

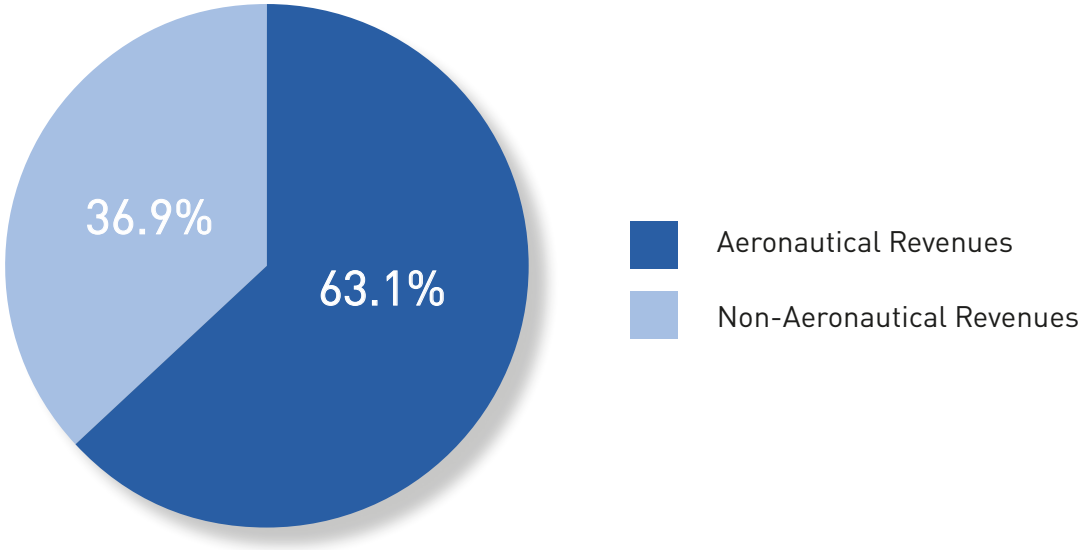


2

Business Context
Revenues
Costs
Revenues & Costs
Investment
Profitability

GRAPH 3

Aeronautical & Non-Aeronautical Revenues, 2014



AERONAUTICAL REVENUES

European airports collected **€21.9bn** from airport charges in 2014, representing a real per-passenger increase of **+2.6%**. This followed consecutive decreases in both 2013 and 2012. Changes in per-passenger aeronautical revenues are driven by the level of airport charges as well as discounts provided by airports to airlines via incentive schemes and commercial contracts – often in return for airlines delivering or committing to deliver higher volumes of passengers.

Airport charges are in turn driven by the degree of competitive pressures, regulatory intervention and – most importantly – the volume of capital expenditure that needs to be invested back into airport infrastructure.

2

Business Context

Revenues

Costs

Revenues & Costs

Investment

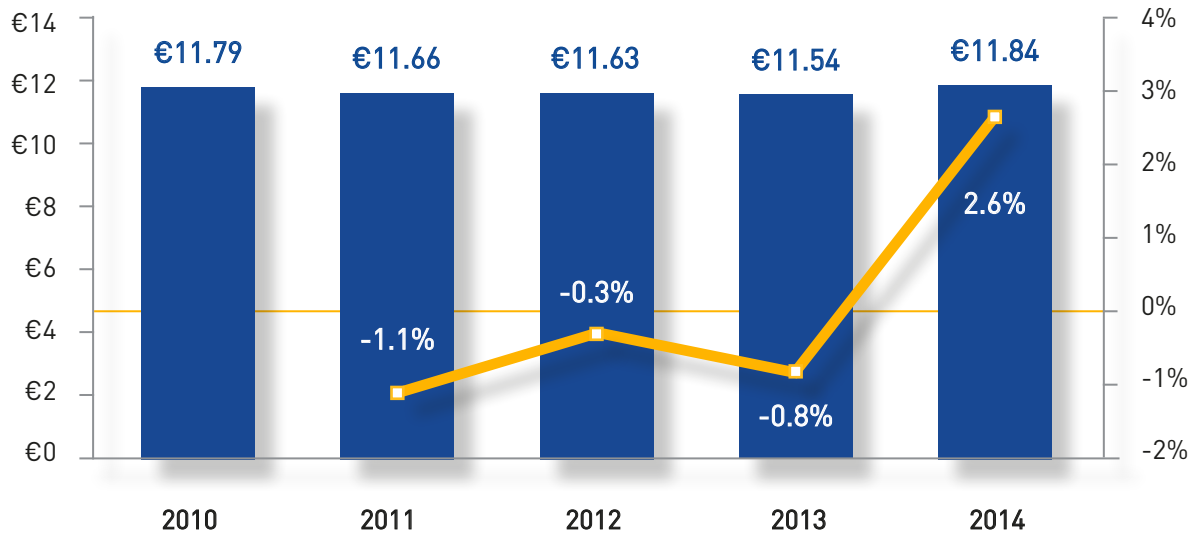
Profitability

Airport charges can be a politically contentious issue between airports and airlines. However, charges paid directly by airlines (for landing & aircraft parking fees) are only one component of airport charges[1], just as revenues from airport charges are in turn only one stream of revenue for the airports. This means that airlines make a limited contribution to compensating airports for the overall costs incurred. In 2014, revenues from airline-related charges comprised of just **18.5%** of overall airport revenues - a slight increase in previous years and low by historical standards.

Revenues from airport charges (both airline and passenger-related) are also significantly less than the cost of providing airport services & facilities. See Section on 'Revenues & Costs'.

GRAPH 4

Aeronautical Revenues (2014 prices)



[1] With the other component – passenger-related charges – being paid by passengers as part of the 'taxes and charges' component of the air fare.

2

Business Context
Revenues
Costs
Revenues & Costs
Investment
Profitability

NON-AERONAUTICAL REVENUES

In 2014 European airports generated **€12.8bn** in non-aeronautical revenues, from sources as diverse as car parking, retail food & beverage, real estate and advertising. This represented a real per-passenger change of just **+0.1%**, and follows equivalent declines of -9.9% and -1.7% in 2012 and 2013 respectively.

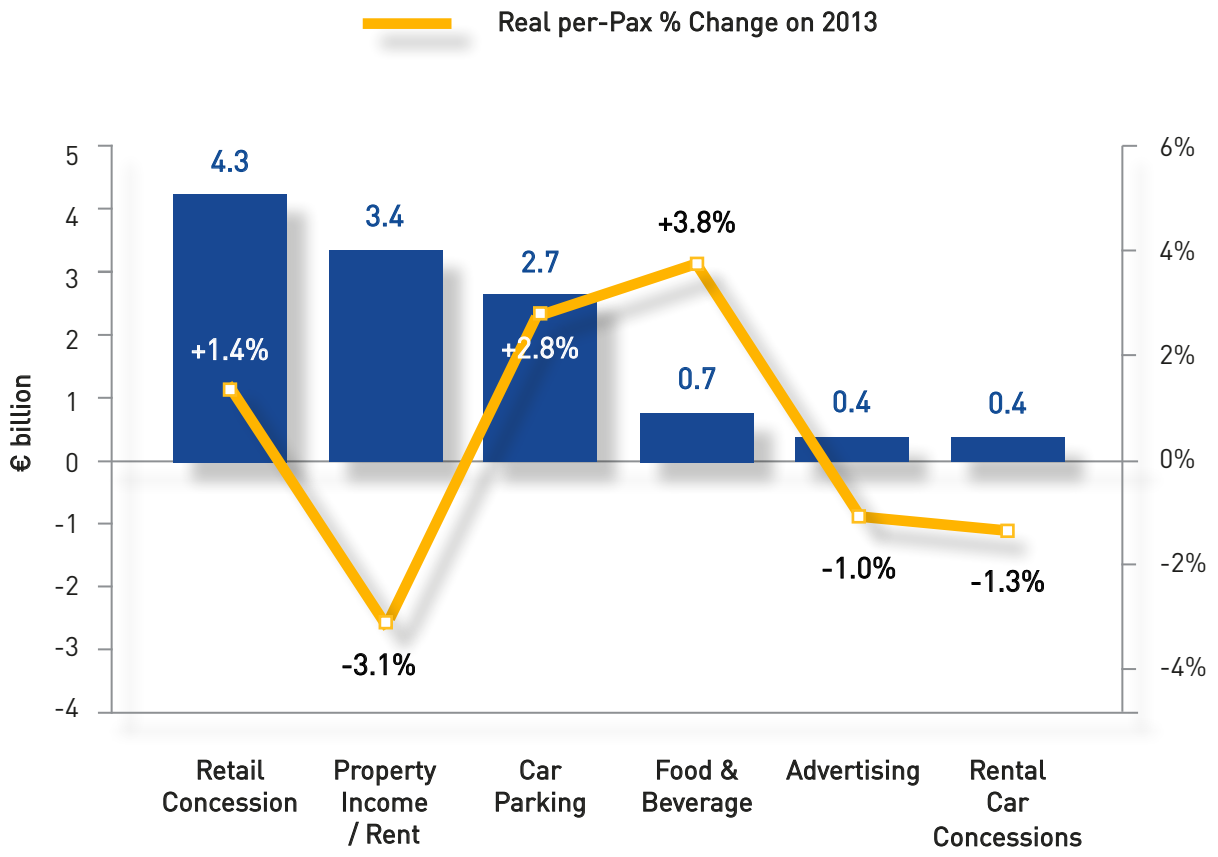
Airports in Europe are finding it increasingly challenging to boost such revenues, due to a combination of factors which significantly increase commercial pressures. Such trends include:

- The proliferation of off-site car parking providers, as well as the commercial arrangements these providers make with airlines, to offer integrated deals when passengers are buying their ticket;
- The increasing competition from online stores which do not have the costs associated with 'bricks & mortar' operations;
- The prevalence of mobile devices, which allow passengers to immediately compare travel retail prices with those of online and other high-street competitors;
- Increased security requirements which create stress for passengers and can lead to uncertainty as to whether airport purchases will be possible;
- The confusion and uncertainty created by the continued enforcement of restrictive cabin baggage allowances by airlines, which disincentivises purchases;
- The growth in repeat passengers and in particular the growth in price sensitive passengers using Low Cost Carriers. Both categories of passengers are less susceptible to impulse and discretionary purchases.

Non-aeronautical activities are a key source of revenues, which are used to maintain and expand airport facilities, and often to reduce the proportion of costs that must be paid by airlines and passengers.
A reduced ability to generate such revenues is therefore a concern for the overall aviation sector.

GRAPH 5

Non-Aeronautical Revenues by Activity, 2014



3

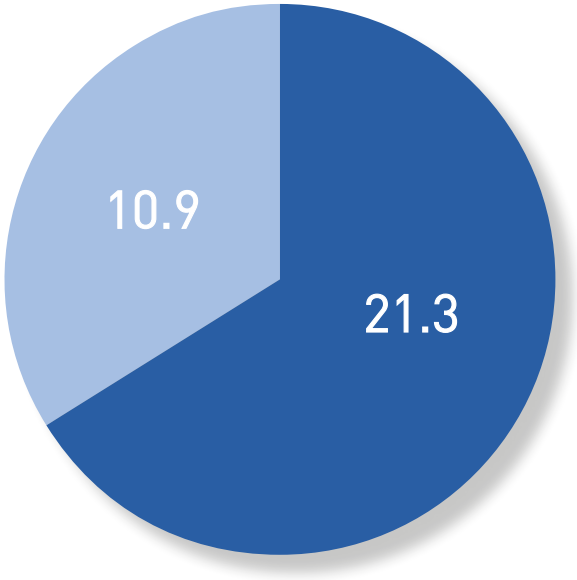
Business Context
Revenues
Costs
Revenues & Costs
Investment
Profitability

COSTS

Total costs at European airports were **€32.2bn** in 2014 – which was a **-1.2%** change on 2013 levels, in real per-passenger terms.

There are 2 main categories of airport costs:

- **Operating costs:** the costs associated with the day-to-day operation of the airport, such as the costs of security, personnel or lighting & heating. These account for circa 2/3 of overall airport costs.
- **Capital costs:** the investment needed to maintain, upgrade and expand airport facilities, such as runway, terminals, apron facilities, etc. – these account for the remaining 1/3 of overall airport costs.



GRAPH 6

Total Costs at European Airports, 2014 (€bn)

3

Business Context
Revenues
Costs
Revenues & Costs
Investment
Profitability

OPERATING EXPENDITURE

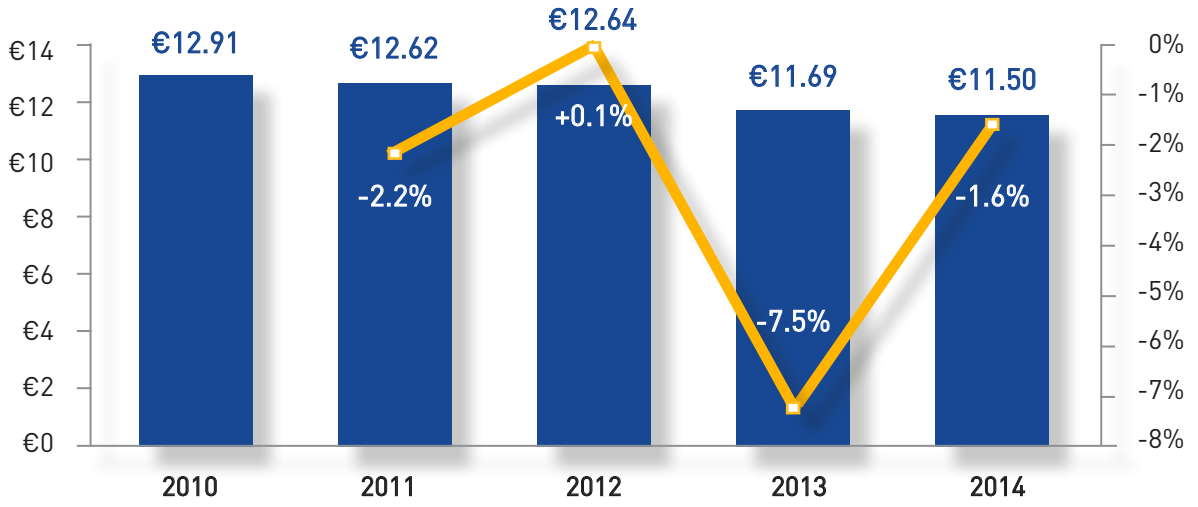
Operating expenditure for European airports in 2014 was **€21.3bn**, which represents an annual decrease of **-1.6%** in real per-passenger terms. Since the crisis European airports have been consistently reducing or keeping stable operating costs. Due to the nature of the business, a significant proportion of airports' costs have limited scope for reduction (in particular due to regulatory requirements) – meaning that airports have focused their efficiency efforts in those specific areas where cost savings are possible.

The decreases in 2014 broadly correspond to decreases in operating costs in previous years – with airports demonstrating a particular focus on costs in those areas where they have the ability to do so. As a consequence **operating costs are significantly below 2008 pre-crisis levels in real per-passenger terms.**

A challenge for airports is to reduce costs without unduly compromising service quality standards. European airports, however, have a track record of improving passenger satisfaction across a range of metrics, alongside reductions in unit costs. Between 2006 and 2015 for example, overall passenger satisfaction with the 21 largest airports in EU & EFTA increased by +12.4%[2].

GRAPH 7

OPEX (2014 prices)



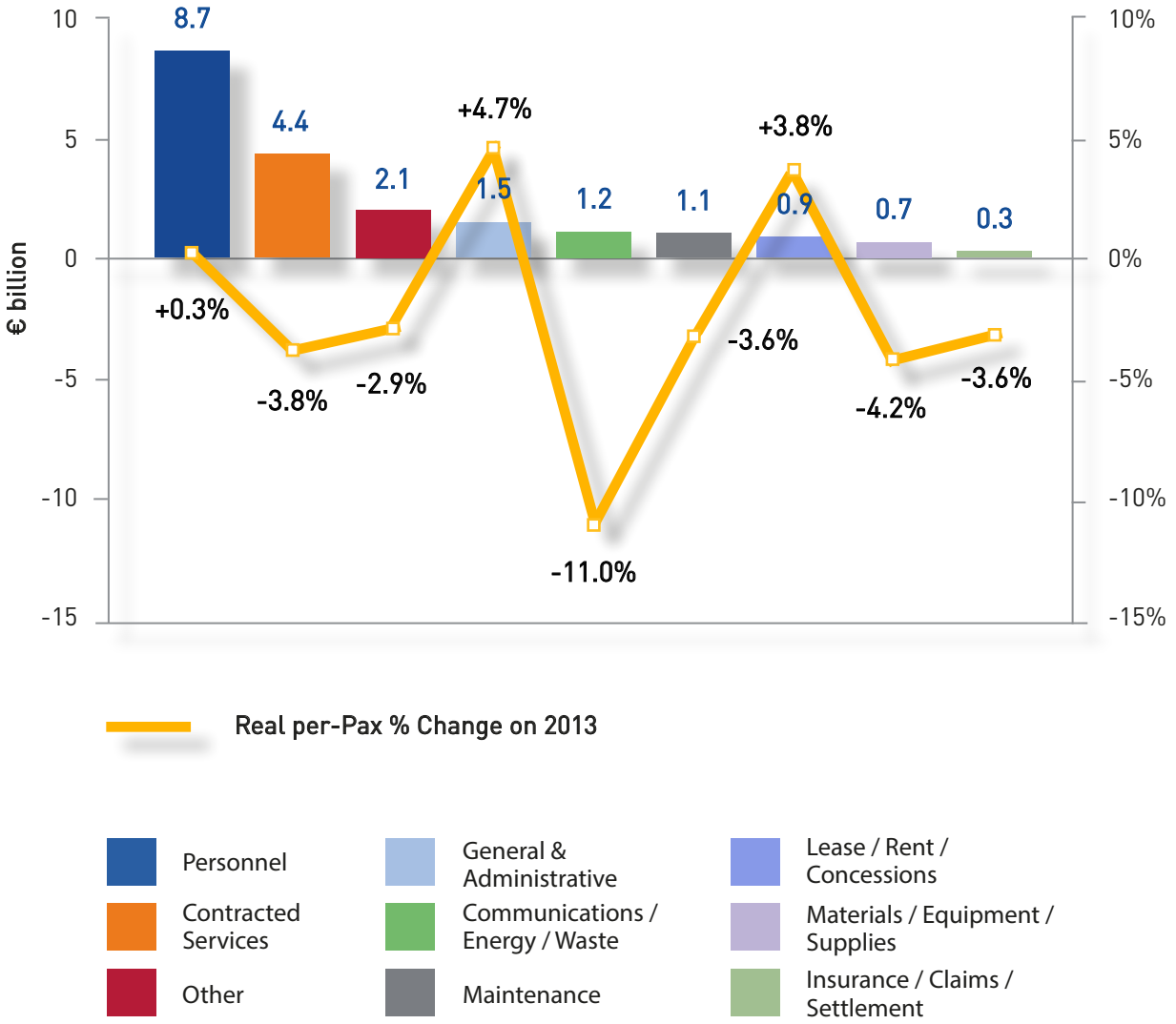
[2] *'ACI EUROPE Analysis Paper: Leveraging Airport Investment to Drive the EU's Aviation Strategy – A Decade of Delivery for the Top 21 Airports in Europe',* ACI EUROPE, June 2016.

3

Business Context
Revenues
Costs
Revenues & Costs
Investment
Profitability

GRAPH 8

Operating Expenditure by Area, 2014



3

Business Context
Revenues
Costs
Revenues & Costs
Investment
Profitability

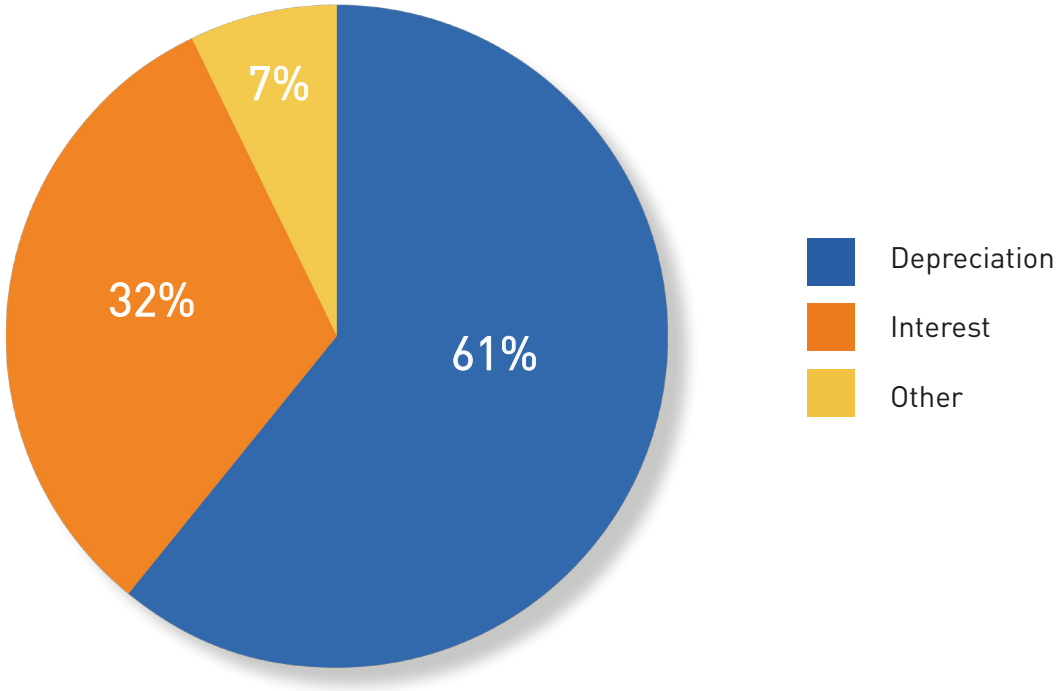
CAPITAL COSTS

European airports paid **€10.9bn** in capital costs in 2014 – a decline of **-0.3%** on 2013 levels, in real per-passenger terms. Capital costs are primarily comprised of depreciation and interest expenses.

Capital costs appear to have stabilised, after shooting up dramatically subsequent to the 2008 crisis, and reducing gradually thereafter. This is important, as capital costs make up approximately a third of overall airport costs, and airports have very limited room to control these. Nevertheless, real per-passenger capital costs remain considerably higher now than they were pre-crisis.

GRAPH 9

Capital Costs at European Airports, 2014



4

Business Context
Revenues
Costs
Revenues & Costs
Investment
Profitability

REVENUES & COSTS

As in previous years, the revenues generated from the provision of aeronautical services and facilities are considerably less than the operating and capital costs incurred when providing those services and facilities.

In 2014 European airports incurred overall capital and operating costs of **€32.2bn.** Revenues from airport charges (both passenger and airline-related) reached just **€21.9bn** – representing a gap of over **€10bn.**

Put another way, revenues from airport charges just about covered the day-to-day costs of operating the airport. The capital costs were not covered – meaning that **the costs of maintaining and expanding airport infrastructure must come from alternate sources**. Instead, airports use margins from non-aeronautical activities such as shopping, car parking and advertising to 'close the gap'.

It should also be remembered that airlines only directly contribute a fraction of overall airport charges (via airline-related charges[3]). These represent just **18.5%** of overall airport revenues.

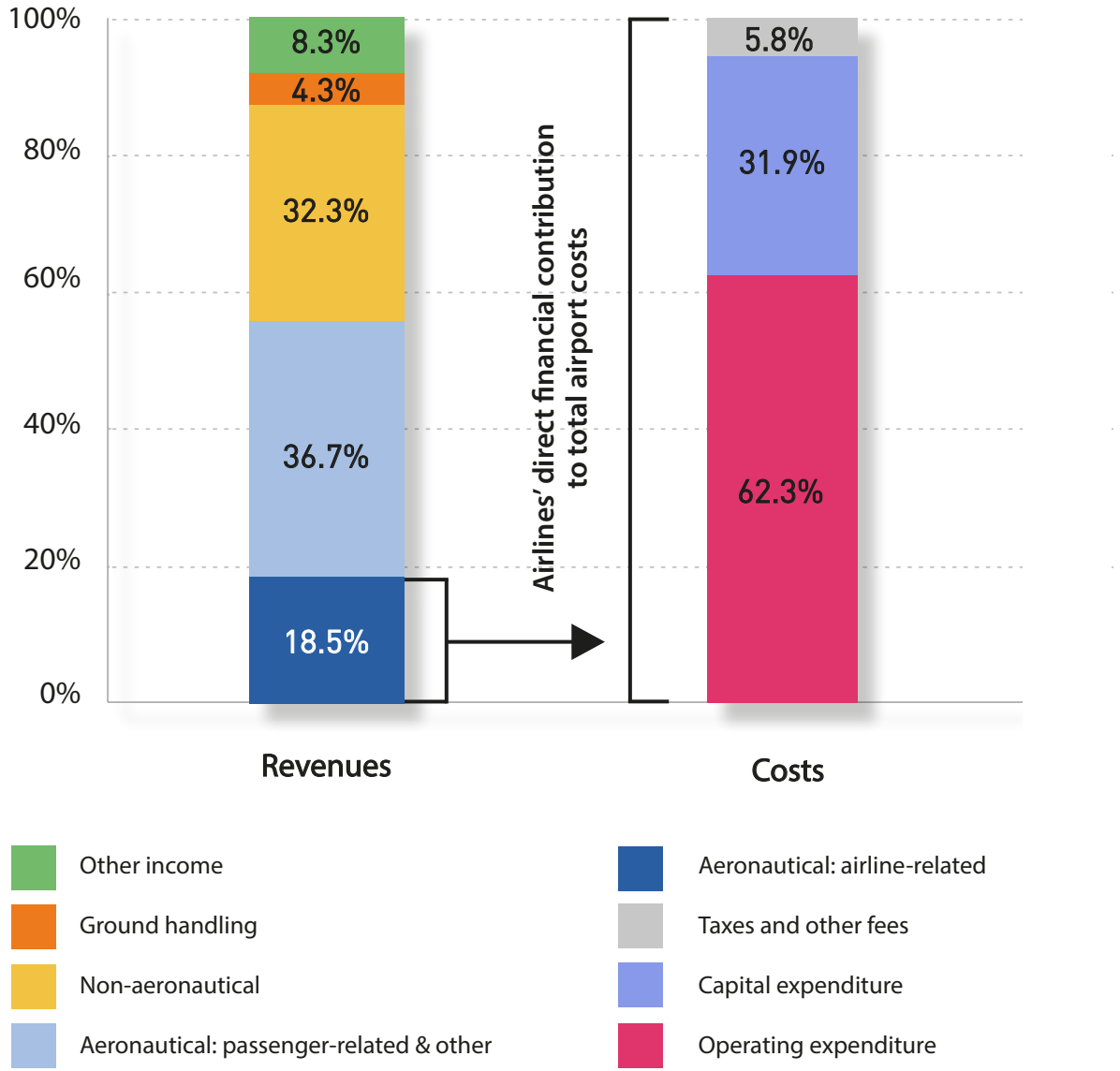
[3] Passenger-related charges are paid by passengers, and collected by airlines as part of the 'taxes and charges' component of the air fare.

4

Business Context
Revenues
Costs
Revenues & Costs
Investment
Profitability

GRAPH 10

Proportionate Breakdown of Revenues & Costs, 2014



5

Business Context
Revenues
Costs
Revenues & Costs
Investment
Profitability

INVESTMENT

European airports invested **€6.2bn** back into facilities & equipment in 2014.

As in previous years 2014 capital expenditure was less than had been previously forecast. However unlike previous years, forecasts for expenditure in the future have actually increased as time progresses. This may reflect the increased certainty that interest rates are set to remain low beyond the short term, as well as renewed confidence in longer-term demand growth. In light of EUROCONTROL's forecast capacity crunch, this sign of increased airport investment is to be welcomed.

Capital expenditure is a fundamental activity of airport operators, to maintain and expand expensive infrastructure, and to ensure sufficient levels of service quality. It can also have implications for the level of airport charges levied. Between 2005-2015 the top 21 airports[4] in the EU and EFTA invested more than **€53bn** back into facilities. This allowed them to add capacity to cater for an additional >175 million passengers per annum – the equivalent of adding another Heathrow, Orly & Charles de Gaulle to the European aviation network.[5]

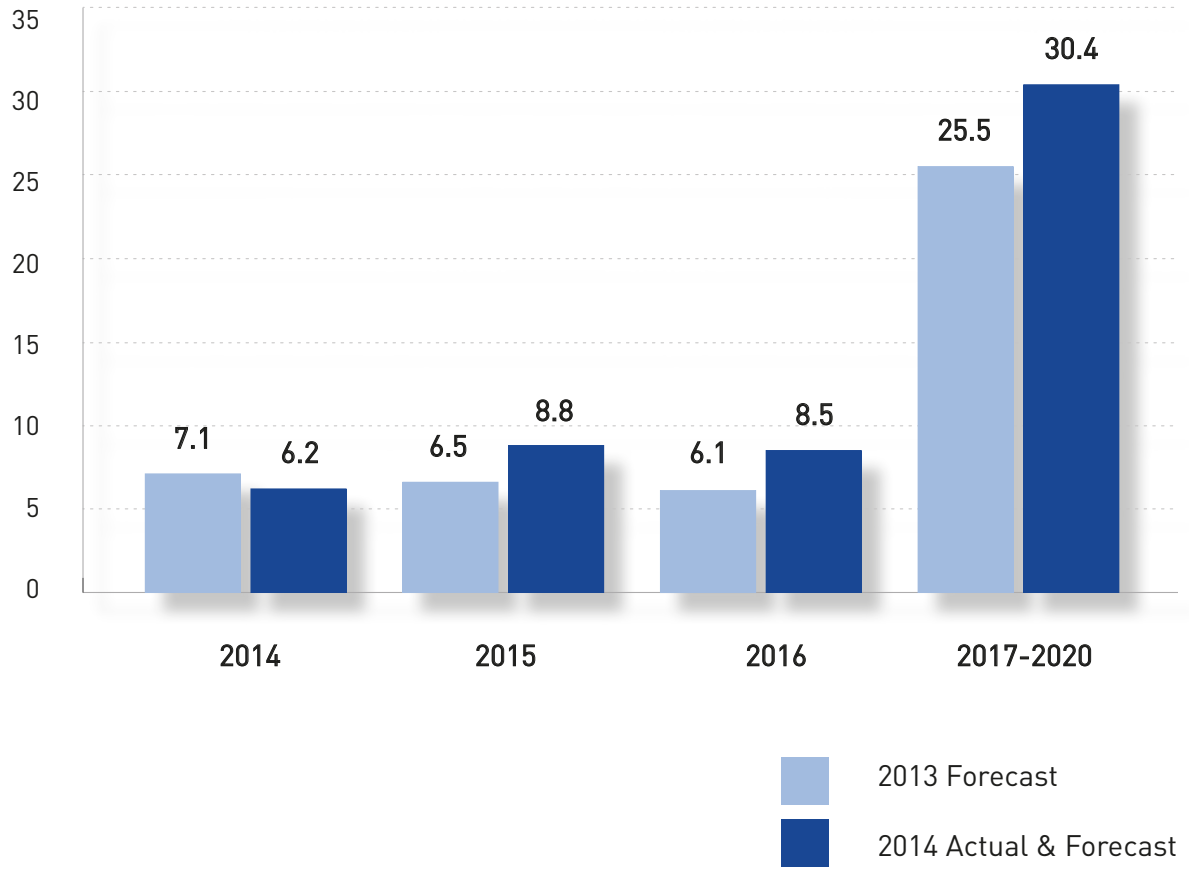
[4] Heathrow; Paris-Charles de Gaulle; Frankfurt; Amsterdam Airport Schiphol; Adolfo Suárez Madrid-Barajas; Munich; Rome Fiumicino; Gatwick; Barcelona-El Prat; Paris-Orly; Copenhagen; Zurich; Oslo; Palma de Mallorca; Vienna; Stockholm Arlanda; Manchester; Brussels; Dusseldorf; Dublin; Berlin Tegel.
[5] *'ACI EUROPE Analysis Paper: Leveraging Airport Investment to Drive the EU's Aviation Strategy – A Decade of Delivery for the Top 21 Airports in Europe',* ACI EUROPE, June 2016.

5

Business Context
Revenues
Costs
Revenues & Costs
Investment
Profitability

GRAPH 11

2014 Actual & Forecast Investment versus 2012 Forecast (€bn)



6

Business Context
Revenues
Costs
Revenues & Costs
Investment
Profitability

PROFITABILITY

European airports made Earnings Before Interest, Depreciation, Taxation & Amortisation (EBIDTA) of **€18.4bn** – an annual increase of **+4.7%** in real per-passenger terms.

Net profits were **€5.6bn** – an equivalent increase of **+7.8%**. This is less than the €6.2bn that was invested back into infrastructure by airports in 2014.

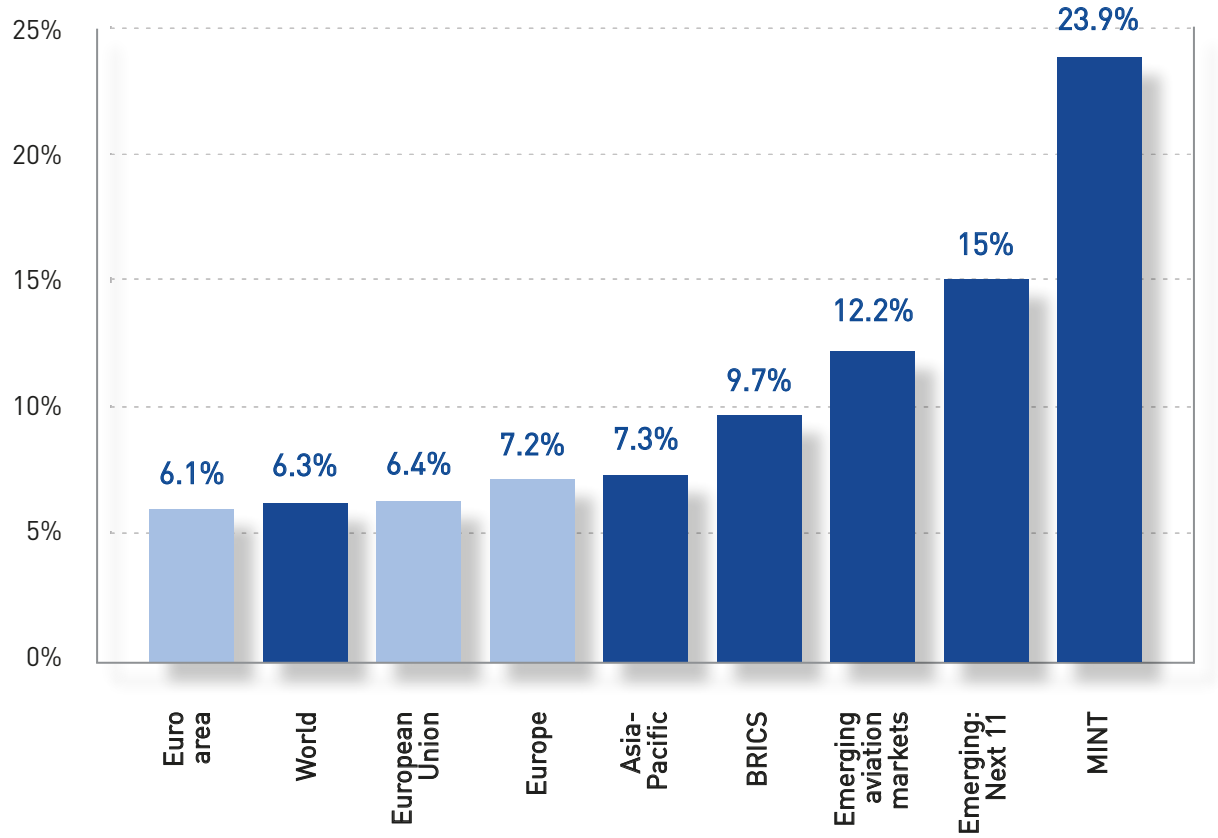
While these margins are healthy, they must be considered relative to the volumes of investments that need to be made – what sort of return are airports able to offer to investors and creditors? For example, European airports continue to hold considerable levels of outstanding debt - **€72.1bn** in absolute terms – which was incurred to finance expansion and which must be paid back with interest. Airport's overall debt decreased slightly in 2014, in real per-passenger terms.

A more appropriate measure is therefore the **Return on Invested Capital (ROIC)**, which reflects the return airports make relative to the capital put into the business. In 2014, European airports earned a ROIC of **7.2%** - within an appropriate range for the industry's cost of capital, and substantially less than the returns being earned by airports in other parts of the world. It should be noted that the average 'World' Return on Invested Capital is weighted down by the returns of airports in the US, which are not operated commercial businesses and which therefore are not profit maximising.

The profitability of the airport industry is also quite **concentrated** – **half of European airports are in fact loss-making**. Typically these are smaller airports, which have high fixed costs and practically no bargaining power vis-à-vis their airline clients. Indeed, loss-making operations are concentrated amongst those airports with less than 1 million passengers per annum.

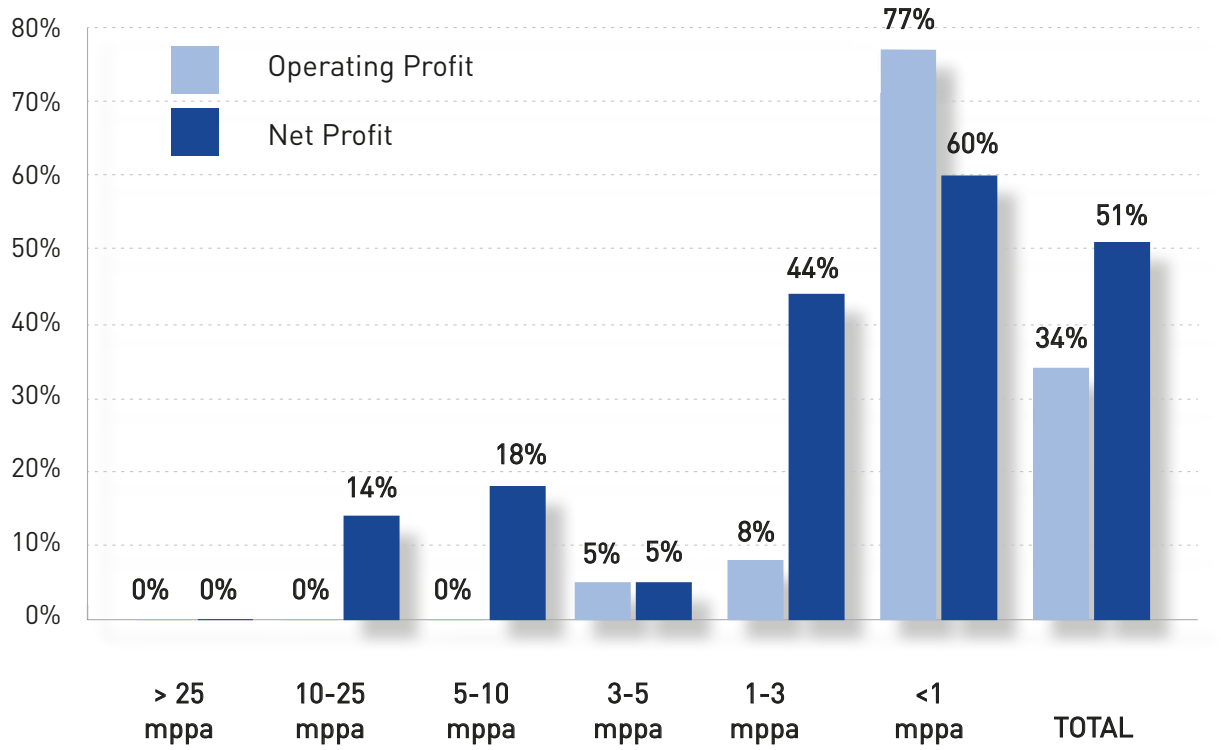
GRAPH 12

Average Airport ROIC in Selected World Regions



GRAPH 13

% of Loss Making Airports in Europe, 2014



TAXES & OTHER FEES

Airports in Europe paid just under **€2bn** in taxes and charges in 2014 – representing a significant real per-passenger of **+30.1%** on 2013 levels. The volume of taxes and other fees paid tends to fluctuate considerably from year to year, in part reflecting changes in the profitability of the airport business.



Business Context
Revenues
Costs
Revenues & Costs
Investment
Profitability



METHODOLOGY

The data used in the 2015 Report is based on the economic and financial results of European airports in the reporting year 2014. **101** airport operators representing **221** airports in Europe responded to the survey conducted by ACI World, representing just under **79%** of total European passenger traffic, or close to **1.457 billion** passengers.

As with last year's Report, the survey collected data for both 2014 and for 2013, which enables comparisons to be made with 2013 data, based on the exact same sample. This ensures more reliable comparison between years within the Report, but means that absolute figures cannot be directly compared with equivalent figures from the previous year's edition.

Where multi-annual per passenger figures are compared directly against each other, all figures are cited in 2014 terms and are based upon the real per-passenger variation between each two years, as reported in the ACI EUROPE Economics Report of the relevant year.

All figures were converted into euros, where airports did not report in this currency. The exchange rates used were based on annual bilateral exchange rates for **2014**, according to the European Central Bank. Year-on-year changes in financial results are reported in per-passenger real terms. A per-unit analysis provides a more accurate indication as to the annual developments of the industry's finances, as these would otherwise be masked by the strong impact of traffic volumes, which can vary considerably each year. To report the figures in real terms, an inflation index was constructed to reflect the composition of the specific sample. National inflation figures for the year 2014 were sourced from the International Monetary Fund, and these were weighted according to the proportion of traffic represented by each country within the sample.

This gave a 2014 inflation rate of **1.47%** for the sample as a whole, **0.44%** for the EU, and **5.65%** for the non-EU block of countries.



ACI EUROPE is the European region of Airports Council International (ACI), the only worldwide professional association of airport operators. ACI EUROPE represents over 500 airports in 45 European countries. In 2015, our member airports handled over 90% of commercial air traffic in Europe, welcoming more than 1.9 billion passengers, 18.9 million tonnes of freight and 22.8 million aircraft movements. These airports contribute to the employment of 12.3 million people, generating €675 billion each year (4.1%) of GDP in Europe.

Based in Brussels, we lead and serve the European airport industry and maintain strong links with ACI World and other ACI regions throughout the world.

EVERY FLIGHT BEGINS AT THE AIRPORT.

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