International Civil Aviation Organization

WORKING PAPER

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CONFERENCE ON THE ECONOMICS OF AIRPORTS AND AIR NAVIGATION SERVICES

Montréal, 15 to 20 September 2008

Agenda Item 2: Specific issues related to airport economics and management
2.2: Cost basis for charges
Agenda Item 3: Specific issues related to air navigation services economics and management
3.2: Cost basis for charges

RATE OF RETURN FOR AIRPORTS AND AIR NAVIGATION SERVICES

(Presented by Airports Council International (ACI))

SUMMARY

Any guidance material from ICAO on determining a reasonable rate of return should not be prescriptive or specific with regard to methodologies or technical details. The weighted average cost of capital (WACC) is a recognized methodology, but only one possible method among others to determine a rate of return. It should be up to the States to decide if and how to determine a reasonable rate of return on a case-by-case basis in line with the principles of economic oversight. When calculating a reasonable rate of return, the various and potentially significant degrees of risk airports are exposed to must be taken into account.

Action by the Conference is in paragraph 4.

1. INTRODUCTION

1.1 Capital intensive companies like airports require a rate of return similar to the cost of capital or higher to satisfy investors or creditors. Risk is a key variable parameter in calculating the WACC which will increase with higher risk.

[1] Language versions are provided by ACI.

2. DISCUSSION

2.1 Airports are entitled to a reasonable rate of return to secure financing of new or expanded infrastructure and to remunerate their shareholders. Private equity and credits are the primary source of capital as public funding is hardly available anymore.

2.2 To ensure future investment in airport infrastructure, it is important that private and institutional investors maintain their confidence in airports as attractive investment targets. Introducing prescriptive and specific guidelines regarding the rate of return that airports are allowed to generate might damage investor confidence.

2.3 Any methodology applied to calculate the rate of return should specifically take into account and segregate the contribution of non-aeronautical revenues to the overall airport financial performance. Non-aeronautical revenues should not be subject to any limitations on profitability as they are not derived from aircraft operators.

2.4 Airports are not *per se* low risk businesses. They are entirely exposed to the airline industry which is very susceptible to external circumstances forcing it frequently to revisit business models and strategies which immediately affect airports. The airports' ability to react to negative developments is rather limited as airport infrastructure, unlike aircraft, cannot simply be decommissioned.

2.5 Airports continue to incur cost irrespective of the level of infrastructure usage, and regardless of market trends or airline industry challenges, airports maintain the highest safety and technical standards and continue to apply the strictest security measures.

3. CONCLUSIONS

3.1 From the foregoing discussion, the following conclusions may be drawn:

a) In performing their economic oversight function, States should decide on a case-by-case basis if and how to determine a reasonable rate of return of airports.

b) ICAO should review the necessity of developing additional guidance material regarding possible methodologies to assess a reasonable rate of return on assets from service providers as sufficient economic literature on this subject is already available.

4. ACTION BY THE CONFERENCE

4.1 The Conference is invited to review and adopt the conclusions in paragraph 3.

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