Weathering the Financial Storm

After Cutting Costs and Salvaging Revenue in the Aftermath of 9/11, Airports Look to the Future

Airports were largely able to weather the initial shock of a business decline and security cost rise following the terrorist attacks of September 11. Even though the squeeze on net income has been persistent, making it harder to fund new security capital costs, airport executives are optimistic about their airports, the aviation market and their ability to steer through the storm. This Measure of the Month uses the results of the latest AAAE Rates and Charges Survey and its special section on 9/11 impacts to assess how airport managers have dealt with the crisis until now and their plans for the remainder of 2002.

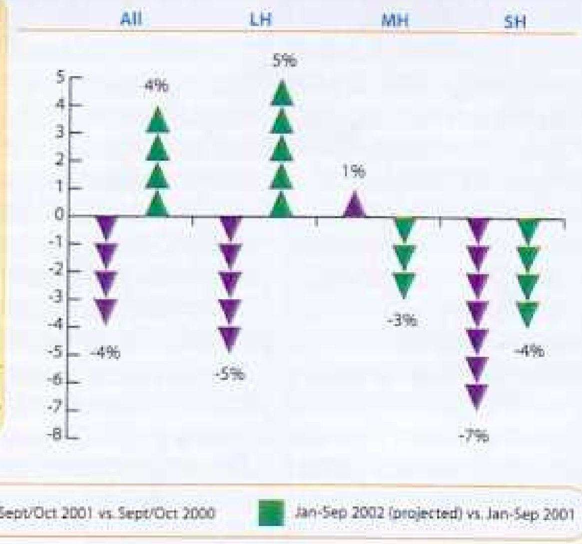


Fig. 1 PROJECTED CHANGE IN AIRPORT REVENUES

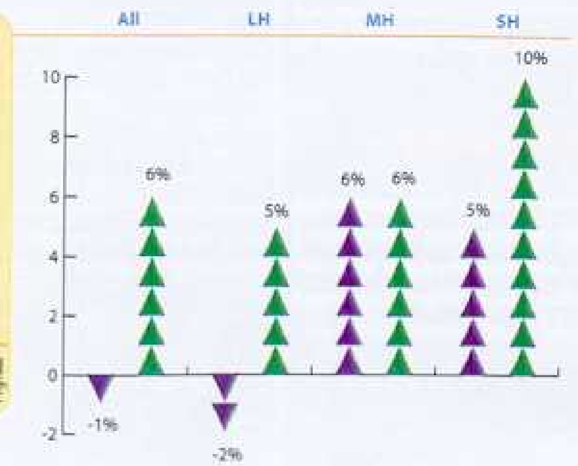


Fig. 2 CHANGE IN OPERATING EXPENDITURES

In September and October 2001, most of the 93 airports in the survey (consisting of 25 large hubs, 20 medium hubs and 48 small hubs) reported that revenues were down as much as 7 percent in this period in comparison with the same period in 2000, with a weighted average of minus 4 percent. This compares with a decline of 20-30 percent in revenue passenger miles of the seven largest U.S. commercial airlines in September and October, year over year. Figure 1 at right shows that U.S. airport executives predict airport revenues will not only recover in 2002 but will be higher than they were in the first three quarters of 2001; that is, they believe air travel will have quickly resumed its pre-9/11 growth path.

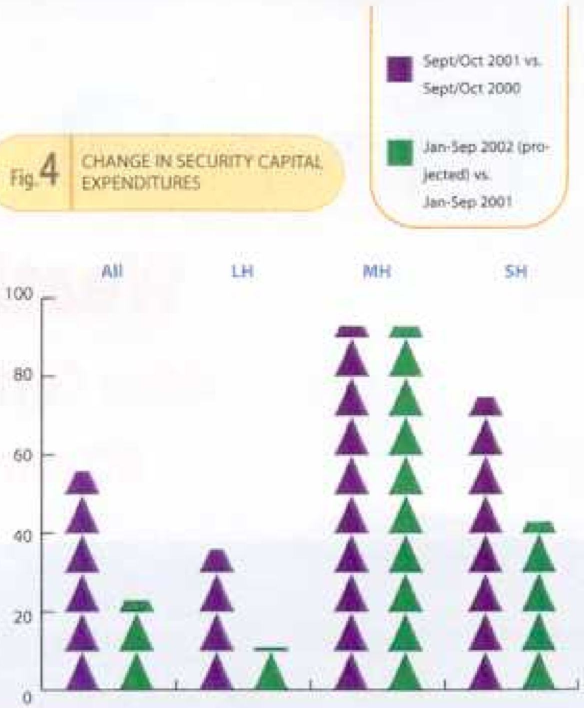
In the same three-quarter period, airports reduced operating expenditures by 1 percent, as shown in Figure 2, a percentage that may have been much greater were it not for added security costs. Without these security cost increases, airport operating expenditures would probably have declined between 5 and 9 percent. By holding costs steady in the short term and relying upon surprisingly buoyant concessions revenue and formula-driven landing fees, U.S. airport finances were able to withstand the sudden drop in traffic following 9/11 surprisingly well.

Looking forward, however, airport executives see continued turbulence. From the vantage point of when the survey was taken—November and December 2001—they do not expect to contain their operating costs, especially security-related costs, and were fairly universal in predicting an increase in costs of 5-10 percent.

The major credit rating agencies have concluded that airport finances will continue to be under stress, although with few actual rating downgrades. Of course, these financial results alone do not fully describe an airport's economic health.

Fig. 3 MEASURES TO INCREASE REVENUES (NUMBER OF TIMES MENTIONED; AIRPORTS COULD REPORT MORE THAN ONE MEASURE)

Fig. 4 CHANGE IN SECURITY CAPITAL EXPENDITURES



Businesslike Measures

How have airport managers addressed the decline in revenues and expected increases in operating expenditures? As Figure 3 indicates, many airports took two primary steps to boost revenues in the face of declining traffic: They increased parking rates and landing fees. The former strategy reflects the importance of parking as a revenue source, and the post-9/11 drop-off was the single greatest revenue loss for many airports due to fewer passengers, fewer meeters and greeters (prohibited from waiting on concourses) and the 300-foot terminal perimeter rule restrictions that affected the supply of lucrative short-term parking.

Airports also took a number of other measures to pump up their finances. These reflect good management practices that might be followed even in better times:

- Exercising all escalation clauses in concession contracts
- Increasing concession retail rents, where allowable
- Expanding retail opportunities, such as after security checkpoints and with flexible carts in increasingly tight terminal areas
- Aggressively developing industrial park and other non-aviation properties
- Seeking additional air service, even when airlines have been cutting back service.

Cutting Costs—and Service

Airports also took action to reduce costs, or at least freeze them. Staff costs were the first areas on which airports focused since personnel costs often comprise 50 percent of an airport's operating expense. While few airports reported layoffs, many reported hiring freezes, reduction of non-security overtime, limiting wage increases and benefits, deferral of new hires and elimination of vacant positions. Some airports are trying to cross utilize staff better, such as having non-security staff assist with vehicle inspections.

A number of airports also said that they had instituted across-the-board cuts of 5-30 percent, with 10 percent mentioned most frequently. Several believed that due to already conservative operating expenditure policies, they had little "fat" to cut. Beyond staff cuts and general belt-tightening, airports reduced routine expenditures for maintenance.

Finally, airports are instituting a host of measures that have, unfortunately, resulted in reduced customer service. This includes reduced janitorial services, increasing the temperature in terminal buildings in warm regions, scaling back shuttle buses and delaying the implementation of time-saving parking AVI systems. Obviously, coupled with the number one 9/11 customer service issue—increased lines at security checkpoints—these inconveniences must be understood in the context of the goal to dramatically improve aviation security. Nevertheless, airports have clearly shifted their focus to financial survival at the expense of their recent investments in customer service.

The Price of Extra Security

Debates continue to rage throughout the airport community on the costs of improved security measures and how they will be funded. Figure 4 indicates that all airports reported significant increases of 36 percent to 93 percent in security capital expenditures in the two months following 9/11. Airports are unsure what 2002 security costs will be, with estimated increases over 2001 ranging from 11 percent to 93 percent, quite a wide range.

Most airports do agree, however, that there will be little additional funding—at the federal or state level—for non-security capital expenditures in the next one to two years, beyond already committed funds.

Few airports have canceled their capital programs in response, but many have put their plans on hold for three to six months. Those programs that were funded primarily from ongoing fees, passenger facility charges and/or bonds are more likely to go forward, but plans relying upon new or continuing income have been affected most dramatically.

We will not know for another year or so if the measures airports have taken to increase revenues and keep operating costs down will be enough to allow both security and non-security capital investments to go forward at the same time, but it certainly appears that airports are doing everything they can to keep that option open.

What have been the financial effects of 9/11 on your airport? If you would like to share your ideas and information, please e-mail spage@imginfrastructure.com.

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