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Determination on Airport Charges at Dublin Airport

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1. Introduction

ACI EUROPE represents over 500 airports in 55 countries. Our members facilitate over 90% of commercial air traffic in Europe. Air transport supported in 2019 13.5 million jobs, generating €886 billion in European economic activity (4.4% of GDP). In response to the Climate Emergency, in June 2019 our members committed to achieving Net Zero carbon emissions for operations under their control by 2050, without offsetting. Based in Brussels, we lead and serve the European airport industry and maintain strong links with other ACI regions throughout the world.

ACI EUROPE welcomes the Commission for Aviation Regulation’s issues paper and consultation with stakeholders, an important way to ensure transparency and effectiveness of economic regulation.

The issues paper was published and the consultation has unrolled at a time as the attention of many in Europe has been shifted to geopolitical issues, even as the COVID-19 pandemic remains a concerning health matter. These developments underline the importance of realism about the foresight that any business or authority may be able to have about future developments, and consequently the need to allow for adaptable, flexible and market-driven approaches.

2. Forecasting, risk allocation and extreme downsides

ACI EUROPE sees it appropriate to discuss issues raised in parts of section 4 and section 5 together; as the question of risk allocation is interlinked with the question of forecasting.

There is no forecast which will always be accurate. This does not demean the purpose of forecasting, which is essential for business planning, operations, tactical management, and equally regulation. Because it is the airport operator which bears the responsibility of dealing with actual performance varying from imperfect forecasts, the airport operators should also have full responsibility for the forecast methodology used in a period.

The issues paper is correct to recognise that there may be incentives on the various parties, but this is only true in the short-run. In a long period of repeated interactions, the airport operator will be the only party who is assured to be at the centre of each discussion about forecasting. This long-run repeated engagement is sufficient to ensure that the airport operator will develop internally, review with its board, and propose and consult with its users and government partners an accurate forecast. Following these discussions and feedback sessions, the final forecast and methodology for the forecast should be the competence of the airport.

The CAR raises the timely question of how to deal with extreme downsides and risk allocation.

In ACI EUROPE's experience, the approach for regulation at Dublin Airport is amongst the most open and consulted regimes in Europe. This consequently calls for maintenance of the existing regime for Dublin Airport related to risk allocation and dealing with extreme downsides.

The rapidity with which CAR responded to the Covid-19 crisis in 2020, in terms of consulting on the 2019 Determination, shows that CAR has put in place a mechanism which can function during foreseen but impossible to predict crises.

For regulated infrastructure entities, such an approach is essential. The focus on efficiency incentives in the CAR approach for DUB further calls for allowing the airport operator the managerial ability to reach for those incentives.

As discussed in the issues paper, there are a number of cases of numerically based mechanisms. The system applying to European air navigation service providers (ANSPs), discussed in the paper, demonstrates that such regimes may still require ad-hoc adjustments, even when they existed ex ante, depending on the depth and length of the shock. The numbers could be calibrated either to recognise the assumed flexibility that airports have to vary their costs in line with traffic or to replicate the degree of traffic risk that airports have in practice assumed over the recent past. The latter would leave the balance of traffic risk between airports and their customers effectively unchanged in 'normal' times but provide airports with security over the tail risk involved in major perturbations like pandemics.

It is important to recognise that the Covid crisis is not over. Indeed, the crisis has so far constantly surprised on the downside, and recent developments point towards more instability.

3. Operating expenses

Dublin Airport faced high powered incentives to reduce costs because of the sheer scale of traffic reduction and the strength of the link between passenger throughput and revenues.¹ The financial consequences meant that airports had to take every operational decision that they could to reduce cash outflows.

Attempts at benchmarking may do little to help understand the adequacy of the response, and simply reveal more about the different locational features of an airport, as noted by the issues paper. Differing responses by airports will likely have been conditioned by varying operating and physical characteristics, while any differences between what could be achieved in different parts of the aviation supply chain are more likely to derive from varying cost structures than any lack of cost cutting will.

The use of 2020/21 results to establish a bottom up analysis would not be appropriate and provide flawed results, given the impacts and of COVID to all cost lines. It is also ACI EUROPE's general experience in Europe, that bottom-up approaches are, at the end, almost always controlled against a top-down estimate. Such a disconnect questions the purpose of the costly and time-expensive former approach.

Therefore, ACI EUROPE objects to the notion that CAR could *"define a 2022 baseline based on what Opex would have been if Dublin Airport responded to COVID-19 efficiently in 2022"* (6.11). Retrospective second-guessing of the airport operators responses is unlikely to be efficient or helpful.

The resulting working assumption for regulators should therefore be that the actions taken by airports were efficient during the crisis, but that as the market and travel patterns normalise, operating costs will return to long-run means similar to what was seen in 2019.

4. Commercial revenue

The discussion of commercial revenues must recognise that in a single till, the consequences of mis-forecasting commercial revenues are even greater.

The single till as applied at Dublin Airport, and in most cases where it applies in European airports, is flawed as it works only in one direction. Airport users benefit from non-aeronautical revenues earned by the airport, that reduce aeronautical costs. But airport users, when there is a shock that results in lower non-aeronautical revenues than expected, do not take any responsibility to cover non-aeronautical costs. This is a flaw of the single till as applied.

An obvious solution is to allow the use of dual till accounting. Allowing a dual till framework naturally can include the possibility for a cross-subsidy from the non-aeronautical till to the aeronautical till, which can even be formalised in a hybrid till structure.

Where the single till is deeply ingrained in regulatory frameworks, and noting that some parties argue strongly for the single till, it is important that the framework appropriately treats divergences from forecasts symmetrically.

¹ Ensuring liquidity for airports during the COVID-19 crisis, ACI EUROPE Working Paper, June 2020, para 2.1. <https://www.aci-europe.org/component/attachments/attachments.html?id=1023>

The projected commercial revenues with a building blocks approach that uses a single till, must also have a robust mechanism for ensuring that airport users not only benefit from the non-aeronautical revenues, but also assume liability for non-aeronautical costs.²

5. Financial viability and correcting the Regulated Asset Base for unrecovered regulatory costs

Covid-19's impacts resulted in large financial losses for all airports, including Dublin Airport. While it might be tempting for regulators and customers to argue that such losses be met by shareholders, two countervailing considerations need to be borne in mind.

Firstly, regulatory systems are generally expected to adjust to exceptional events, even if these have not been spelled out explicitly. The EU forum of national airport charges regulators (the "Thessaloniki Forum") has stated this in its January 2022 paper on '*Airport Charges in Times of Crisis*' in sections 4.12 to 4.15, where the paper states that where economic regulation does not compensate for exceptional circumstances, loss compensation should be considered.

Secondly, even if regulators would prefer to avoid this above responsibility, there is still good reason for action. Investors' perceptions of sector risk are formed not just by the theoretical design of regulatory frameworks but by their experience of how regulation has operated in practice, particularly when confronted by an exceptional crisis and truly transformative losses and financing strains. This is discussed below regarding the Cost of Capital.

What therefore might seem like an easy win for customers will not be so if the longer-term consequences for investor risk appetite are factored in.

Debt as well as equity investors are interested in the functioning of the regulatory system – credit rating agencies are likely to look for evidence of regulatory support in assessing airports' risk.³

5. Cost of Capital

The CAR is correct to update key parameters of the 2019 Determination for the Cost of Capital.

The Covid experience makes airports a fundamentally more risky proposition for equity investors. There is already evidence of this in the marked and sustained increase in airport equity betas since the crisis.

This clearly indicates that **a Covid-like event was not previously priced in.** The crystallisation of a (previously theoretical) global pandemic risk and the arrival of war on Europe's borders are bound to affect equity investors' perceptions and appetites.

While volume risk was already inherent in the airport business in a way it is not in other regulated industries (such as water, electricity or telecommunications), the impact of recent events is of a scale not seen since the emergence of modern air transport.

² This for example is explicit in the United States Federal Aviation Administration's policies on rates and charges, which states that in a single till ("residual") regime, aeronautical users may be cross-subsidized, and they "in turn agree to assume part or all of the liability for non-aeronautical costs".

Policy Regarding the Establishment of Airport Rates and Charges, 2.1.1, United States Federal Aviation Administration.

³ CAP 2014, UK CAA, para 3.43

Correctly addressing the Cost of Capital and investor perceptions is critical. If ignored or diminished, then the consequence will be less airport investment at higher costs in the future with adverse consequences for airport customers.

6. Environmental Sustainability

It is important to recognise here the **additional pressures entailed by governments' greenhouse gas reduction commitments**.

Without little access to public subsidies for green/decarbonisation investment, airports need to be in a position to self-finance what may be more expensive investment. Capital expenditure that achieves higher standards of energy efficiency and that enables airports to achieve decarbonisation and net zero goals comes with a cost premium. This premium has been estimated at 8% for greenfield capex, and 14-19% for brownfield capex.⁴

Furthermore, consumer expectations increasingly expect the entire travel eco-system to take sustainability focused action. A November 2021 study found that 83% of travellers would make sustainable travel a priority.⁵

The CAR should factor in this prospective view from travellers for the quality factor – measured by environmental performance – of the airports that they use, and the ability of the airport to fund this.

7. Conclusion

The issues paper is focused issues for a full building block review via adjustments to each building block. Paragraph 4.6 states that the CAR does not intend to change this approach as part of this review. The fact that so many and such significant adjustments are necessary points towards **the need for regulation to move in a direction that would mirror better the realities of the commercial world**.

The model of regulation designed for stable utilities is simply not fit for the fast moving, commercial and uncertain world of airports. As ACI EUROPE has previously reported, all airports have to compete at the margin and for important segments of their business.⁶ Those **competitive pressures are likely to strengthen in the aftermath of Covid**. That happens in normal times and is only likely to intensify post-Covid.⁷ The evolution of the airport marketplace should likewise merit reflection on the continued form and approach to economic regulation of Dublin Airport.

Dublin Airport needs to be ready to serve travellers to and from Ireland and support investment and trade with Ireland. ACI EUROPE has long supported research about the economic value creation supported by airports.⁸ This requires adequate future capacity to serve demand and expectations of airport service quality, related to airside operations and terminal facilitation. Taking resources off Dublin airport or pushing efficiency factors that cut to the bone will only harm the investment and service quality needed by the people using the airport in the short and long run.

⁴ ACI Global Outlook of Airport Capital Expenditure Report, Oxford Economics (July 2022). Commissioned by ACI WORLD.

<https://www.oxfordeconomics.com/recent-releases/Global-Outlook-of-Airport-Capital-Expenditure>

⁵ New report from WTTC and Trip.com Group reveals latest consumer trends and the shift in traveller behaviours (Nov 25, 2021) Trip.com Group. <https://www.trip.com/newsroom/trip-com-group-wttc-release-trending-in-travel-report/>

⁶ "The continuing development of airport competition in Europe", Oxera (September 2017) <https://www.oxera.com/insights/reports/the-continuing-development-of-airport-competition-in-europe/>

⁷ "Budget airlines put squeeze on airports in coronavirus cost drive," Reuters (May 28, 2020); <https://www.reuters.com/article/us-health-coronavirus-airlines-airports-idUSKBN2341JL>

⁸ <https://www.aci-europe.org/industry-topics/industry-topics/15-economics-finance.html>

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