Alternatives for Management and Operation
LA/Ontario International Airport

Prepared for Los Angeles World Airports

August 2, 2010
Organization of Materials

- Situation assessment
- Benchmark results
- Alternatives for improving financial operations
- Next steps
Situation Assessment

Key Points

1. Previous forecasts expected ONT passenger traffic to grow rapidly, but the most recent (December 2009) Terminal Area Forecast (TAF) suggests that ONT will not return to FY 2008 passenger levels until 2040 (1.5% average annual growth rate)

2. The reduction in passenger traffic has resulted in a substantial increase in airline cost per enplaned passenger (estimated to increase by more than 50% in FY 2010 versus FY 2008)

3. ONT has long-term strategic value as the only airport in the LA Basin without capacity constraints, but the realization of this value is dependent on airline service decisions largely outside of LAWA’s direct control

4. Reducing CPE alone would not result in an increase in air service from incumbent airlines in the short-term, but doing so could be an important step in the long-term growth in air service from incumbent airlines and in attracting competitive air service from new-entrant airlines
Recent Trends in Seats at Selected West Coast Medium-Hub Airports

Key Points
- ONT has experienced the largest seating capacity reductions of selected West Coast medium-hub airports
- OAK experienced similar decreases in total seating capacity

### Percent Change in Scheduled Departing Seats at Selected West Coast Medium-Hub Airports

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Recent Trends in Enplaned Passengers and Seats at ONT

Key Points

- Enplaned passenger trends stabilized in the first half of 2010 but remain below 2009 levels.
- The number of scheduled departing seats at ONT has decreased in each month since April 2008 and is expected to decrease further through the end of 2010 (based on advance schedules).

MONTHLY TRENDS IN ENPLANED PASSENGERS AND SEATS
Ontario International Airport

ONTr’s New Baseline—*Forecast Long-term Growth in Enplaned Passengers*

**Key Points**

- As the only airport in the LA Basin with few capacity constraints, prior forecasts assumed that ONT would capture an increasing share of regional passengers
  - The airlines implicitly acknowledged this long-term value in their 2009 decision to extend their airline agreements, despite the fact that ONT’s CPE was the highest of any LA Basin airport and was expected to increase
- Facilities and operations at ONT were planned and sized based on historical rates of growth and those forecast by the FAA and others
- The drastic traffic reductions in FY 2008 and 2009—unforeseeable a short time ago—have shifted ONT’s baseline FAA forecast of enplaned passengers *down* by 7 million enplaned passengers in 2040

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### Forecast Enplaned Passengers

*LA/Ontario International Airport*

- Historical
- 2005 TAF (3.3% annual growth)
- FY 2008
- 2009 TAF (1.4% annual growth)

-7m enplaned passengers
The chart below shows a comparison of the CPE for ONT and other medium hub airports and the average yield from those airports. (Yield is a reasonable proxy for the airline revenue potential at each airport.)

ONT generates yields slightly less than the medium-hub average (but yields would be lower if stage lengths were at the U.S. medium-hub average)

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**Yield vs. Cost per Enplaned Passenger**

Selected Medium-Hub Airports

- **ONT** = Ontario
- **SMF** = Sacramento
- **TUS** = Tucson
- **RNO** = Reno Tahoe
- **ABQ** = Albuquerque
- **SNA** = John Wayne
- **BUR** = Burbank

Benchmark Results—ONT versus other Medium Hub Airports

**Key Points**

1. ONT was compared with both a large-basket (37 airports) and small-basket (6 airports) of medium-hub airports (the benchmarking approach is explained in the Appendix)

2. ONT’s CPE is among the highest of comparable airports due to:
   a. The drastic decrease in passenger traffic since 2008
   b. High unit O&M expenses (partly the result of the decrease in passenger traffic)
   c. The benchmark analysis suggests that decreased costs and increased nonairline revenues could be achieved at ONT
**Key Points**

- Airline rates and charges are a product of each airport's airline agreement and its operating results.
- ONT's CPE is among the highest of medium-hub airports.
- ONT's CPE is the highest of any LA Basin airport.
- CPE does not include the $4.50 passenger facility charge.

- Under the existing airline agreement, airline revenues accounted for about 60% of FY 2009 revenues.
- Despite the trends, the airlines did not opt out of the airline agreement in 2009. The next option for the airlines to terminate the agreement occurs in 2014.
- Orange County/John Wayne Airport (SNA), comparable to ONT with a similar level of customer service and distance from Downtown LA, has a CPE of approximately $10.
  - At ONT, approximately $12 million in annual savings (any combination of reduced expenses and increased revenues) would be required to achieve a $10 CPE and maintain the required debt service coverage ratio.
On the whole, ONT generates greater nonairline revenue per passenger than the U.S. medium-hub average, due to high-performing rental car and advertising contracts and land and building rentals.

The largest nonairline revenue contract is public parking operations, which expires in 2012.

LAWA has the opportunity to change the business terms of contracts to improve financial performance in FY 2011 and 2012 (retail and public parking), 2013 (food and beverage), and 2015 (rental car) as contracts expire.

Key Points:

- Public parking revenues were 23% of FY 2008 revenue and is the largest nonairline revenue source.
- Rental car privilege fees were 11% of FY 2008 revenues.
- Retail concession revenues were 2% of FY 2008 revenues.
- Food and beverage concession revenues were 1% of FY 2008 revenues.

Source: FAA Form 5100-127.
Key Points

- The achievability of O&M expense efficiencies primarily depends on the proportion of fixed to variable costs and LAWA’s contracts with employees and service providers.
- Comparable information for terminal building M&O was not available for all medium hub airports.

Total M&O Expenses

- ONT’s total operating expenses per enplaned passenger are more than twice as high than the average for U.S. medium-hub airports.
- From FY 2008 to FY 2009, ONT had the third highest reduction in O&M expenses of the benchmarked medium hub airports.

Terminal Building M&O Expenses

- ONT’s terminal building M&O expenses per square foot rate in the terminal buildings (excluding expenses allocable to parking and roadway operations) is approximately $80, higher than the comparable airports shown below.
- Part of the inefficiency at ONT may be attributable to the cost of maintaining and operating two unit terminals (also the case with SMF and SJC).

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Benchmark Results—Operating and Maintenance (M&O) Expenses

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Key Points

- All LA Basin airports charge a $4.50 PFC per enplaned passenger.
- The $4.50 PFC for ONT pays for noise mitigation improvements, in-line baggage screening implementation, Runway 8L/26R reconstruction, and other improvements (shown in chart).
- A lower PFC rate—without changing the original purpose and intent of the PFC—may be one strategy to make ONT more competitive.

Remaining PFC Authority
LA/Ontario International Airport
(amounts in millions)

- Noise mitigation, $50.1
- Runway 8L/26R reconstruction, $15.6
- IT security implementation, $16.9
- In-line baggage screening, $19.4
- Other projects, $11.4
- Total remaining authority: $113.4m

Source: LAWA records.
Alternatives for Improving Financial Operations
## Overview of Alternatives—Short-term Actions and Potential Long-term Solutions

<table>
<thead>
<tr>
<th>Overview</th>
<th>Short-Term Actions</th>
<th>3&lt;sup&gt;rd&lt;/sup&gt; party Terminal and Parking Concession Agreement</th>
<th>Long-term Concession Agreement</th>
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<tbody>
<tr>
<td>Overview</td>
<td>LAWA continues to operate ONT pursuant to the existing airline agreement and implements certain operational improvements to improve financial results and lower CPE</td>
<td>LAWA enters into a concession agreement with a 3&lt;sup&gt;rd&lt;/sup&gt; party that is responsible for operation and maintenance of the terminal facilities, concession program, public parking and rental car</td>
<td>LAWA enters into a long-term concession for the operation and management of ONT; LAWA would maintain ownership of the airport and would continue to be responsible for safety and security</td>
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<tr>
<td>Responsibilities</td>
<td>LAWA continues to manage and operate ONT</td>
<td>3&lt;sup&gt;rd&lt;/sup&gt; party operates terminal and parking; LAWA continues to manage airfield and any other areas not managed by 3&lt;sup&gt;rd&lt;/sup&gt; party</td>
<td>Concessionaire operates entire airport</td>
</tr>
<tr>
<td>Effect on air service and regionalization</td>
<td>Operating efficiencies would lower airline costs and could create an opportunity for increased air service from incumbent airlines and/or service from new entrant airlines. The PFC rate could also be lowered to provide a perceived increased in competitiveness among LA Basin airports</td>
<td>Third party operator is incentivized to increase passenger traffic to obtain benefits of increased revenues from parking and terminal concessions ($31m, or approximately 40% of ONT revenues in FY 2009)</td>
<td>Optimal alignment of concessionaire financial interests with increasing passenger traffic would likely result in the greatest possible air service and regional benefits</td>
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<tr>
<td>Term</td>
<td>Immediate</td>
<td>20-30 years</td>
<td>40-60 years</td>
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<td>Capital structure</td>
<td>Existing LAWA bonds remain outstanding; LAWA could potentially use cash to pay debt service on a near-term basis (to be repaid at a later date) to reduce further the CPE</td>
<td>Existing bonds remain outstanding; additional capital expenditures (if any) are funded with new revenue bonds issued by LAWA providing a low cost of capital to the 3&lt;sup&gt;rd&lt;/sup&gt; party operator</td>
<td>Cash and upfront sale proceeds are used to defease outstanding bonds; concessionaire would provide new debt and equity to fund working capital and projects</td>
</tr>
<tr>
<td>Operating efficiencies</td>
<td>Further reductions in variable O&amp;M expenses may be possible within the limits of LAWA’s contracts with employees and vendors</td>
<td>Third party incentivized to gain maximum reductions in operating expenses in the terminal buildings and landside operations (parking, ground transportation, and rental car)</td>
<td>Concessionaire is incentivized to gain maximum reductions in operating expenses from all facilities</td>
</tr>
<tr>
<td>Operating revenue enhancements</td>
<td>Negotiate more advantageous terms for LAWA in the management of public parking and for retail concession agreements to achieve increased nonairline revenues</td>
<td>Third party incentivized to gain maximum increase in net revenues in the terminal buildings and landside operations (parking, ground transportation, and rental car)</td>
<td>Concessionaire is incentivized to gain maximum increases in operating revenues</td>
</tr>
</tbody>
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Next Steps
Next Steps--Options

Provided below are possible next steps examining options for the operation and management of ONT. As a general rule, the benchmark results need to be evaluated in greater detail to understand why some airports outperform ONT, but in general, the approach would be to take some immediate short-term actions potentially in parallel with longer-term changes. The identified options are as follows:

- **Option 1:** Rely on the rate-making methodology of the airline agreement to guarantee the financial operations of ONT, and take only conventional actions to manage revenues and expenses prior to the next airline termination option date (October 2014)

- **Option 2:** Prior to the next airline termination date and if Southern California traffic demand evidences signs of recovering, initiate strategic changes, such as reducing the PFC level and abating debt service with cash

- **Option 3:** Issue an EOI or RFQ to solicit responses from companies that having interest in operating and managing ONT, or from the City of Ontario. This would allow LAWA to specify broad based goals and objectives and to receive input from these companies on (a) the level of financial improvement that could be attained under private management and operation and (b) the types of rights and responsibilities outside a municipal structure that would allow them to achieve LAWA’s stated goals and objectives

- **Option 4:** With Option #2, further define how the operation and management options would have to be structured in order to achieve the goals and objectives of LAWA, and move towards the issuance of a competitive solicitation for one of those two options
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August 2, 2010
Appendix
**Benchmarking Approach—**Benchmarking Approach—Comparison Set of Data

- **Key Points**
  - ONT was compared against both a large basket average (37 airports) and small basket average (6 airports) of airports.
  - Data from FAA Form 127 financial reports filed by airport operators with the FAA for the most recent year (2008) and the 2009 Airport Revenue News Fact Book were used.
  - For benchmarks to be meaningful, qualitative comparisons are also important.

- The comparison set included:
  - A **large basket** of all 37 U.S. medium-hub airports was used to calculate average metrics for use in comparing with ONT.
  - A **small basket** of medium-hub airports located in the Western U.S. (with emphasis on California) with activity levels comparable to ONT was used to facilitate more detailed, one-on-one comparisons with ONT.

- It is important to remember that the characteristics of the data may distort comparisons:
  - Some of the large-basket airports are in locations that require significant amounts of snow removal or other operational costs (e.g., reliever airports) that do not exist at ONT.
  - The difference in traffic levels between the largest medium-hub airport (PDX, with 7.1m passengers in 2008) and the smallest medium-hub airport (SDF, with 1.8m passengers in 2008) is significant, which is important given the facility and infrastructure requirements of larger medium hub airports.
  - The effects of the national economic downturn on regional economies has been different, with most areas not experiencing the magnitude of effects as has been experienced in the Inland Empire.
  - Benchmarks were generally calculated on the basis of 2008 enplaned passengers (approximately 3.0m); since ONT experienced among the highest decline in passengers of any medium-hub airport (forecast 2.4m in 2010), ratios for O&M expenses per enplaned passenger are significantly understated.

### 37 U.S. Medium-Hub Airports

As Ranked by Enplaned Passengers in 2008
6 small basket airports and ONT in blue

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<tr>
<th>Airport</th>
<th>City, State</th>
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<td>PDX</td>
<td>Portland, OR</td>
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The FAA classified medium-hub airports as those airports with at least 0.25%, but less than 1.00% of total U.S. passenger enplanements for a given year.