Port of Seattle

ITEM NO. 9a Supp

DATE OF MEETING August 18, 2009

# Aviation Division 2010-14 Business Plan Overview

August 18, 2009

# Outline

- Airline Industry
- Outlook for Sea-Tac
- Strategic Goals
- Challenges
- Strategies

# Airline Industry

- Strength of economy is major driver of travel demand
- Amid worst recession in generations
- Airlines:
  - Lower demand, particularly for “front of airplane”
  - Revenue dropping faster than passenger levels
  - Higher, volatile fuel costs
  - Strategy:  new fees and additional round of capacity cuts are latest additions to longstanding cost cutting
  - Staggering losses since 2001 leaves little capability to absorb additional losses

# Airline Industry Outlook

- As economy begins to recover, demand for travel will likely lag
- Have new video conferencing and webinar tools significantly altered demand for business travel?
- Experts say domestic industry still has too much capacity
  - Recent airline announcements indicate capacity cuts are coming
  - Will cuts be enough to improve profitability?
  - If not:  merger, bankruptcy, liquidation?
- How will needed capacity cuts affect Seattle market?
- Competition-induced capacity bubble on west coast?

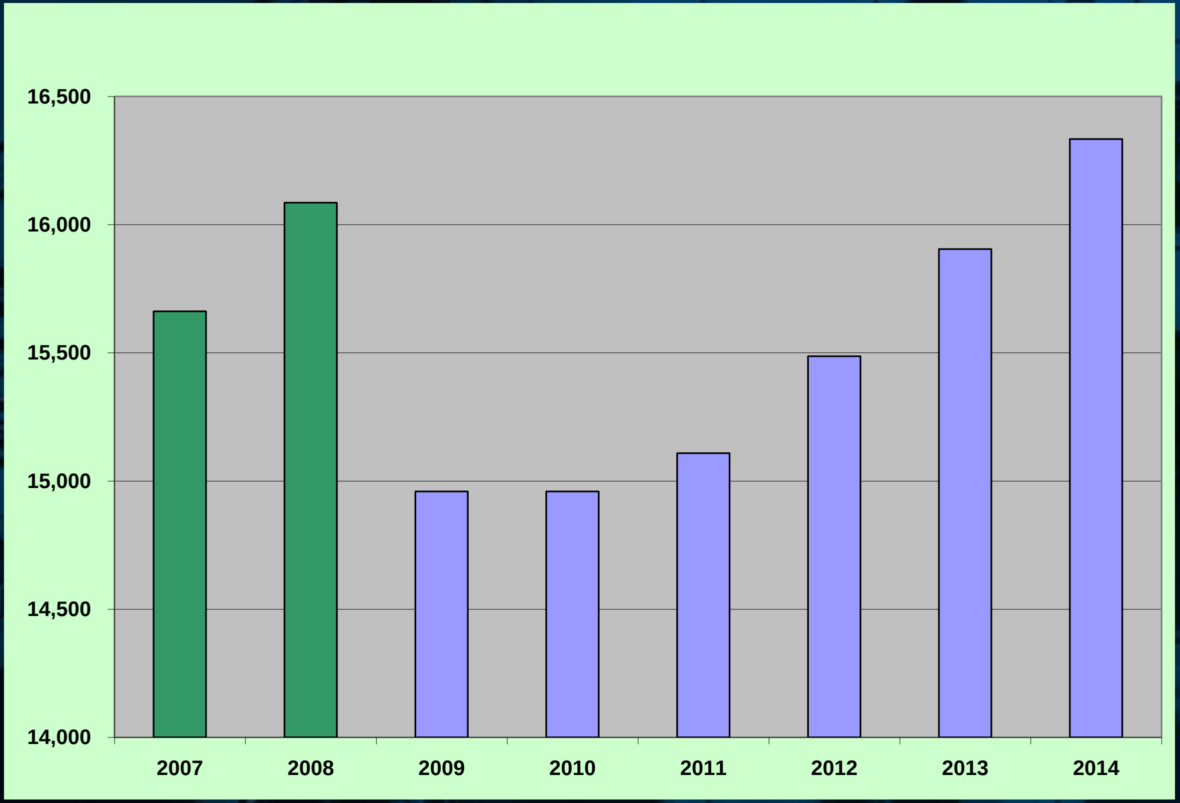
# Outlook for Sea-Tac

- Diverse mix of carriers
- Strong origin and destination base
- Reasonably balanced economic base in Puget Sound
- Largest carrier (Alaska) has strong cash position

- Conclusion:
  - SEA traffic holding up better than most airports
  - Do not expect “V” shaped rebound

# Enplaned Passenger Forecast
(Preliminary)

| Year | Assumption |
|---|---|
| 2009 | -7.0% |
| 2010 | 0.0% |
| 2011 | 1.0% |
| 2012 | 2.5% |
| 2013 | 2.7% |
| 2014 | 2.7% |




- Not typical recovery; no sharp rebound
  - Travel demand may pick up in late 2010 as economy improves, but capacity cuts and/or increased fares may dampen demand
- Growth rate in out years reflects FAA long-term forecast (2.7%)
- Continuing to review and refine forecast

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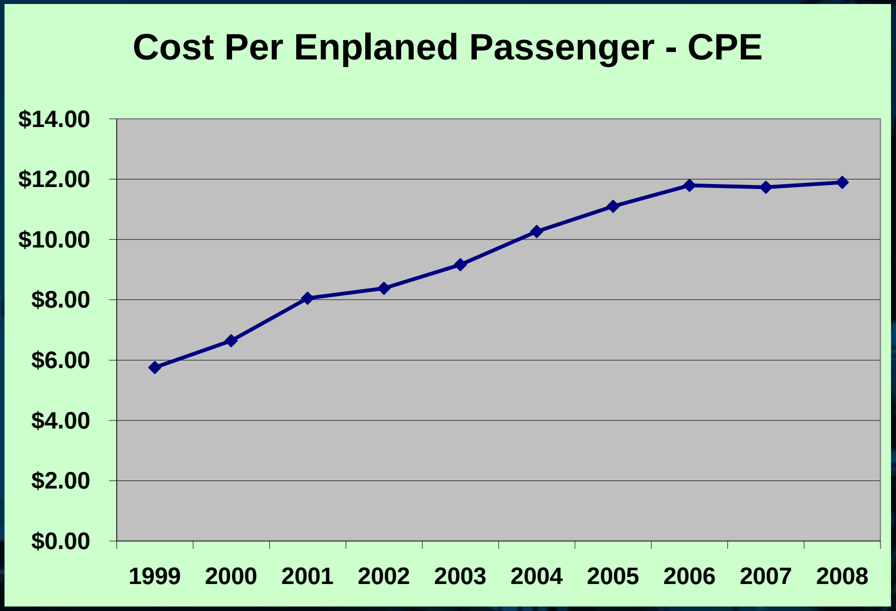
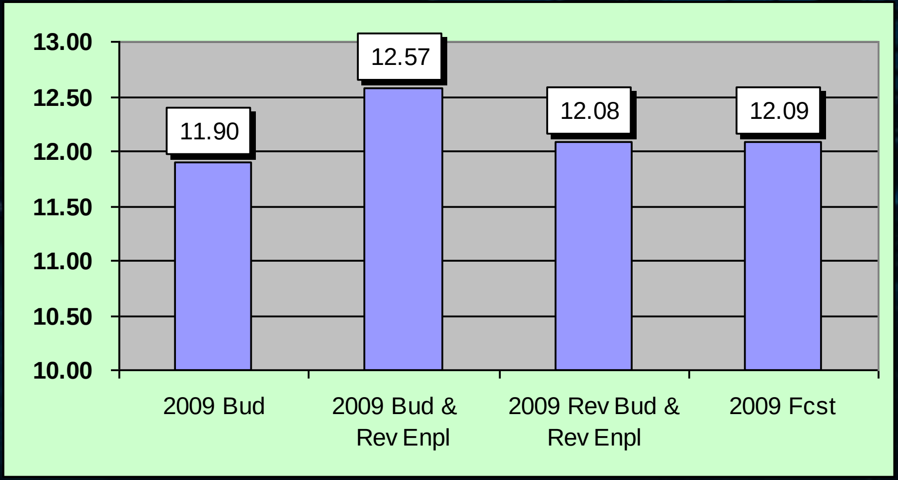
# Strategic Goals

Given crisis facing airline industry, Sea-Tac has two overriding goals:

1. Manage airline costs
   - Cost per Enplanement
2. Increase non-aeronautical Net Operating Income
   - Debt service coverage
   - Cash fund capital improvements

# CPE History




- Growth in CPE due to capital spending
- CPE flat for three years (2006-8)
- 2009 budget cuts mitigated increase due to falling enplanements
- Challenge for 2010 is that most 2009 budget cuts were not sustainable

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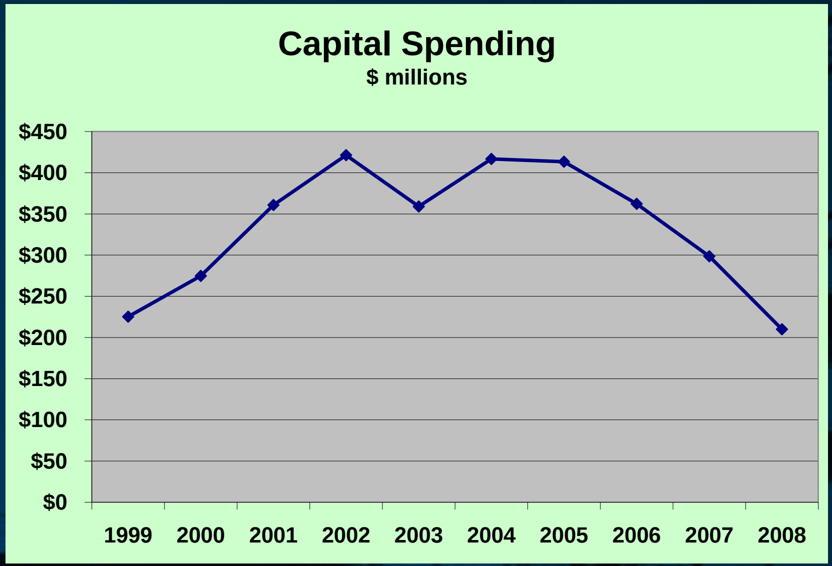
# Challenges – Managing O&M Costs

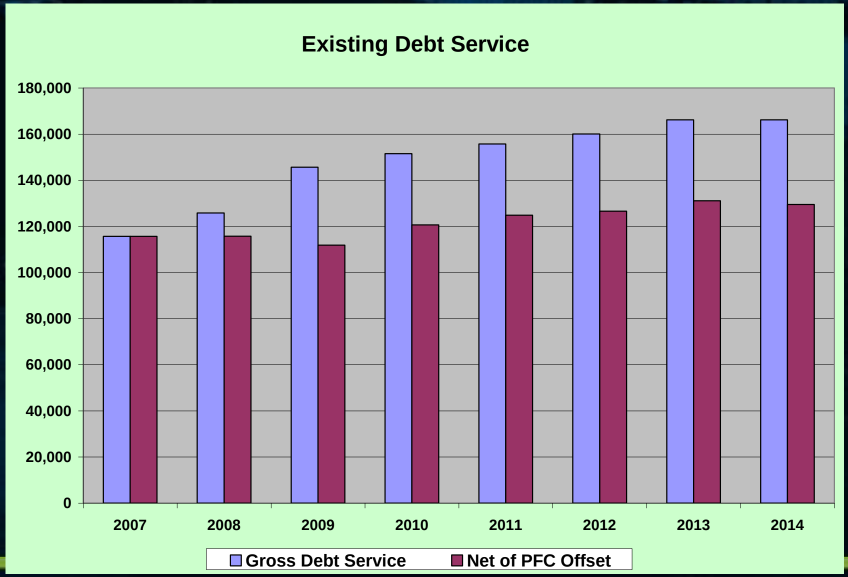
| 2009 Budget | $ (000's) | AV % | % |
|---|---|---|---|
| Payroll | 84,777 | 64% | |
| Outside Services | 23,737 | 18% | |
| Utilities | 13,571 | 10% | |
| Other | 10,580 | 8% | |
| Total Aviation | 132,665 | 100% | 70% |
| Corp/Police/CDD | 56,856 | | 30% |
| Total | 189,521 | | 100% |

- Payroll costs are major component
- Corporate costs also large, as AV receives ~ 70% of Corp Costs
- Implications:
  - Reducing costs requires reducing FTEs
  - Corporate decisions have significant impact on airport

- Cost drivers include:
  - Square footage of terminal
  - Acres of airfield pavement
  - Lineal feet of baggage system
  - Number of elevators and escalators
  - Few costs directly tied to enplanements
- Need budget capacity for new initiatives:
  - Part 150 study
  - Maintenance for elevators & escalators
  - Wetlands adaptive management

# Challenges – CIP and Debt Service



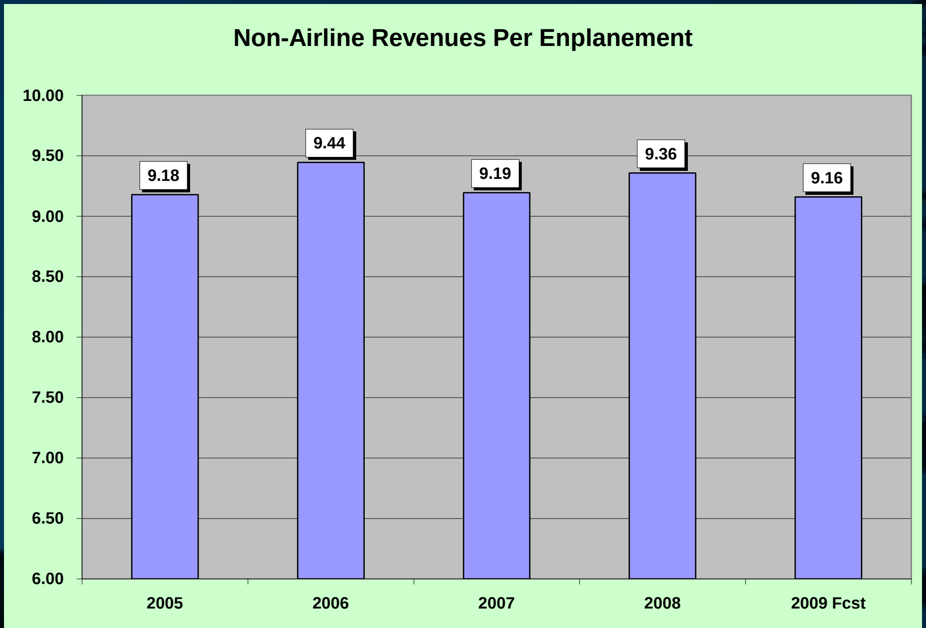



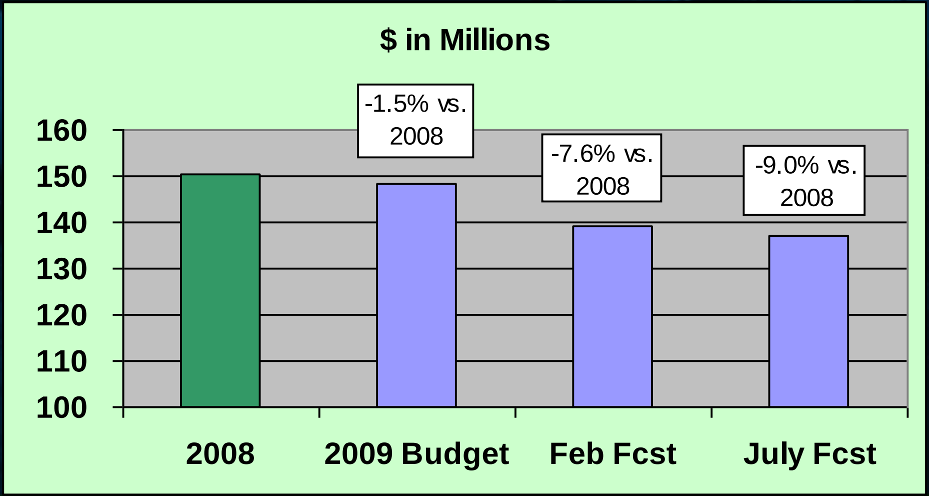

- Spent $3.5 billion since 1999
- While capital spending is falling, existing debt service will rise through 2013
- Use of PFCs to offset revenue bond debt service is key to managing CPE
- Necessary new debt-funded spending in 2010 and beyond will add to cost structure

# Challenges – Capital Spending Needs

- Maintaining operational integrity of facility and equipment requires ongoing reinvestment
- Airline industry consolidation/cost saving strategies are driving facility changes & costs:
  - Delta and NW on South Satellite
  - Alaska move to North Satellite
  - United and Continental?
- Capital costs drive increases in CPE – challenge is to strike the right balance

# Challenges – Non-Aeronautical




- Compared to recent years, revenues per enplanement are down slightly
- Actual dollar decline compared to 2008 is significant
- Fewer passengers, spending fewer dollars
  - Parking: revenues down 17% while passengers down 5%
  - Concessions: drop in sales per enplanement
- Depressed market for property development
- Airline relocations have depressed business for concessionaires on Concourses A and D
  - Difficult time to invest in new facilities/concepts

# Strategies

1. Manage/reduce operating costs
2. Restore/develop/defend non-airline revenues
3. Prudent capital investments focusing on:
   – Renewing existing assets
   – Customer needs
   – Common-use systems -- implemented opportunistically

# Manage/Reduce Operating Costs

- Reducing O&M contributes to both strategic goals:
  - Reduced airline costs, CPE
  - Improves non-aeronautical NOI
- For 2010 budget, Aviation initiated business unit reviews and zero-based budget process to achieve 5% reduction target, Port implemented voluntary separation program (VSP)
  - Identify non-critical functions
  - Sustainable for current traffic levels
- Future:  maintain focus on managing costs
  - Benchmark key functions
  - Process improvements, “Lean” efforts
  - Explore airline consortium initiatives

# O&M Reductions for 2010

- How we “hit” target:
  - – Payroll: No furlough; normal salary & wage increases, flat benefits cost
  - – Eliminate 73.5 positions – half empty; half filled
    - Scaled back on level of customer service
  - – Eliminate renewable energy purchase
  - – Assume $1.5 million savings from VSP
- FTE summary

| | |
|---|---|
| – Positions to be cut: | 73.5 (8.8%) |
| – Eliminated positions occupied: | 37.5 |
| – Open positions (to be filled): | 12.0 |
| – Voluntarily separating: | 7.0 |

# Restore/Develop Non-airline Revenues

- Public parking: Explore new products and innovative services to win back customers
- Increase advertising through value-added promotion programs
- Develop advertising on Port's Wi-Fi home page and web site
- Concessions: Expand array of products and services
- Property development: Continue pre-development activities with City of SeaTac, Burien, and Des Moines for under-utilized property

# Prudent Capital Investments

- Focus investments on maintaining and renewing existing assets. Many projects competing for approval:
  - Key Aeronautical assets such as:
    - Runway 16C
    - Airfield pavement
    - Baggage systems
    - North Satellite: mechanical, seismic
  - Key Non-aeronautical assets:
    - Garage, revenue control system
    - Freight elevators, grease ducts
- Selective new investments to:
  - Accommodate customer needs:
    - Delta club
  - Enhance productivity of facility to achieve cost savings for airlines and/or airport
    - Electrify ground service equipment
- Prepare facilities to maximize capacity and flexibility of existing footprint with common-use equipment
    - CUSE expansion

# Summary

| | Actual 2008 | Fcst 2009 | Preliminary Forecast 2010 | 2011 | 2012 |
|---|---|---|---|---|---|
| NOI ($ millions) | 163.1 | 163.0 | 164.1 | 176.5 | 190.5 |
| D/S Coverage | 1.42 | 1.43 | 1.36 | 1.31 | 1.27 |
| CPE (2009 Cap Bud) | 11.89 | 12.09 | 12.78 | 13.86 | 14.29 |

- NOI stable in near-term, growing in future
- 2010 operating budget will reflect need to reduce operating costs to achieve aeronautical and non-aeronautical goals
  - Maintain strong debt service coverage
  - Reduce aeronautical operating costs to mitigate rise in CPE due to increasing debt service
- 2010-2014 capital budget will reflect need to renew existing assets
  - Timing and priority balanced against need to moderate growth of CPE