



Innovative agreement sets new industry standard, say airport and airline officials

Terms of IND agreement will remain in effect through 2015

INDIANAPOLIS—The Indianapolis Airport Authority Board today approved what both airport and airline officials say is the most collaborative, forward-thinking airline use agreement in its 80-year history.

The agreement is the foundation upon which airlines will operate at Indianapolis International Airport (IND) for the next five years. It determines airline costs for doing business at IND and defines the rates and charges the airport authority will assess for leased space in the terminal, landed aircraft weights, and parking on the tarmac, among other key business operations.

Collectively, these costs are known in the industry as cost per enplanement (CPE), which has a major impact on the bottom-line profitability for airline operations at specific airports. In most U.S. cities, the rates airlines pay are forecasted to increase. In Indianapolis, however, those costs will actually **decrease** steadily over the next five years, which will make Indianapolis International more attractive for additional or expanded air service.

According to Executive Director & CEO John D. Clark III, the airport authority began the process of negotiating acceptable terms for the agreement—which takes effect January 1, 2011 and continues through December 31, 2015—nearly a year ago.

“Despite the turbulence and financial strain in the industry, we were committed from the outset to efficiently and creatively craft an agreement that would satisfy the dual objectives of both the airlines and the airport,” Clark reports.

The end result is a stronger, more solid working relationship between the airlines and the authority that will benefit the entire central Indiana region, he said.

“The lower projected rates put us in a very favorable position. Equally important, we believe this agreement demonstrates our door is wide open for continued dialogue with airline executives about new and expanded air service in Indianapolis, especially to key West Coast markets,” adds Marsha Stone, IAA’s chief financial officer.

Notably, both airport and airline officials describe the negotiation process as “refreshing.”

Airline executives say the Indianapolis agreement is not typical, especially among those like IND who have made significant financial investments in new, state-of-the-art facilities. The framework and terms have generated praise from Delta Air Lines, among others.

Based on her experience, says Pam Drenner, regional director of corporate real estate and airport affairs for Delta Air Lines, the Indianapolis agreement “changes the landscape” for airline use agreements at other airports.

“The corporate culture set forth by the airport leadership in Indianapolis is one founded in sound business acumen, strict cost control, the importance of robust revenue development, and an acute awareness of the need for a sustainable win-win strategy,” finds Drenner. “This makes us true business partners. That is not always the case at other airports.”

Drenner notes IAA’s agreement creates a favorable lease structure with incentives for both parties while ensuring an affordable, predictable cost structure for the airlines. It will also help ensure the long-term success of IND’s new facilities while yielding a positive impact on central Indiana’s economy.

As a commitment of service to IND, Delta will open a \$2.5M new SkyClub at IND just before the new agreement takes effect. “We have increased our lease footprint, up-gauged flights to mainline aircraft, worked with the airport to ensure priority screening and will be rolling out more SkyPriority amenities. Meanwhile, our network team continues to work with John Clark, Marsha Stone, and other airport officials to explore the feasibility of adding new routes.”

Adds Amy Weaver, properties manager for Southwest Airlines, “These negotiations have given the industry an example of an airport that spent an extraordinary amount of money on a new terminal, yet when it was all said and done, they have also made extraordinary changes to keep it affordable for airlines.”

OVERVIEW & HIGHLIGHTS

- Signatory airlines bear the financial risk and fund the net cost of operations at IND. No state or local tax dollars are assessed or used to fund airport costs.
- Terms are residual. Signatory airlines will receive credit from IAA’s nonairline revenue and, in exchange, they agree to cover revenue shortfalls and cost increases, should they occur.
- Declining, not increasing, CPE for the period 2011–15. Of those U.S. airports listed in Table 1, IND is one of just two forecasting declines; Raleigh-Durham International (RDU) is the other.
- Allows IAA to provide competitive rates, fund its capital program, maintain adequate liquidity to cover debt and expenses, and not take on new debt. Maximizes leasing flexibility to attract new tenants.
- Includes reductions to IAA operations and maintenance costs from previous forecasts; decrease expected to be a total of \$65M by 2015, achieved through ongoing efficiency initiatives and activities.
- Requires no majority-in-interest (MII) vote among signatory airlines for IAA capital projects not funded by bond proceeds. In turn, IAA has reduced its capital improvement program (CIP) by \$150M over term of agreement as compared to previous forecasts.
- Begins with 2010 CPE at more than \$10.50 per passenger; by 2015, that amount is forecasted to decline to \$8.86 per enplaned passenger. Prior to completion of the agreement, projected costs approached \$13 per passenger.

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- 2011 rate for leased terminal space remains constant at \$95 per sq. ft; leased space for tarmac parking decreases to \$1.86. Both rates will decline by about two percent between 2012–15, whereas previous forecasts reflected increases in excess of 30 percent.
- Helps ensure continued success of FedEx with competitive landing fee of \$1.95 per 1000 lbs. Fee is forecasted to drop to \$1.80 per 1000 lbs by 2015. Previous forecasts called for landing fees to increase to over \$2.15 per 1,000 lbs. Cargo and passenger carriers worked cooperatively with IAA to ensure business costs for FedEx, which is vital to the central Indiana economy, remain affordable.
- Includes no amortization of cash-funded capital projects; reduction in possible amortization charges could save airlines about \$10-15M/year or a total of approx. \$65M by 2015.
- Airline charges of 12.5% for nonairline revenue up to \$90M or 62.5% for nonairline revenue that exceeds \$90M incents IAA to increase nonairline revenue forecasted; increased charge for revenue over \$90M could result in additional \$6.1M during term of agreement.
- Covers a five-year period; prior agreement was for ten years. Negotiations were completed in just under one year and prior to expiration of current agreement, which ends Dec. 31, 2010.

TABLE 1: IND COMPARISON TO OTHER U.S. AIRPORTS

Based on a five-year compounded annual growth rate, the following comparison between IND and other airports provides additional perspective.

Measure	IAA	Others*	Comments*
Enplaned passengers (EPAX)	1.5 percent	2.3 percent	IAA agreement is conservative in growth forecast
Cost per enplaned passenger (CPE)	-4 percent	4 percent	IND is one of two airports** forecasting a decrease in CPE between 2011 and 2015
Operation & maintenance (O&M) expenses	2.3 percent	5.2 percent	IAA forecasts are more aggressive in lowering O&M expenses
Nonairline revenue	2.2 percent	4.3 percent	IAA forecasts on EPAX growth are conservative
Airline revenue	-2.0 percent	6.4 percent	IAA forecasts are lower than average and are driven by 2010-15 strategic goals and objectives
Net debt service	-0.8 percent	6.6 percent	IAA forecasts are lower than average

* Other airport and/or airport authorities for whom current forecasting data is available include: Raleigh-Durham Airport Authority, Metropolitan Airports Commission (Minneapolis–Saint Paul International Airport), Metropolitan Washington Airports Authority (Washington Dulles International Airport and Ronald Reagan Washington National Airport), Memphis-Shelby County Airport Authority, Greater Orlando Aviation Authority, Miami-Dade County Aviation Department (Miami International Airport), Sacramento County Airport System (Sacramento International Airport), and Portland International Airport.

** Raleigh-Durham International Airport is the other airport forecasting declining CPE for 2011.

SUMMARY

No agreement of this nature is without opportunities and risks, however.

- **What are the potential opportunities?** Increases in nonairline revenues, increases in airline activity, and changes in federal funding or legislation (i.e., if the PFC rate in FAA reauthorization bill increases to \$7/passenger)
- **What are the potential risks?** Capital requirements exceed current forecast, decreases in airline activity, reductions in nonairline revenue, increases in O&M expenses, increases in debt service costs.

In summary, IAA has worked with the airlines to reduce its O&M costs, cut capital spending, and eliminate amortization expenses, creating a precedent-setting new airline use agreement covering the 2011–15 period.

- O&M costs reduced by six percent to an average of \$66M year (inclusive of expenses for the Indianapolis Maintenance Center, if any). IAA is committed to NO NEW DEBT over the term of the agreement.
- CIP funding was reduced by 66 percent, but still allows for a \$90M five-year program to include runway and taxiway rehabilitation projects, environmental protection, master planning, safety and equipment upgrades, security and IT enhancements, and revenue development initiatives.
- The agreement saves airlines \$10-15 million annually in amortization expenses, 100 percent of which are eliminated over the life of the agreement.
- In total, over the term of the agreement period, the airlines are expected to save nearly \$300M while being incentivized to sustain or increase passenger and cargo service.
- If enplaned passengers increase beyond the conservative 1.5 percent growth forecast, CPE could drop below \$8.

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ABOUT THE AUTHORITY

The Indianapolis Airport Authority (IAA) owns and operates Indiana's largest airport system. In addition to Indianapolis International Airport (IND), its facilities include the Downtown Heliport, Eagle Creek Airpark, Hendricks County Airport, Metropolitan Airport, and Mt. Comfort Airport. Indianapolis International Airport was named the best North American airport by J.D. Power and Associates serving under ten million passengers per year in 2010. IND's economic impact in central Indiana is more than \$3.3 billion annually and about 10,000 people work at the airport each day. According to U.S. Department of Transportation data, IND's average domestic air fare is one of the lowest in the nation. IND averages 154 daily departures to 35 nonstop destinations. Home of the second-largest FedEx Express operation in the world, IND is the eighth largest cargo facility in the U.S.