Auckland Airport

4 September 2015

Keston Ruxton
Manager, Market Assessment and Dairy Regulation Branch
Commerce Commission
PO Box 2351
Wellington 6140
By email

Dear Keston

Cross Submission on Commerce Commission's Input Methodologies Problem Definition Paper

Auckland Airport endorses and supports NZ Airports' cross-submission on the Input Methodology problem definition paper. In this letter we briefly outline additional submissions from Auckland Airport in relation to: (i) the impact on incentives to invest in airport infrastructure associated with mis-estimating the WACC range; (ii) land held for future use and; (iii) Auckland Airport's moratorium on asset revaluations.

Incentives to invest

BARNZ puts it to the Commission that there is no real risk of under-investment for airport infrastructure if it uses the mid-point as the benchmark WACC. Our position is that there is a real risk of under-investment in airport infrastructure where:

- the regulatory settings provide insufficient incentive to invest; or
- capital constraints that require the rationing of investment exist (which is the case, to some extent, in almost all commercial businesses).

There are examples across the globe where systems and incentives to invest in airport infrastructure have been insufficient. This has led to delays in investment, which, in turn, has resulted in sub-standard airport service levels.

Auckland Airport agrees with BARNZ that there are areas where airports will be compelled to invest (like projects to meet safety and security requirements). However, there is a broad range of demands for airport capital, across a range of interests and indeed segments of aeronautical customers. It is inevitable that capital must be rationed.

BARNZ sets out logical incentives that airports might have to provide appropriately sized facilities in order for passengers to be processed quickly and have time to shop. Yet, as illustrated in a number of overseas airports, there is often inadequate infrastructure for check-in and security facilities. For example, London-Stansted and Luton suffer poor waiting times and terminal congestion. The Economist has referred to American Airports as "shabby" and unworthy as an entrance to the country.[1] BARNZ asserts that public (or airport consumer) pressure provides adequate incentives to retain airport facilities and services at satisfactory standards. Our view is that public pressure is a slow and blunt tool for incentivising investment if the regulatory settings are wrong or financing constraints exist.

[1] 'America's awful airports - a new ranking', *The Economist*, 29 March 2014.

New Zealand airports have had a good reputation to date. This could be jeopardized by arbitrary changes to the WACC estimate for airports. Therefore, we caution the Commission against making material changes to the regulatory model whilst Auckland, Wellington and Christchurch airports are delivering sound quality outcomes.

Auckland Airport's 30 year vision is to build a world-class airport that supports airlines and aviation-related businesses to be economically successful and to boost Auckland's and New Zealand's economies. Over the next two years we will develop and test the 10 year capital programme necessary to support this. Auckland Airport is strongly committed to engaging on this programme with airlines operating at Auckland Airport. Our direct experience has been that the airlines engage constructively when testing proposals, but each of the 21 major airlines have different priorities. Their appetites and priorities for investment are influenced by their respective financial health, operating goals, views on the quality standards for customers and investment horizons. Any one of those might constrain both their ability and desire to cooperate with the airport in the best interests of passengers.

Moreover, passenger airlines are not the only segment of airport customers with capital requirements at the airport. General aviation and freight operators also seek support from the airport to invest in incremental assets to enable growth of their businesses. In an environment of capital rationing there is a risk of underinvestment across a range of airport infrastructure if incentives to invest are insufficient.

Assets held for future use

Auckland Airport is not surprised that BARNZ reiterates the rationale set out by the Commission for the development of the land held for future use input methodology. At the same time, it is silent on the matters raised at the recent problem definition forum such as:

- acknowledging that there may be alternative approaches to pricing that are consistent with workably competitive markets and;
- principles that might guide the reasonable evaluation of signalling the cost of increasing congestion.

The challenge for us with land held for future use for the northern runway remains that, as well as the actual build being a very challenging investment for Auckland Airport, creating an appropriate price path is not easy. Even if the land held for future use approach remains appropriate (once tax errors are corrected), it remains important to understand how the Commission would assess profitability in the event that an airport were to smooth prices in advance of commissioning an asset held for future use.

It is, in our view, inaccurate to characterise this issue as one of pre-funding asset yet to be built. The land asset is currently owned by Auckland Airport, and it is not our understanding that BARNZ considers that Auckland Airport is owning and holding the $235m of land imprudently. In fact, BARNZ has worked constructively with Auckland Airport on as part of the unitary plan process to protect for the future development of a northern runway. This is because it is important for the sector that we gain the necessary environmental approvals and preserve the ability to construct and operate the northern runway in the future. As discussed at the problem definition forum we have had discussions with Air New Zealand, Cathay Pacific, Emirates, Singapore Airlines, Virgin Australia and Airways, to test the proposed northern runway options and ensure that the preferred runway option is technically appropriate and justifiable and that its planned operation has support from the wider aviation industry.

Annual revaluations

Auckland Airport is in a unique situation compared to the other airports, in the sense that it entered in to a moratorium on asset revaluations prior to the development of the Input Methodologies. In this respect Auckland Airport would support the input methodology being changed to allow annual revaluations to be CPI *or* some other rate (e.g. zero). This would then place the onus on the airport to adequately explain the rationale for a departure from CPI.

If the Commission has any questions in relation to this cross submission please contact Adrienne Darling at Adrienne.darling@aucklandairport.co.nz.

Yours sincerely

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