The Global Financial Crisis (GFC) has heightened the focus on organisations needing to have a prudent approach to the financing of their operations. The GFC exposed organisations which had significantly leveraged themselves, or which had not had appropriate capital management policies and practices in place to the fallout from the market dislocation. This presented itself in many ways, including:

› Inability to refinance maturing debt
› Inability to raise debt and equity finance
› Much higher margins on debt and risk premiums for equity investment
› Significantly tighter lending conditions and restrictive lending covenants

Any one of these scenarios places the organisation under significant financial pressure and can have material consequences for shareholder value and potentially, the viability of the organisation.

Continued on page 2.
By Wayne Ticehurst (CPA), Consulting Director – Airport Finance & Governance

The first article in this series looked at the sources of financing for airports in Australia. In this article, we look at the key considerations that airports need to take into account when planning the capital structure for the organisation.

A prudent approach to financing an airport requires a sound understanding of key financing principles to ensure the capital structure of the organisation is suitable and that the organisation has an appropriate resilience to withstand unexpected shocks to the airport’s business and the financial markets.

The following factors need to be carefully considered when determining and in the ongoing management of the organisation’s capital structure:

1. Debt Service Capacity
   It is a well-established principle that introducing debt, or gearing into an organisation’s capital structure can assist in providing greater financial return to shareholders, as the cost of debt is almost always less than the cost of equity. Of course, gearing can also magnify losses to equity providers when financial and/or operating conditions deteriorate.

   The challenge for organisations is to achieve a balance in the funding of the organisation between debt and equity to achieve the optimal capital structure.

   An important initial task in assessing this balance is to determine the organisation’s debt service capacity. This can be measured in a number of ways, with the more common method being expressed as a ratio called the Debt Service Cover Ratio (DSCR) or sometimes the Interest Cover Ratio (ICR).

   These ratios can generally be defined as the ratio of operating cash flows to the interest (and ongoing cost) of debt. Obviously, the higher this ratio, the stronger the financial profile of the organisation (all else equal) and the greater the ability of the organisation to be able to withstand unfavourable trends in the operating environment or financial markets.

   A general indicator of a satisfactory DSCR would be where it is maintained at a ratio of > 1.8. That is, operating cash flows for a given period (usually determined over a 3 month period) are 1.8 times greater than the costs of servicing the debt.

   Clearly, in order to properly assess its debt service capacity, the organisation needs to look not only at its current performance but probably more importantly at its projected performance. This will help to identify future periods where funding may need to be augmented, for example – periods of greater capital expenditure. This may well require an injection of additional equity or at least retention of cash in the company for a period. It will also assist in identifying the impact of selected scenarios or sensitivity analysis on the organisation – for example, the impact of a change in interest rates or in the operating environment of the organisation.

   To undertake this analysis it is essential that the organisation has a sound financial model, constructed to an appropriate level of detail and with sufficient flexibility. Indeed, when seeking finance, it will be expected that the organisation has such a model. More on this in Part 3 of this series.

2. Tenor
   An important consideration of the organisation is to have a spread of debt tenor (duration), so that there is not a concentration of debt maturing at the one time in the future (refinancing risk).

   From the borrower’s perspective, having particularly onerous covenants can restrict financial and business flexibility, so this part of the borrowing process is particularly important and usually the subject of intense negotiations. As far as possible, borrowers should seek to familiarise themselves with a particular lender’s terms (or at least assess the lender’s track record) on covenants before formally committing to the process as this may be a differentiating factor between lenders, particularly in a climate which is conducive to borrowers.

   The tenor of the debt is linked to the pricing and to the source of debt. Depending on the state of the financial markets at a particular point in time, shorter dated debt may be priced more competitively, however the shorter maturity requires more frequent refinancing. Airports typically seek to have at least a portion of their debt funding as longer term, reflecting the long term nature of airport assets.

3. Pricing
   The pricing of debt has two dimensions.

   The first is the relevant interest rate, usually defined by reference to the Bank Bill Swap Rate (BBSW). This rate rises and falls depending on general economic conditions and Gov’t monetary policy.

   The second element is the particular credit margin that the lender will apply. This is determined by the lender’s assessment of the credit profile of the borrower (and often, the industry the borrower operates in), which among other things is informed by the debt service capacity of the borrower, and by the tenor of the debt.

   During the GFC and in the immediate aftermath, BBSW rates fell (and have continued to fall in response to Gov’t monetary policy); however credit margins widened considerably, reflecting both a heightened sensitivity by lenders and, particularly during the GFC, limited lending capacity. This has ameliorated significantly in recent months.

4. Covenants
   Depending upon the credit cycle a borrower is seeking access to finance, the credit history of the borrower and the lending parties’ own policies, lending covenants can vary greatly.

   Covenants are set out in the lending documents and are expressed as restrictions and understandings. These can range in coverage and complexity but will typically include negative pledges (things the borrower cannot do), information requirements, events of default and acceleration and enforcement provisions in the event the borrower breaches a key lending term.

   As previously noted, borrowers should avoid having a concentration of debt maturing at a given time. This exposes the organisation to refinancing risk, and can weaken the negotiating position of the borrower. The costs of refinancing should not be under-estimated. These will include legal fees, borrowing fees, as well as establishment and commitment fees as well as the costs of the borrower’s own staff (and any advisers) involved in the process.

   Refinancing need not necessarily be at the maturity of the existing debt. Favourable changes in operating and/or financial market conditions may present opportunities to refinance on more favourable terms. Due consideration needs to be given to any costs associated with refinancing prior to maturity, such as any borrower prepayment fees, and costs associated with early termination of hedges.

5. Capital Management Policies
   The organisation’s effectiveness in managing its capital structure is one of the most significant drivers of value to its shareholders. It is therefore important for the organisation to have a rigorous framework for managing this.

   This framework is a key part of this process. The capital management policies should, as a minimum describe the organisation’s policies and approach to each of the factors identified in this article.

   The next article looks at preparations the borrower should make when raising new capital or refinancing.
OLs Familiarisation Course – Brisbane
5th March 2013
TAG has introduced a 1 day OLs Familiarisation Course which is a summarised version of the popular 4 day OLs course. The introduction to OLs Familiarisation is free to all applicants. Further details are available on our website www.theairportgroup.com.au for more details.

Perth 10-12 April 2013
Course presentation to Jandakot and Perth Airports, as well as development industry and Council representatives.

Presentations at Aerodromes for Local Councils and Developers
TAG has been engaged to present together presentations to introduce the OLs and PANS-OPS concepts and the importance of aircraft protection in the vicinity of local aerodromes. These presentations are an important part of the communication between the airport, councils, developers and crane operators. Not only do they inform all parties the importance of protecting the airspace and understanding the regulatory requirements. Furthermore, the regulations also cover the effect and potential results of a surface infringement on both the developer and the airport operator. Presentations can be tailored for each aerodrome including any material relevant. With all the developments around aerodromes, we believe these presentations will play a vital part in operators protecting their airspace and ensuring infringements do not occur.

TAG is running a Protected Airspace Awareness and Responsibilities Course on the 22nd of May, at Ballina Airport. The presentation covers such topics as:

Need for Protected Airspace
Components of Protected airspace
 › OLS
 › PANS-OPS
 › Additional Navigational Aids
 › Visual approach aids
 › Airport Reporting Responsibilities
 › Control Tower Activity
The presenter will be Ray Romano — one of our airspace specialists. To obtain the registration details or any further information please contact enquiries@theairportgroup.com.au

Melbourne Airport – Peer Review of the GA Helicopter Zone
TAG performed a peer review of the GA Helicopter Zone at Melbourne Airport to identify any potential issues and associated risks with the design.
STAFF APPOINTMENTS

TAG welcomes Robert Callway, Project Director. Robert brings to TAG an extensive project and construction management experience in the property and construction industry, including airport urban master planning and a range of other on-airport projects. Robert will manage the co-ordination of the various parts of TAG and external consultants for larger projects to ensure timely and accurate delivery of client objectives. You can contact Robert at robc@theairportgroup.com.au or +61 416 013 634.

TAG welcomes Peter English, Senior Airfield Engineer. Peter has extensive expertise in major city airport development projects and aeronautical operations, on the airside, terminal and landside aspects. He is recognised throughout the aviation industry for his broad set of skills specific to Australian airports. Peter’s relevant history includes his employment as Project Manager with GHD Pty Ltd with extensive airports exposure, Senior Projects Manager and Design Manager with Sydney Airport (SAACL) responsible for airside/aeronautical/terminal upgrades and redevelopment works, and more recently, with Gold Coast Airport (GCA) as their senior development manager/engineer. You can contact Peter at petere@theairportgroup.com.au or +61 7 3295 0232.

We are pleased that Catherine Thompson (nee Kennedy) has agreed to a new role as Business Administrator/Production Manager in order to meet the rapidly growing needs of the TAG business. Catherine’s extensive business knowledge originates from owning, developing and managing various small businesses for over 25 years. Catherine co-ordinates the administrative and strategic requirements in all areas of The Airport Group, utilising her vast experience in managing and developing staff and client relationships. You can contact Catherine through the Brisbane or Canberra offices at cat@theairportgroup.com.au or +61 412 081 284.

TAG welcomes Julie Neylon, Office Manager. Julie is the manager of the Brisbane office and coordinates all offices and staff. As the ‘face’ of TAG, Julie brings great enthusiasm as well as extensive experience in office administration, bookkeeping, and marketing. You can contact Julie at julien@theairportgroup.com.au or +61 7 3295 0232.

UPCOMING EVENTS

AAREC 2013
Auckland, 6–8 June 2013

TAG is again the Co-Organiser and Major Sponsor for AAREC (Australasian Airport Real Estate Conference). This year Auckland Airport is the Host Partner. The program is both very informative and also promises a fun-filled visit to NZ! We have some exciting site visits – the Auckland on-airport development program has been truly innovative.

To obtain the program and registration details, please contact Taylor Gailey on +61 433 718 696 or taylorg@theairportgroup.com.au.

AAA Pavements & Lighting Forum
Brisbane Convention Centre
16 & 17 April 2013

TAG Protected Airspace Familiarisation Course (to follow on from AAA Chapter meeting)
Ballina, 22 May 2013

AAA (NSW) Chapter
Ballina, 21st May 2013

TAG is pleased to be a sponsor of the NSW Chapter Meeting to be held at Ballina. Please contact the AAA for all the details.

Reference Material & Press

› Infrastructure Australia – Australia’s Public Infrastructure (Part of the answer to solving Australia’s Infrastructure Deficit) (October 2012) ("Successful airports involve building commercial operations including retailing and property development, which may be better undertaken in the private sector. There appears no significant impediments to the further transfer of residual public sector airport assets to the private sector.")

› Australian FIFO Industry – an essential and growing service (Catapult Partners, September 2012)

ABOUT US

The Airport Group offers a comprehensive ‘whole of airport’ solution for regional and metropolitan airports in Australia, New Zealand and the Pacific Region.

We are the only firm that brings together 60 years of airport operational, planning and design experience coupled with Australasia’s leading airport commercial experience. Increasingly, airport stakeholders require a complete solution that is cognisant of the balancing priorities of airside and landside assets, and the benefits that the effective integration and commercialization of these assets can deliver.

› Airside civil design
› Airport master plans and approvals
› Air space and procedure design
› Land use planning and feasibilities
› Airport management
› Airport finance and governance
› Training
› Strategy and business planning
› Commercial transactions
› Development and construction management