EXECUTIVE INSIGHTS

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U.S. Airports: Increase Your Performance through a Radical Reconsideration of Your Non-Aeronautical Revenues

The managers of U.S. airports are well aware of the impact the weakened global economy has had on the aviation industry. Specifically:

- Passenger volumes have broadly declined over the past two years. The Air Transport Association (ATA) reported that 4% fewer passengers traveled on U.S. carriers in July 2009 versus July 2008. The drop in passenger traffic continues to fall despite double-digit declines in fares, demonstrating the continued weakness in demand for passenger air traffic. And to date in 2009 most U.S. airports have experienced a volume drop of 5% or more.

- The biggest impact on revenues has been a marked decrease in the most profitable business travel segment – and this segment is likely to be the most sluggish to improve given that many corporations are using the recession as a way to permanently change their travel policies through much greater use of video and teleconferencing.

- U.S. carriers are reducing capacity to try to regain profitability, and do not appear to be pursuing market share growth in the short term.

- Despite the fact that leading indicators suggest the economy may have finally bottomed out, research shows that consumers remain pessimistic and do not expect to alter their current lower spending behavior for the foreseeable future.[1]

The implications of these factors for U.S. airports include:

- Aeronautical revenues are declining and airports have little or no flexibility to increase rates.

- Non-aeronautical revenues such as retail and parking are being adversely affected – not only are passenger volumes dropping, but the total dollars spent by passengers are also dropping.

- In-airport advertising revenues are declining because there are fewer passengers.

With passenger volumes not expected to return to their pre-2008 levels anytime soon, it is imperative that U.S. airports find a new way to increase their financial performance. How? By radically re-assessing their non-aeronautical revenue activities and applying rigorous analytical tools to maximize revenues in these areas.

Very few U.S. airports fully leverage the revenue potential of the passengers who walk through their concourses every day, and they lag behind their European and Asian counterparts in the generation of non-aeronautical revenues as a percentage of total revenues.

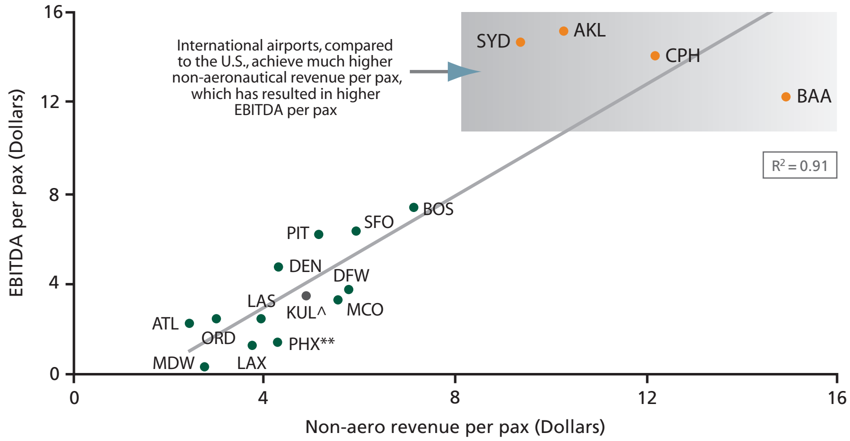
L.E.K. Consulting has found that there is a direct and positive relationship between non-aeronautical revenue per passenger and EBITDA per passenger. Airports that drive higher non-aeronautical revenues per passenger generate more profits than those that do not, as shown in Figure 1.

[1]*Source: L.E.K. Consumer Sentiment Survey, April 2009*

U.S. Airports: Increase Your Performance through a Radical Reconsideration of Your Non-Aeronautical Revenues was written by **Jamil Satchu** and **Bob Neapole,** Vice Presidents of L.E.K. Consulting. Please contact L.E.K. at aviation@lek.com for additional information.

Figure 1

EBITDA per Total Passenger vs. Non-aero Revenue per Total Passenger
(FY 2007*)



Note: * Financial year periods differ by airport for EBITDA calculation; EBITDA includes aero and non-aero revenues; ** PHX also includes data for the smaller DeerValley and Goodyear airports; ^Malaysia Airport Holding BHD includes all airports in the country

Source: Airport annual reports; ARN 2008 Fact Book; FAA CATS 127

This suggests that even in these difficult economic times many U.S. airports are missing important revenue opportunities. We believe that most airports in the U.S. do not deeply understand the needs of passengers who pass through their facilities. While some have done broad-based demographic studies, gathered dwell time data and measured satisfaction, almost all of them stop there. For example, do most U.S. airports know the following about their customers:

a. How can an airport's diverse passenger base be segmented into distinct consumer behavioral segments?

b. What are the airport spending behaviors of each of those segments?

c. What are the current levels of unrealized spend across passenger segments?

d. What are the primary reasons for unrealized spend?

e. What is the potential expenditure per head by segment and product category? Based on their own financial situation? General economic perspectives?

L.E.K. believes that this approach can be applied to two critical areas of non-aeronautical activities: retail and parking.

Retail

Retail is a significant non-aeronautical revenue opportunity for U.S. airports. In our experience, there is substantial opportunity to drive growth in retail revenue per passenger by identifying distinct customer segments within the passenger population.

L.E.K. has worked with numerous airports to drive substantive revenue growth through customer segmentation. An example of a representative passenger segmentation framework is shown in Figure 2.

To develop and define distinct customer segments that reflect an airport's true passenger base, it is important to gather customer data over a substantive period of time, and include different times of the day, days of the week, and seasons. This methodology will ensure that the segments are reflective of an airport's entire passenger base. Once it identifies distinct segments with distinct airport habits and purchase behaviors, an airport should develop appropriate retailing propositions to meet the needs of each segment – and ones that maximize revenues and profits for the airport.

In addition, based upon our experience, most airports often do not dedicate adequate space to retail, and correcting this can have an immediate impact on revenues. While some point to their legacy infrastructure as the reason for suboptimal retail density, our research finds that most airports can increase their sales per enplaned passenger by at least 30% simply by increasing retail density by 10%.

The wrong mix of retailers is another common problem we find in U.S. airports. Compared to international benchmarks, U.S. airports are over-weighted in food and beverage versus other retail categories. As a result, their international counterparts drive significantly higher sales per enplaned passenger.

To offer the optimal retail mix, an individual airport must apply its customer segmentation data. For example, an airport with a higher proportion of unfulfilled travelers or shopaholics could drive additional revenue with more specialty and higher-end retailers.

Figure 2

Illustrative: Airport Retail Customer Segments

	Airport Shopaholics	Unfulfilled Shoppers	Agitated Travelers	Low-Effort Shoppers	Value Seekers	Measured Shoppers	Unlikely Shoppers
Typical Passenger	Middle-aged male on leisure trip High-income earner	Young male (60% bias) or female on leisure trip Low- to mid-income earner	Young male or female on a business or leisure trip Middle-income earner	Young male on business or leisure trip	Male or female (60% bias) on business or leisure trip Middle-income earner	Middle-aged male on a leisure trip Middle-income earner	Young male (57%) or female on business or leisure trip
Description	Enjoy shopping in general and at airport Look forward to treating themselves at the airport	Look forward to shopping at the airport, but don't see the shops as relevant or inspiring	Find airport highly stressful and irritating Many enjoy shopping	Enjoy shopping if it is easy/ low effort Look forward to shopping at the airport	Avoid shops and cafes at airport due to the price	Make carefully considered and non-impulsive purchases Generally dislike shopping; do not look forward to airport shopping	Do not look forward to shopping or treating themselves at the airport A high proportion do not enjoy shopping
Spending Behavior	High spend across all categories, especially planned spend	High spend across all categories, especially perfume and cosmetics (planned) High food and beverage spend	High levels of unplanned spend, especially on duty free and perfume High food and beverage spend	Has a high level of planned spend across all categories Medium food and beverage spend	Medium spend overall; has similar levels of spend on planned and unplanned purchases Low spend on food and beverage	Low spend, but higher on planned than unplanned spend Low food and beverage spend	Lowest spend overall; medium spend on unplanned basics Low food and beverage spend

In addition to offering the right mix, airports need to ensure that they are capitalizing on their passengers' time in their facilities. Analyzing and controlling passenger flow can drive improved retail performance. For example, an airport may want to create a "free flow" environment that enables and encourages browsing and impulse purchases. In this scenario, storefronts should be designed with easy-to-access entrances. In certain locations, "speed bumps" can be created to guide passengers toward retail establishments.

While the space located before security tends to be a stressful area for passengers who are less likely to linger and shop, the area immediately after security often offers an opportunity for capturing revenues through appropriately configured retail offerings.

There are also certain passenger segments – such as the "agitated traveler"– that prefer to continue straight to their gates even if they have plenty of time before departure. If your segmentation analysis indicates that you have a good number of these travelers, then having a cluster of the appropriate retailers close to the gates would probably make sense. These retailers should include food and beverage providers, since airlines largely do not serve food to domestic coach-fare passengers.

In summary, an airport must first segment and analyze its unique travelers to then be able to strategically improve terminal layout and passenger flow patterns, and provide the right retail offerings to significantly improve its retail revenues.

Parking

Parking is the second substantive non-aeronautical revenue opportunity to which applying customer segmentation analysis can yield additional revenues. This area is often the largest non-aeronautical revenue driver at U.S. airports, often more than 50% of total non-aeronautical revenues.

The first step to maximizing airport parking revenues is for airport managers to ensure that they have adequate capacity. They also need to offer a competitive parking proposition, when compared to off-airport parking and other transportation (e.g., limos, airport van services).

Figure 3

Segment	Usage Definition	Distinctive Segment Needs
Short Business Trip	Sunday, 1–3 days duration Monday to Thursday, 0–3 days duration Friday, day-trippers	Information Convenience–minimize "airport" time Security Accurate receipts
Business Commuters	Sunday, returning Wednesday to Friday Monday or Tuesday, returning Thursday or Friday	Minimize weekly commute time Security Reasonable prices Friendly, efficient car transfer
Weekenders	Departing Thursday for a long weekend Friday and Saturday for an extended or overnight trip	Minimum time delays Clear directions Frequent shuttle service Security Price competitive
Traditional Holidays	Stays over a week	Simple and easy at all times No long hauls of luggage Security Price competitive Frequent shuttle service Easy access to public transportation

Recognizing that parking rates vary across airports because of local market dynamics, L.E.K. has demonstrated that airports across the country have the opportunity to increase revenue by providing increased tiering of parking options, and increasing the price levels for premium parking options. For example, L.E.K.'s experience shows that in several large metropolitan markets, the demand for daily parking and valet services is relatively inelastic and therefore may offer opportunities for revenue enhancement through strategic price increases. L.E.K.'s experience further indicates that customer segmentation can be a very effective tool in driving increased parking revenues at airports. As with retail revenue opportunities, rigorous analysis of usage patterns of airport parking customers analyzed by lot and terminal, across a day and across a week, can identify distinct segments. A parking segmentation framework may look like the following in Figure 3. This information can then be leveraged to develop distinct strategies for each segment.

Summary

The current economic situation and its impact on the financial performance of U.S. airports is not going to change anytime soon. Therefore, airports need to look at increasing their non-aeronautical revenues to offset declining passenger volumes and reduced overall spending in airports. This can only be achieved effectively through proper segmentation of airport travelers, analysis of buyer behavior and designing the best strategies.

Figure 4

Customer Segment	Examples of Strategy
Domestic short term	
Meeters	• Launch "short stay" product.
Farewellers	• New covered lot with extra space.
Short Business	• Increase prices over 3 hours. • Implement frequent premium parker program.
Weekenders	• Promote "fast track" product on Friday nights.
Domestic long term	
Off-Peak Leisure	• New facility should better meet needs, competed away by off-airport.
Business Commuters	• Enhance product (e.g., flight information display screens (FIDs) and moving walkways).
Weekender	• Introduce discount weekend product with online booking capability.
Traditional Holiday	• Develop remote parking product.

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