

# New Handbook Presents Expansive View Of Concession Programs

Although there have been many articles written and presentations made regarding various aspects of airport in-terminal concession programs, there is no single handbook available that covers the full scope of planning, developing and managing airport concession programs. To fill this need, the Airport Cooperative Research Program under the Transportation Research Board commissioned a project to prepare a resource manual for use by airport staff, policy makers, concessionaires, airlines and other stakeholders with an interest in airport concessions. Following a competitive selection process, **LeighFisher**, in association with **Exstare Federal Services Group LLC**, was selected to prepare the resource manual, which is scheduled for release in the first half of 2011. The project is overseen by ACRP staff and an expert panel including representatives of airports, Airports Council International-North America, the Federal Aviation Administration, concessionaires, airlines and others. When completed, the resource manual will be made available free of charge through TRB and ACRP.

Airport concession programs have grown in scope and complexity over the years. Long gone are the days when generic concessions were operated by one or two master concessionaires under long-term exclusive agreements. Today, airport concession programs feature many familiar local, national and international brands, and offer customers value and choice as never before. At the same time, airports and concessionaires must manage burdensome security requirements, react to changes in a volatile airline industry and operate in a period of economic uncertainty. These challenges also increased the importance of terminal concessions, which are a key driver of passenger satisfaction and contributor to the airport's bottom-line financial results. As ACI-World's Airport Service Quality survey has clearly shown, great airports have great concession programs.

## *Research Approach*

The project included a review of available literature, a Web-based survey and follow-up oral interviews.

First, more than 800 documents were reviewed to determine the overall depth and breadth of available information, and to identify material that would be of value in preparing the resource manual.

Second, a two-tiered interview approach was used to gather information from industry leaders and practitioners, including concession managers, concessionaires, consultants and airlines.

A comprehensive Web-based survey was developed and distributed to airport terminal concession managers at large, medium, small and non-hub airports. The survey included questions related to the characteristics of their current concession program, including the types of concessions currently offered, business terms, management structure and contracting practices. Similar, though less extensive, Web-based surveys were forwarded to airline terminal concession managers, concessionaires, developers and consultants. More than 50 Web surveys were received and approximately 40 follow-up oral interviews were conducted. In addition, non-airport concession managers and overseas airport managers were interviewed. The survey and interview data together provided a comprehensive view of current issues, practices and standards. Sixty-five industry professionals participated in one or both surveys and made a significant contribution to the future success of the project.

An outline of the Resource Manual is shown below. Eight case

## Outline Of The Resource Manual For In-Terminal Concessions

<b>Part I</b>	<b>Introduction</b>
Chapter 1	Purpose of the Resource Manual
Chapter 2	Attributes of Successful Concession Programs
<b>Part II</b>	<b>Concession Planning</b>
Chapter 3	Establishing Goals
Chapter 4	The Passenger and Customer Profile
Chapter 5	Developing the Concession Space Plan
Chapter 6	The Concession Mix
Chapter 7	ACDBE Programs
<b>Part III</b>	<b>Contracting and Business Practices</b>
Chapter 8	Concession Contracting Approaches
Chapter 9	Business Terms and Concession Agreements
Chapter 10	Procurement
<b>Part IV</b>	<b>Management and Operations</b>
Chapter 11	Services, Storage and Logistics
Chapter 12	Capital Investment
Chapter 13	Managing the Program

studies highlighting successful concession programs at select U.S., European and Asian airports will also be included.

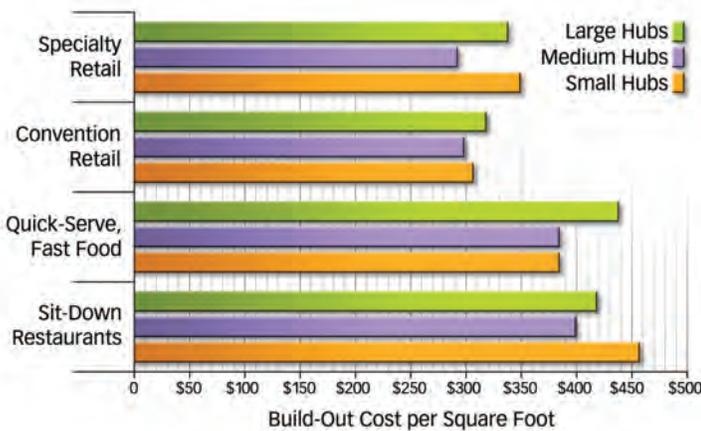
Sales, revenue, space and other data was taken using the Airport Revenue News' annual Fact Books. Data for the period 1998-2008 was extracted and used for analysis and comparisons.

Examples of a few of the topics covered by the research and included in the Resource Manual are presented below.

### Concession Build-Out Costs

Concessionaires surveyed for the study expressed concern over the increasing costs of building concession facilities. After high minimum rents, development costs were cited as the next most important airport concession-related business practice in need of improvement. Concessionaires cited generally increasing

#### Average Build-Out Costs By Hub Size



costs, arbitrary design review processes and unreasonably high standards among factors contributing to the rise in concession development costs. Shorter lease terms aggravate the problem, according to the survey.

The cost of building concession facilities as reported by concession managers is summarized in the figure above. Cost per sq. ft. ranged from more than \$300 for retail facilities to nearly \$450 for quick-serve food and beverage units and sit-down casual dining restaurants at large hubs. The costs presented above are averages; the numbers were higher in large hubs serving high-cost areas, and otherwise varied according to local factors.

For airports of all sizes, the cost of building out a full-service restaurant averaged \$415 per sq. ft., with quick-serve units coming slightly lower at \$402. Convenience retail and specialty retail units averaged just over \$300 per sq. ft. About 10% of airports reported build-out costs for food and beverage units of \$500 per sq. ft. or more, with a few airports reporting costs above \$600 per sq. ft.

The actual cost of building out concession space is almost always in excess of minimum investment requirements contained in requests for proposals.

### Mid-Term Investment

There was no standard approach used for establishing mid-term investment requirements, which are included in about 80% of concession agreements, according to the survey. The

approaches cited included setting a fixed amount per sq. ft.; applying a percentage (say, 15% to 25%) to the initial investment requirement or proposed investment; negotiating the amount prior to the start of the agreement; establishing the amount as a "bid" item in the proposals; and requiring submittal and negotiation of a scope of work near the mid-point of the term to return the concession to a first-class standard.

### Typical Term Lengths And Option Periods

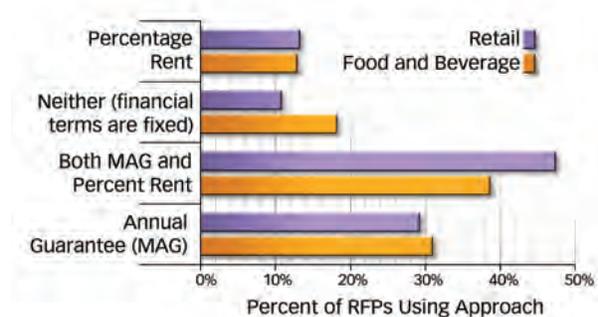
Options to extend the term are included in almost half of food and beverage and retail concession agreements, according to the survey. For example, 44% of airports include option periods in their food and beverage agreements, with two years being the most frequently cited option period. The average option period was about 2.8 years. A similar percentage included options in retail agreements, with two years as the most frequently cited option period. A number of airports reported they were looking to develop performance-based methodologies for determining which concessionaires should be offered term extensions.

Concessionaires noted that options to extend terms were nice to have, but only the base term can be used in securing financing or valuing the concession agreement. Concern over term length was linked directly to concerns over the cost of developing concession units. According to some concessionaires, although the trend has been to shorter terms, development requirements have increased and are out of proportion to the anticipated life of the improvements.

### Financial Evaluation Of Proposals

A significant number of airports are opting for open-ended financial proposals, with proposers asked to propose both minimum guarantees and percentage rent. Some 47% of airports used this approach in their most recent retail RFP. A smaller percentage, about 38%, used open-ended financial elements in

#### Financial Components Of RFPs



food and beverage proposals.

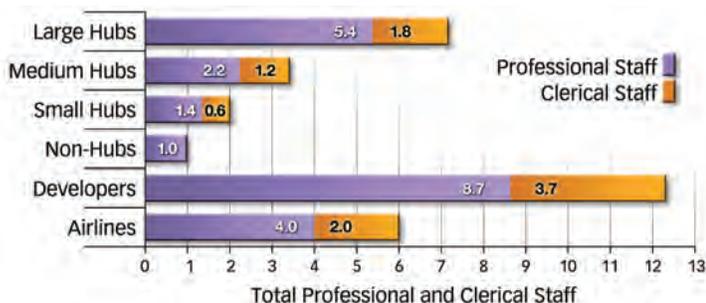
The next most often used approach was setting the percentage and leaving the minimum annual guarantee open to propose, followed by fixing both the percentage rent and the MAG. The fewest number of airports used the percentage rent as the sole financial variable. Evaluating percentage rents can be tricky; a high-volume brand paying a lower percentage rent may produce substantially more revenue for the airport than a generic concession paying a high percentage rent.

The open-ended approach places the greatest burden on the airport to evaluate the multiple variables.

### Size Of Concession Staffs

Survey participants were asked about the number of full-time equivalent staff dedicated to managing the concession program. Not surprisingly, the number of dedicated staff increased with the size of the airport, with large-hub concessions staffs averaging just over 7, medium hubs 3.4 and small hubs 2 FTEs. One large hub reported a concession staff of one professional and one clerical staff. The number of staff varied widely.

### Average Size Of Concession Staff



Developers employed the largest staffs to manage concession programs with about 12 FTEs. Developer staff was in addition to airport concession staff. The comparison of developer staff numbers may not be directly comparable, however, as developers also may perform duties not typically performed by airport concession management staff, such as accounting, marketing and construction oversight.

Two airlines also responded to the survey and averaged 6 FTEs. The airlines managed unit terminals at large hubs.

Reporting relationships for the concession manager also varied by hub size. At large hubs, the concession manager typically reported to a commercial director or a deputy director. At medium hubs, the concession manager typically reports to deputy director or finance director. At small hubs, the reporting relationship was likely to be to the airport director.

### Differences Between U.S. And Overseas Airport Concession Programs

Several overseas concession managers were also interviewed for the project. Overall, business practices used at overseas airports were similar to those at U.S. airports, with concessions awarded usually based on a competitive proposal process and business terms similar to those used in the U.S. Overseas airports were more likely to negotiate term extensions with high performers, however.

Many European airports are partially or fully privatized, or corporatized, that is, publicly owned but legally organized as corporations. This ownership model has advantages in terms of hiring, procurement and other business practices, including financial reporting.

Overseas airports typically have more concession space and place greater emphasis on retail. Ratios of food and beverage to retail space are reversed. U.S. airports devote about two-thirds

of concession space to food and beverage services, which has the highest spend rate and produces the most revenue. At overseas airports, the ratio is reversed; retail occupies the majority of space and produces by far the highest spend rate and largest share of concession revenues. There are broad differences between airports, so generalizations must be made with caution.

Tax-free and duty free shops are a major differentiator when comparing U.S. airports, which serve a huge domestic market, with their overseas counterparts, which often have a much higher percentage of international passengers. International passengers are eligible to make purchases at tax- and duty-free shops, which can represent large savings to passengers from high-tax environments where value-added taxes, excise taxes and import duties can add 20% to 100% or more to the price of some items. For U.S. passengers who are used to lower taxes and discount stores, duty free savings aren't as great and sales to U.S. residents lag those of most other developed countries.

Comparisons of U.S. airports with their overseas counterparts should be made with caution. Three airports – Dubai, London Heathrow and Seoul Incheon – are estimated to produce annual duty free sales of \$1B. In the U.S., the top-producing airport in terms of total concession sales (food and beverage, retail and duty free) is **John F. Kennedy International (JFK)**, with \$442M in 2008 concession sales, about two-thirds of which came from duty free. Clearly, the structural advantages of large volumes of international passengers combined with the strong value proposition of tax-free and duty free sales are a distinct advantage that supports not only higher revenues, but allow for larger, glitzier and higher-end concession programs.

Historically, overseas airports provided their passengers with low prices, quality branded merchandise and a large array of specialist shops that collectively offered the customer a strong value proposition. On the other hand, U.S. airports evolved at a time when long-term contracts with guaranteed revenues were considered important to supporting revenue bonds that financed airport expansion. Although these agreements provided long-term guaranteed revenues, they also produced high prices, poor service, and lackluster shops and restaurants with an unfavorable reputation that has taken years to overcome. Today, U.S. concession programs offer more brands, more space, more choice, lower prices and, most importantly, better value.

### Summary

It is hoped that the resource manual developed with the direction and funding of the Airport Cooperative Research Program will provide a valuable reference tool to airport concession managers and other stakeholders. It can be used as a comprehensive guide to developing and managing airport concessions and will provide insights for the rationales and techniques in use at airports of today. As terminal concessions continue to take on more and more significance to airports and their users, and as the breadth of concession opportunities at airports continues to change and grow, it is expected that the resource manual can be updated to reflect changing practices.

*We'd like to hear your opinion about this article. Please direct all correspondence to Pauline Armbrust at [pauline@airportrevenue.com](mailto:pauline@airportrevenue.com).*