Region: Latin America and the Caribbean

State: Jamaica

Airport: Sangster International Airport (ICAO: MKJS, IATA: MBJ)

Note: this case study has been developed by the Caribbean Development Bank and is extracted from the *Public Private Partnerships in the Caribbean: Building on Early Lessons* report of the Bank.

Introduction

The Value Proposition of Private Sector Participation in Jamaica's Airports

On 12 April, 2003, the Government of Jamaica (GoJ) handed over control of the Sangster International Airport (SIA), Jamaica's largest airport and gateway to its vital tourist industry, to the Vancouver Airport Services Consortium, under a 30-year concession agreement. In its first decade of existence, this Public-Private Partnership (PPP) has been an unqualified success and has led to major expansions and improvements in quality of service at SIA. Consequently, this project has important lessons in the structuring and implementation of PPPs in the Caribbean Region.

In the early 1990s, GoJ recognized the need to privatize the Sangster International Airport, which served as the gateway for all of Jamaica's tourists in the North coast resorts. Under public ownership, the airport was becoming more crowded and its assets were ageing - new investments were needed to renovate and expand the airport to meet the passenger load. Furthermore, the airport's operations were becoming a significant drain on the Government's fiscal resources while Jamaica's national debt levels was high and rising, leaving the Government with little ability to pay for the required capital investment.

Privatization was deemed the best option for the Government to meet the Airport's needs and thus avoid endangering its critical tourism industry. In a comprehensive transport sector study, the Government set out the following key policy objectives for the development of the aviation subsector:

- Reducing public sector involvement in the operations of airports and airlines;
- Developing aviation infrastructure through the use of private debt and equity capital;
- Strengthening the role of the public sector in regulation and policy planning in airport related activities so as to create an adequate economic environment to encourage private sector investments in the sector; and,
- Providing quality services with an appropriate standard of safety and security.

In pursuit of the above objectives, the Government, through a special Airport Task Force and a Project Unit at Airports Authority of Jamaica (AAJ), developed a proposed structure for the privatization and expansion of SIA. Through privatization, the Government hoped to reduce or eliminate its fiscal obligations regarding the airport's operations while the private partner brought new investment capital for renovations, expansions and improved airport services.

The Privatization Process

The First, Non-Competitive Approach Fails

Under the direction of the AAJ, the Airport Task Force sought to pursue the selection of a strategic partner on a negotiated basis, rather than through a competitive process. In the mid-1990s, initial discussions were held with American Airlines about the possibility of establishing a hub at SIA. The Airport Task Force proposed a privatization structure that would ensure that the Government continued to exercise a significant degree of control over the operation of the Airport and proposed arrangements that would:

- Privatize only the landside terminal operations and not the airside operations;
- Ensure that no single entity could have more than a 25 per cent holding in the airport terminal operating company; and
- Ensure that Government would have a Golden Share in the terminal operating company.

AAJ engaged Citibank as a Financial Advisor and hired Birk Hillman Zipperly as airport design consultants, spending considerable sums on the production of a feasibility study and airport expansion proposals (including architectural plans). After several approaches to financial institutions and the market, however, the privatization of SIA was still stalled.

In 1996, an exclusive Memorandum of Understanding with United Infrastructure Company/ Airport Group International (UCI/AGI) was signed, to evaluate the feasibility of the Project. After undertaking an initial investigation, UIC/AGI issued a preliminary report in January of 1997, and at the same time, requested an extension of their period of exclusivity in order to carry out further due diligence and submit what the Government believed would be a more thorough proposal.[1] However, the UIC/AGI proposal which resulted from this arrangement was eventually rejected by the Government as

[1] At the time, UCI/AGI reportedly had a large number of projects under consideration and were reportedly bidding on concessions for the privatisation of 35 state-owned airports in Argentina, 4 airports in Columbia, and were also involved in the New Berlin International Airport and a new terminal for the Beijing International Airport in China (Report in the Miami Herald International Edition Pg. 3B 2 July, 1997). It appeared, to the Government, that owing to the relatively small size of Jamaica's requirements, UIC/ AGI saw its own interest being better served in pursuing larger opportunities.

unacceptable. After the UIC/AGI failure, it became clear that the Government needed to take a new approach to the airport privatization.

Success from the National Investment Bank of Jamaica Bidding Process

Following the aborted efforts described above, Cabinet in May 1998 approved the establishment of an Enterprise Team under the direction of National Investment Bank of Jamaica (NIBJ). The Enterprise Team included representatives of all the agencies that had an interest in the efficient operations of the airport, namely, the Office of the Prime Minister, the Ministry of Finance and Planning, the Civil Aviation Authority, the AAJ/SIA, the Attorney General's Office and the Ministry of Transport & Works. With NIBJ at the helm, the Government was now able to follow a more orderly, transparent and competitive process.

The revised objectives of privatizing the SIA were limited to:

- Relieving GOJ of the financial burden of finding the necessary capital for the development and expansion of the airport.
- Facilitating the exploitation of the full commercial potential of the airport, thereby broadening its revenue base and reducing its dependence on passenger charges and landing fees.

NIBJ became the *de facto* day-to-day coordinator of the SIA privatization process, and it proceeded to prepare an Information Memorandum (IM) in respect of the privatization. At the time, SIA which had been designed for a peak passenger throughput of 1,000 per hour, was experiencing peak traffic of up to 1,800 passengers per hour. The airport was rated by the International Air Transport Association (IATA) at a level of service D (A being the highest), and was in danger of falling below minimum acceptable standards, with serious negative implications for Jamaica's tourism industry. The privatization effort was perceived as an urgent necessity to avoid further erosion of the Airport's rating.

The NIBJ Enterprise Team made two strategic changes in the approach to the privatization transaction:

- reversing the AAJ approach and including the entire airport operations and its revenues, both airside and landside, in the concession arrangements;
- elimination of the Government's Golden Share; and
- allowing the Concessionaire to establish an airport operating company wholly under its control with no limitations on its shares, other than restrictions prohibiting control by an airline shareholder, and a requirement that an established airport operator control no less than 10 per cent of the shares.

The above changes made the privatization offer much more attractive to commercial airport operators. In addition to transferring management and control of the airport to private shareholders, the Concession also called for about USD180 million in project financing to finance new capital investments at the Airport.

Tile Bidding Process

The SIA privatization involved a three-stage bidding process which incorporated pre-qualification, submission of a first round of proposals and the submission of a final round of proposals. The key milestones in this process were:

- In July 1998, GOJ's announced its intention to divest SIA in the local and international press, and interested parties were invited to submit applications for pre-qualification. The pre-qualification was carried prior to the hiring of any professional advisors but subsequent to this, financial advisors were engaged to assist with the preparation of the RFP and IM.[2]
- The final round of bidding was launched in November 2000 with the issuance of a Supplementary Information Memorandum (SIM). The SIM provided information on the new regulatory arrangements and principles and outlined proposals for removing the obstacles to the privatization presented by Air Jamaica's continuing debt to the AAJ. These problems are discussed below in greater detail.
- In April 2001, four pre-qualified companies submitted proposals. A preferred bidder, Vancouver Airport Services Consortium, was selected and announced in August 2001, with approval from the National Contracts Commission and Cabinet. It then took 18 months to finalize negotiations and achieve financial close with the Vancouver Airport Services Consortium.
- Handover of the airport took place on 12 April 2003.

Major Roles in tile Bidding Process

Role of the National Investment Bank of Jamaica

NIBJ was the Secretariat to the Enterprise Team. In practice, this meant that NIBJ handled all administrative and logistical activities related to the divestment process, including:

- contracting supervision, and paying the advisors and consultants;

[2] Approximately 35 companies requested the pre-qualification document and 12 of these actually submitted applications for pre-qualification. Although the original intent was to pre-qualify only 4 - 6 companies, a decision was taken by the Enterprise Team to consider all 12 companies as pre-qualified and no company was eliminated at this stage. The general criteria used for evaluating applications for pre-qualification included: (i) experience in the development; management and operation of airports; (ii) the ability to raise financing for the development of the airport; (iii) technical capability and qualifications of key personnel; and (iv) experience in operating in an efficiency driven regulatory environment

- actively participating in all negotiations;
- arranging and hosting all meetings;
- documenting the project activities and preparing minutes, reports and Cabinet Submissions;
- supervising and assisting with operational matters such as preparation of the data room; and
- serving as the focal point of all communication in respect of the project.

Role of the Airports Authority of Jamaica

AAJ was in effect the Technical Advisor to the Enterprise Team. The AAJ Management Team gave full support to the privatization activities and alerted NIBJ and the Enterprise Team of potential problems that could arise during the privatization. This included explaining to staff that AAJ would henceforth oversee the concession contract and the operations and management of the airport company, rather than serve as operator of the airport facilities. As a result, NIBJ decided not to engage external technical consultants and relied on AAJ's inputs where technical matters were concerned.

Role of Financial Advisors

The Enterprise Team engaged international investment bankers with a strong record in airport privatization to advise on the privatization process. UBS Investment Bank (UBS), formerly Warburg Dillon Read Infrastructure Management Group, was engaged by NIBJ in April 1999 to advise on the privatization. It was assisted by a Caribbean-based affiliate CFAS Limited, which did much of the local leg-work in the initial stages of the divestment process.

UBS provided financial advice in relation to the privatization, including the preparation of a Sale Memorandum and its circulation to a restricted list of potential purchasers approved by NIBJ. UBS also provided assistance in the coordination of due diligence, and assistance in negotiating the terms and structuring of the transaction.

Role of Other Consultants

The London-based law firm of Clifford Chance was selected as legal advisors to the privatization, but its involvement was later transferred to another firm, DLA Piper. Aviation marketing consultants, regulatory consultants and land surveyors were also contracted at various points in the privatization process for specific short term assignments.

In addition to the above international financial and legal advisors, NIBJ also engaged a local coordinating consultant, Stephen Wedderburn, who had considerable experience in assisting NIBJ with other privatization matters. Mr. Wedderburn was engaged by NIBJ in May 1999 and his scope of work included accounting support such as financial analysis, providing assistance with expediting the finalization of AAJ's financial statements, assisting with the preparation of the IM and negotiation support to the Negotiating Team.

In the view of NIBJ, all the major advisors performed well and contributed to the success of the privatization.

Role of Donors

In the implementation of the SIA privatization transaction, donors and Multilateral Development Banks (MDBs) did not play a significant direct role. In this case, the absence of direct involvement from MDBs was not a critical omission because the Government, through NIBJ, decided early on to invest the significant amount of funds required to avail themselves of first rate technical and financial advice.

Performance in the First Decade

Improved Services and Lower Costs to the Government

The consortium that formed MBJ Airports Limited at the time of privatization included: Vancouver Airport Services (Canada), Agunsa (Chile), Ashtrom (Israel) and Dragados (Spain). Shares in MBJ Airports Limited were subsequently transferred to two key principals:

- **Abertis Infraestructuras SA** (formerly, Dragados) - Abertis, a 74.5 per cent shareholder, is an international group that manages infrastructure assets in five areas: airports, telecommunications, toll roads, car parks and logistic parks. The company is a European leader in infrastructure management and one of the world's major benchmark companies in the field.
- **Vantage Airport Group** (formerly, Vancouver Airport Services) - Vantage, a 25.5 per cent shareholder, manages and develops a global network of airports. Vantage Airport Group is ranked among the world's premier airport operators and provides a full range of management and investment services to their clients.

Immediately after privatization, the Consortium set about expanding and upgrading SIA, with financing from a consortium of international lenders led by the International Finance Corporation (IFC). To date, IFC has made four investments in the Airport since 2003 for a total of USD105 million, including USD53.5 million mobilized from other investors. SIA's construction phases were as follows:

Phase 1A (completed March 2004):

- Installation of six Boarding Bridges.
- Expansion of Ground Transportation Hall.
- Expansion of Customs Hall and Baggage Claim Area.
- Installation of closed-circuit television, controlled security access.
- Installation of intercom system.
- Installation of internal elevator within existing building.

Phase 1B (completed December 2005):

- Construction of hold room concourse to east of Terminal.
- Construction of new aircraft parking position and supporting taxiway.
- Extension of fuel hydrant.
- Extension of public address system and computer security system.

Phase 2 (completed February 2009):

- Construction of the Arrivals Hall extension to the South Concourse.
- Renovation of the existing Customs Hall into a new Immigration Hall.
- Construction of the Landside Pavilion structure.
- Renovation of the West Concourse in the existing terminal.
- Renovation and expansion of the check-in hall.

Overall results of construction upgrades:

- Terminal building more than doubled in size to over 47,000 square feet.
- 12 additional loading bridges and gates-bringing the total to 18.
- A 46 per cent increase in apron area.

Customer Service improvements:

- Expanded Arrival and Customs Halls.
- Larger Baggage Claim area.
- Over 750 parking spaces.
- New ground transportation facilities.
- More retail space and a greater selection of shops (14 Food and Beverage, 9 Duty Free and 24 Specialty retail outlets).
- More check-in counters (100).

To date, MBJ Airports Limited has invested nearly USD200 million into the expansion of the facility and improvements, including a recent USD20 million runway rehabilitation and overlay. These projects were financed through shareholder debt and IFC loan agreements, repaid from the Airport Improvement Fee of USD5 per outbound passenger.

According to the Airports Council International (ACI), Sangster Airport has improved its ranking to #3 in Latin America and the Caribbean. The Airport has won the Caribbean Leading Airport by the World Travel Awards five years running.[3]

[3] Information provided by MBJ Airports Limited

Financially Sustainable Airport Operations

Information on the financial performance of MBJ Airports Limited is not publicly available. However, the Company reports that "MBJ meets all concession agreement requirements with the Government including a significant annual concession fee payable to Jamaica annually". Having IFC as a strategic investor demonstrates the continued bankability of SIA, and indicates continued confidence in the provision of private infrastructure services in Jamaica.

Passenger numbers at MBJ have continue to grow, even throughout the economic adversity of the last five years, with 2013 showing a 3.15 per cent growth over 2012, with a total of 3.49 million passengers. The commercial programme has grown in gross revenues by 199 per cent to almost USD32 million/year.[4]

Key Issues in the Privatization of the Sangster International Airport

The lack of success of the early efforts to privatize SIA appeared to have been due to several factors, the chief of which were:

- The lack of a marketable business plan and transaction structure that would attract significant investor interest.
- The absence of a structured competitive bidding process to select the project sponsors.
- Lack of a coherent institutional coordinating mechanism defining the roles of the Government agencies involved in the privatization; and lack of clarity as to the terms of reference of each agency in achieving the privatization goals.
- Imprecision on critical revenue issues such as revenues from airside and landside operations; and Government's retained rights under its insistence on a Golden Share.

However, even under the new approach adopted by Government and NIBJ, the SIA privatization, which was originally scheduled for completion within one year, took five years to complete - from May 1998 to April 2003. The main causes for these delays were:

- **Inadequate Regulatory Framework.** Although it was possible to regulate the Concession by contract, there was no pre-existing regulatory framework for privatized airports in Jamaica.[5] The Government decided, following the advice of its advisors, to develop such a framework during the transaction, to give lenders and developers greater certainty. However, enacting the new

[4] Information provided by MBJ Airports Limited

[5] The Airports (Economic Regulation) Act (2002) was passed in 2002. The draft Economic Regulation of Jamaica's Privatised Airports which would cover areas such as airport charges had earlier been approved by the SIA Enterprise Team because the establishment of the regulations was critical to the successful SIA privatization.

law took approximately three years. Also contributing to this delay was uncertainty about whether to privatize together in one package SIA and Norman Manley Airport in Kingston. It was ultimately decided to carry out separate privatizations because of difference in the markets served by both airports.

- **Problems with Payments from Air Jamaica.** SIA's largest customer, Air Jamaica, had a poor record of meeting its obligations in respect of aeronautical charges for use of the airports in Jamaica. This was a major cause for concern by the investors who confronted both the issue of accumulated arrears and the prospect that future payments would also be delayed. After several aborted attempts by the Government to allay these fears, the matter was ultimately resolved through an IATA payment scheme and a hypothecation arrangement with American Express receipts from Air Jamaica.

Lessons Learned

The SIA privatization ultimately achieved its objectives. The transaction reduced the Government's financial commitments to the Airport, increased the flow of traffic, reduced delays, expanded facilities and commercial revenues, and significantly improved customer satisfaction.

To the extent that we can discern lessons from the SIA privatization process, the following appear the most important:

- Transactions should be handled by specialized institutions such as NIBJ, which are staffed and organized with the assistance of outside advisors to handle complex competitive bidding processes and subsequent negotiations with sophisticated investors.
- Transaction processes should be standardized as much as possible, to avoid improvised solutions which may reduce the confidence of investors and lenders.
- Critical to the success of the privatization is a solid business plan, based on market realities. This requires reliance on expert outside consultants and advisors who fully understand market perceptions.
- The structure of the transaction should be matched to the business realities and allow the private operators freedom to make commercial decisions.
- The privatization can be greatly aided through a tightly controlled coordination of all interested agencies. The Enterprise Team used here was particularly effective.
- An appropriate regulatory environment will greatly facilitate the privatization and should be put in place prior to the transaction. Delays in this case caused by the need to create the legal framework for a private airport operator could have been avoided with more forward planning.
- Inclusion of an experienced and competent airport operator as a requirement for the bid was appropriate to ensure technical performance of the Concessionaire.
- Experienced outside advisors were needed to complete the transaction; such advisors are

expensive. Governments will need to cover these costs and should include them in its financing plan for the transaction. International sources of funding and technical support should always be sought.

- The provision of appropriate post-privatization financing for expansion is a key requisite for sustained success.

Good Practices and Lessons for the Future

Strengths - What to Repeat

- Competitive bids are better than one-on-one negotiations. The first transaction foundered when negotiations with the sole bidder broke down and the GoJ had no other bidders to turn to. Experience suggests that governments obtain better Value for Money (VfM) through competitive tenders, rather than sole-source negotiations.
- Specialized PPP staff members are critical to a successful transaction process. The staff at the Development Bank of Jamaica (DBJ) had previous experience in divestment transactions, which greatly assisted the PPP process.
- Tight agency coordination, driven by strong political will, is critical. With strong political leadership, DBJ played the role of a conductor of the orchestra, eliciting timely responses where needed and keeping all the agencies informed.
- Hiring qualified experts helps to ensure a strong business plan and a well-structured Request for Proposals (RFP) and bidding process. DBJ hired experienced international legal and technical consultants, with local partners to ensure retention of knowledge.
- Inclusion of an airport operator in bid requirements and pre-qualification process is necessary for the long-term success of the project.

Lessons Learned - What to Change

- Regulatory framework needs to be established prior to the transaction. The transaction was delayed for two years while The Airport (Economic Regulation) Act, 2002 was passed; this should have been completed prior to the transaction.
- Roles and responsibilities of government agencies must be clear and reliable. In the second transaction, AAJ was in effect the technical advisor to DBJ.
- Be proactive in seeking solutions to obvious problems before they become deal- breakers. The Air Jamaica payment problem was not resolved until late in the transaction.

The Last Word:

The beauty of the privatization of Sangster International Airport is that the airport operator can be proactive rather than reactive in terms of decision making, service levels and the management of partnerships that make up the entire team at Sangster International Airport. Operating as an entrepreneur, focused on business decisions allows for the flow of new ideas and quick implementation. MBJ Airports Limited is invested and committed to a 30-year concession, with 20 years remaining. This long term commitment allows for proper planning and development of Sangster International Airport over a long period for the benefit of Jamaica and MBJ.

Elizabeth Brown Scotton
Chief Commercial Officer
MBJ Airports Limited

— END —