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AIRPORTS AUTHORITY

Putting Our Communities First

Submission by Winnipeg Airports Authority Inc.
to the Canada Transportation Act Review Panel

May 6, 2015

INTRODUCTION

Winnipeg Airports Authority Inc. (WAA) is pleased to make this submission to the Canada Transportation Act Review Panel (the Panel).

The intent of this submission is to offer the perspective of a major regional air-transportation gateway and to amplify certain aspects of the Canadian Airports Council submission of January 2015 (the CAC Submission).[1]

The essence of WAA's submission is Canada's National Transportation Policy must recognize Canada's communities as the foundation upon which our national economy is built. They must be given the ability to succeed, or fail, on their own terms in a marketplace free of artificial barriers to competition.

Spread over a vast geographic space our communities exist within a remarkable diversity of economic and social contexts. Over the past twenty years there has been a revolution in global connectivity; people are connected to other people in more ways and more places more often than has ever been the case in human history. Canada's success over the next 30 years will stand or fall on the ability of people and businesses to use Canada's transportation system to connect to the domestic and global economies. Connectivity will be the key to thriving communities. Without it we will hollow out the core of our nation and concentrate people and activities in a few large centres.

To achieve the connectivity our communities will require, Canada's transportation policy and the initiatives taken under it must be consumer-centric; they must focus on maximizing the system's utility to the *consumers* of transportation services, be they businesses or individuals. It follows that Canadian air transportation policy ought to view everything first and foremost through the lens of those who *consume* transportation services rather than those who *supply* it. Airports and air carriers are suppliers of transportation services; they are simply links in a supply chain connecting people and goods in one place with people and goods in another.

Canada needs well-articulated policy guidance to harness the activities of all industry participants to achieve a clear goal. Yet, over the past ten to fifteen years, Federal aviation policy activities have become increasingly *ad hoc*. They have focused mainly on the *suppliers* of air transportation services without a clear understanding of how those policies impact the *consumers* of those services.

To succeed over the next three decades, Canada must focus its strategy squarely on the consumers of transportation services and pursue only those policy initiatives that provide a net benefit to them. Consistent with that focus, Canada must also ensure its policy efforts are coordinated across portfolios and, as much as possible, across jurisdictions. For example, the benefits of liberalizing trade or promoting tourism could easily be squandered if Canada's transportation policy makes it too expensive or too inefficient to get there from here. Imagine an otherwise wildly successful campaign to promote tourism to the North being brought to nought because you cannot get there. In the absence of any clear goal and coordinated effort, air-transportation initiatives will continue to drift along buffeted by the demands of the day; be they

[1] http://www.cacairports.ca/sites/default/files/CAC_CTA_Review_Submission.pdf

government budgetary restraint, competing departmental priorities, or that day's "loudest voice". Our communities deserve better than that.

To put WAA's submission in context, some background on WAA and our airport, Winnipeg James Armstrong Richardson International Airport (YWG), is in order.

YWG – AN ECONOMIC ENGINE

Background

WAA assumed control of YWG in 1997 as part of the second round of commercializing Canada's airports.

The seventh largest airport in Canada, YWG is Canada's longest serving international airport and is Canada's only Class 1 airport between Toronto and Calgary. It is competitively positioned as a 24-hour unrestricted airport.

YWG offers a broad range of air passenger and cargo services, including international carriers, commuter airlines, air cargo carriers, fixed base operators, and various charter operations. It currently serves over 3.6 million passengers and handles about 138,000 aircraft movements per year and approximately 175,000 tonnes of cargo annually.

In October 2012, YWG received the results of an independent economic impact study commissioned to examine its effect on the economy. Since commercialization in 1997 YWG's total economic output has grown to $3.64 billion annually and total wages have more than tripled to over $800 million. YWG's contribution to GDP has increased more than five-fold to some $1.6 billion, making it one of the province's single biggest contributors to GDP. It generates some 20,000 jobs in and around the airport. Since 1997, YWG has generated over 11,000 *new* jobs, including more than 5,000 that are directly airport-related.

Over the next 20 years YWG anticipates its cargo and passenger volumes will nearly double. Unquestionably, additional jobs and economic impacts will accompany that growth.

As impressive as they are, these statistics do *not* include the impact the airport has on the businesses and lives of all of those companies and individuals who rely on YWG to connect with Canada and the world. Impacts like that, while less easily measured are no less real. In order to sense the critical role YWG plays to every Manitoban one need only ask, "How would Manitoba businesses fare without the ability to connect with their customers face-to-face?"

Local Control

As the Panel may have sensed from this and other submissions, each of Canada's airports operates in its own unique local context. Indeed the devolution of the airports to local control was, in part, a recognition of that fact. The role of an Airport Authority is, among other things, to understand its community's needs, to determine how best to link its airport with the national and global economies so as to maximize the growth opportunities in the local economy, and to facilitate that linkage.

Local control, including the current arms-length governance structure, has enabled WAA and YWG to introduce the mix of services and offerings that best suit the transportation consumers in our market. It has been critical to the success YWG has found over the past twenty years and will be equally critical to its future success.

Diversification

One way in which WAA has responded to YWG's local conditions is to consciously focus on diversifying revenues.

YWG's goal is to be cost-competitive for carriers to operate here and to do it in a way that encourages economic growth. The regional market is not big enough to enable YWG to meet that goal through direct airport revenues alone. (By way of a simple example, it costs as much to clean a runway in Winnipeg as it does in Calgary, but WAA has far fewer flights over which to spread that cost.) We recognize we cannot remain cost competitive if we rely on Airport Improvement Fees and carrier charges as the primary means of funding the expenditures required to enable YWG to meet our community's demands.

WAA's diversification efforts to date have included developing the full commercial potential of the airport campus, exporting airport knowledge to other jurisdictions and helping local businesses to succeed. Included in the list of areas and industries in which WAA has played a leading or key supporting role are Winnipeg's aerospace industry, the assumption (through a subsidiary) of operational control of Iqaluit International Airport under a 34-year contract and the development of YWG as a major cargo hub, to name just a few.

<u>Aerospace</u>

Canada is a global leader in aerospace and Manitoba is home to Canada's third largest aerospace industry, the largest in Western Canada.

The sector is anchored by four companies that are either headquartered, or have a significant presence in Winnipeg, including Boeing Canada, StandardAero, Magellan Aerospace and Cormer Aerospace. Some two dozen established regional and national firms and a host of small to medium-sized aerospace suppliers including precision machine shops, tool and die makers, precision sheet metal fabricators, plating and coating operations and electronics companies support and enhance the strength of the sector in Manitoba. The industry has also come together to partner in the establishment of the Composites Innovation Centre, a not-for-profit corporation that supports and stimulates economic growth through research, development and the application of composite materials and technologies for manufacturing industries.

Winnipeg is recognized as one of the most cost-effective cities for aerospace manufacturing in North America.

Our aerospace sector is competitive on a global level, producing world-class products for customers on six continents. Over the last 10 years, Winnipeg aerospace companies have shipped more than $3 billion in product exports, including $400 million in exports to emerging markets where Winnipeg companies help meet growing global demand for aircraft and aircraft parts.

Aerospace manufacturing, repair and overhaul account for approximately 80% of industry revenues with aerospace training and services providing 20%.

WAA has played a critical role in the current and continued success of this sector. Canada's largest aerospace composite manufacturing centre (Boeing), the world's largest independent gas turbine engine repair and overhaul company (Standard Aero) and two of the world's most advanced aircraft engine testing and certification centres developed by Pratt & Whitney and GE Aviation are located on or around the YWG campus. YWG's ability to quickly and efficiently move valuable air freight and WAA's willingness to work with aerospace tenants to facilitate the location and development of their facilities along with our dedication of airport lands for future aerospace development give a critical stability to the industry enabling it to plan for the long-term.

Exporting our knowledge

Since 2013, Winnipeg Airport Services Corp. (WASCO), a subsidiary of WAA has participated in a joint project with a major international facilities management company to provide facility maintenance services to Kelowna International Airport.

The Kelowna project served as a springboard to a much more substantial undertaking in which Nunavut Airport Services Ltd. (NASL), another WAA/WASCO subsidiary, has entered into a 34-year management contract to operate the airport in Iqaluit, the capital of Nunavut. This is an innovative P3 arrangement in which other consortium members will design and build a new airport in Iqaluit while NASL manages the existing airport during construction and the new airport after it opens in 2017. The additional revenue it has generated has helped to push WAA's revenue above the $100 million mark for the first time since it was incorporated.

Cargo

As the following map shows, located at the geographic centre of North America, YWG is ideally positioned to function as a cargo gateway for shipments connecting Canada and the world. Although Winnipeg's airport has been involved in cargo shipping for over 80 years, in the past dozen years WAA has developed into one of Canada's most important cargo hubs.

Winnipeg has extensive trucking operations and can reach most major points inside 24 hours and all of the Continental United States and Canada within 48. It is also fully served by three Class 1 railways, CN, CP and BNSF.

YWG has been able to leverage this continent-wide connectivity to become the largest cargo distribution centre between Vancouver and Toronto. One of the most reliable airports in the world, it has less than two hours in downtime *annually*. It is the number one dedicated freighter airport in Canada with over 5,000 flights per year. A certified trans-shipment point, YWG is the main hub for transit freight in Canada with the capacity to trans-ship cargo between foreign carriers, with truck/rail carriers, and with Canadian air carriers.

YWG is also the northern hub of the Mid-Continent Trade and Transportation Corridor, connecting Canada to a central North American market of 100 million people. The Corridor provides seamless and efficient inter-modal transportation linking major commercial centres in the Canadian and American Midwest, through the Southwest and deep into Mexico.

The Mid-Continent Trade and Transportation Corridor

Since 1999, cargo shipments through YWG have increased from an estimated 100,000 tonnes (approximately) to over 175,000 tonnes today. Through the implementation of the airport Master Plan, WAA anticipates total cargo shipments will increase over the next twenty years to over 280,000 tonnes.

Looking to the future, YWG sits within the catchment area of CentrePort Canada Inc., the first inland port in Canada, which, when developed to its full potential could significantly augment YWG's position as a cargo centre.

YWG's ability to achieve its full potential as a cargo hub will obviously depend on a variety of factors. Not least among them is the development of a cohesive, national air transportation policy that fosters the success of Canada's communities. Part of that policy must include a focus on international trade and services agreements that liberalize *cargo* movement. Canada has a number of agreements in place intended to liberalize *passenger* movement, but more are needed to address *cargo* traffic, particularly with countries where trade and the potential for trade is large, for example, the BRIC nations.[2] The payoff for liberalizing air cargo movement is disproportionate; according to the Conference Board of Canada, even though air cargo accounts for only about 3% of the volume of shipped goods, due to its value and time-sensitivity it accounts for about 35% of the value of shipped merchandise.[3]

WINNIPEG & WAA – GATEWAY to the NORTH

We recognize the Panel has a particular interest in Canada's North and the unique transportation challenges it faces. WAA agrees with the Panel's statement in the Discussion Paper that, "transportation infrastructure is the key to unlocking potential developments that can

[2] Brazil, Russia, Indian & China
[3] *Growing Canada's Economy: A New National Air Transportation Policy*, Conference Board of Canada, September 2013 http://www.cacairports.ca/sites/default/files/Docs_2013/GrowingCanadasEconomy-ANewNationalAirTransportationPolicy.pdf

be leveraged to improve connectivity and services in remote northern Canada."
WAA has a unique and longstanding relationship with the North and so has a unique perspective on the role air transportation can play in its future. Since the earliest days of its operation over 80 years ago flying supplies to mining and logging camps, Winnipeg's airport has had a close connection to the North. From the first Fokker Universal Monoplane to today's jets, people and cargo have been flying between Winnipeg and the North.

Today tourism and resource development are recognized as two central drivers of the North's economy. As the main hub for moving people and cargo to and from the Central and Eastern Arctic, YWG is a critical enabler of both of those drivers.

In just four years, cargo movement through YWG to the North has grown from under 7,000 tonnes annually in 2010 to over 8,520 tonnes in 2013. YWG has become a critical part of the re-supply chain for the Central and Eastern Arctic. For example, since 2012 two of the largest Northern retailers, The Northwest Company and Artic Co-operatives Limited have each dramatically increased cargo operations to supply their northern outlets. We now have daily non-stop flights to Rankin Inlet and multiple weekly non-stop flights to Iqaluit. In the coming years total tonnage shipped to Northern destinations from YWG is expected to continue to increase.

Although detailed data is simply not available, we know from anecdotal sources that Winnipeg and YWG serve as a jumping off point for a significant percentage of Northern tourism. We also know we are ideally positioned to capture an even larger share of a growing market since many flights to the North combine cargo and passengers. Given the importance tourism holds for the North's future, it's also clear Canada will have to invest in tourism promotion in the United States and elsewhere.

Recognizing the potential it holds, WAA has a specific strategy to deepen its connections and opportunities in the North. The strategy includes community and partner development. For example, WAA has entered into a partnership with the Town of Churchill to work with the community to realize the economic potential of its transportation assets. WAA's strategy also includes securing management contracts for Northern community airports. The NASL venture in Iqaluit is just one example. WAA's plan is to build on that project to secure more contracts.

WAA sees the potential for, and has long-range plans to develop, a health facility located at YWG and specifically geared to the needs of Northern residents since a large proportion of trips are made to access medical services.

At the same time, WAA recognizes the challenges Northern transportation faces and the important role this Panel has in shaping that future.

In its December 2010 report, "Mapping the Economic Potential of Canada's North" the Conference Board of Canada said:

> …air services to Canada's North are relatively expensive, placing its tourism destinations at a disadvantage, in terms of price-competitiveness. Flight schedules can be inconsistent and inconvenient, especially for visitors travelling from abroad. In many communities, airport infrastructure is aging and inadequate, and needs significant upgrading. And, even if the airport infrastructure is in place, expanding the level of air capacity can be a

> complicated and costly venture, as airlines are often reluctant to gamble on new air services without a financial incentive.[4]

Although the report was speaking of tourism in particular on this point, similar issues arise for resource development.

And as the Panel's Discussion Paper notes:

> Ports and airports in remote areas of Canada often do not have sufficient traffic volumes to generate revenues necessary to maintain their infrastructure, while continuing to meet the strengthened safety and security standards that Canadians expect. Similarly, air, bus, rail and ferry passenger services that provide regional connectivity in many parts of the country are often challenged to maintain year-round routes and frequencies for small numbers of travellers. Federal, provincial and territorial governments subsidize some of these services, but there is no clear federal policy and levels of taxpayer support vary widely between modes and jurisdictions.

No one can say at this point what the solution, or more likely *solutions,* might be but we do know the costs of safety and security, as well as basic airport operational costs from procurement to IT to financial management are all increasing. The cost impacts of such increases will only be magnified in the North.

It is our view the solutions can and will be found if we focus Canada's national transportation strategy on the *consumers* of transportation services and foster the ability of local authorities to customize the transportation services and offerings at their airports to the needs of their communities.

While by no means the only solution, innovative arrangements like that entered into by NASL, the construction consortium and the Government of Nunavut to build and operate a new airport in Iqaluit may be one of the best ways to ensure adequate infrastructure remains effective and affordable in the North. Canada's policy as it relates to airports needs to foster such arrangements.

WAA Recommendations Related to the National Transportation Policy, International Trade & the North[5]

1. Amend the *Canada Transportation Act* to place Canadian communities and the individual and business consumers who live and work within them at the heart of Canada's National Transportation Policy.

2. Ensure effective coordination of transportation policy initiatives across relevant Federal departments and with provincial counterparts, including international trade, tourism, environment, Northern development.

3. Increase the number and scope of bilateral trade agreements to liberalize *cargo* traffic, particularly with countries where trade and the potential for trade is large,

[4] http://caid.ca/CBoCMapEcoPotNor2010.pdf
[5] All recommendations in this submission are intended to supplement the recommendations contained in the CAC Submission.

for example, the BRIC nations.

4. Invest in tourism promotion in the United States and elsewhere with a special (though not exclusive) emphasis on the North.

5. Foster the development of innovative arrangements between and among airports to meet the unique demands of the North.

IMPEDIMENTS TO CONTINUED SUCCESS

But what of YWG's future?

YWG faces a number of significant impediments and challenges to its long-term growth and viability. Chief among them are the unduly high taxes, fees and other system costs imposed on Canadian airports, a broken air transportation security agency, an air carrier duopoly resulting in a basic lack of competition and *ad hoc* policy making by the Federal government.

SYSTEM COSTS

Introduction

WAA shares the view that the Canadian model – to use the language of the 2012 report from the Canadian Senate [6] – treats our airports as "toll booths" while other countries have recognized them for the economic engines – or "spark plugs" – they truly are.

Two broad considerations emerge. First, is the burden of system costs being shared appropriately? And second, are the costs imposed achieving an appropriate end?

Airports are strategic assets that benefit *all* Canadians. Even if a person working at the Fairmont Hotel in downtown Winnipeg or a farm in southern Manitoba never sets foot in YWG, they clearly benefit greatly from its presence. But for the ability of others to connect to Winnipeg through YWG, the hotel wouldn't have guests and the farm wouldn't have markets. Similarly, airport security is a national issue of great importance to *all* Canadians regardless of whether they physically use an airport. Yet Canada has created a model where those who use the airport system shoulder *all* of the costs and more. If one accepts airports are now a critical component to the success of the *entire* economy, is it still sound policy to load the full cost of airports onto only those consumers who directly use the facilities?

Common sense says every dollar a consumer spends on fees, taxes and the like is one less dollar they have available to spend on other items. It is therefore critical that all government fees, charges and system costs related to air transportation be carefully scrutinized. Is the particular charge necessary? What purpose is it trying to achieve? Is there another way to achieve the same end without further taxing the consumer? Has the consumer already paid the charge directly, or indirectly? Are the costs being shared appropriately and in the most economically efficient way? Does the charge incent the desired behaviour?

[6] Standing Senate Committee on Transport & Communications, June 5, 2012 "*The Future of Canadian Air Travel: Toll Booth or Spark Plug*", Report on the Future Growth and Global Competitiveness of Canada's Airports, <http://www.parl.gc.ca/content/sen/committee/411/trcm/rep/rep05jun12-e.pdf>.

Airport Rent
The CAC Submission, as well as submissions, commentaries and reports to the Panel and elsewhere have commented on the rents paid by airports to the Federal government. WAA certainly echoes all of the concerns already raised.

Since assuming control of the airport, WAA has paid just shy of $75,000,000 in airport rent to the Federal government. By the end of 2018, we expect to pay at least an additional $30,000,000 in rent under the Ground Lease.

Transport Canada and the Airport Authorities entered into their rent arrangements over two decades ago. Times have changed since then – dramatically. The government's financial situation at the time was a key driver of the devolution decision. At the same time the funding practices then in place formed an important part of the context in which the rent formula was derived. Certainly no one foresaw how much the formula would truly cost airports and how much it would contribute to federal coffers.

To put some perspective on WAA's contributions to Canada's general revenue fund and the degree to which the current rent arrangement can create perverse results one need consider only a few examples.

When WAA took over the Winnipeg airport in 1997, it was understood one runway, the central utilities building, or "CUB" and the terminal itself would all need to be replaced within about a decade. Indeed, the replacement of Runway 13/31 was an express requirement under the Ground Lease. By the terms of the Ground Lease, WAA paid for and completed the reconstruction and once completed began to pay an additional $2.6 million in rent each year. The total cost of the runway reconstruction was $12 million. The CUB was rebuilt at a cost of $38.5 million. The new Air Terminal Building together with the associated work on aprons, taxiways, parking and the like cost approximately $585 million. Work on both the CUB and the ATB was completed in 2011. Simply to maintain YWG's infrastructure, WAA spends an average of $15 million every year on capital.

WAA pays for all capital expenses at YWG through debt financing by issuing bonds in the marketplace. It currently has some $624 million in such long term bonds for which the annual financing cost is $33 million. Airport Improvement Fees, or "AIF", collected from YWG passengers, offset the financing cost. Because the ground rent is calculated on the basis of gross revenues and because the AIF is included in airport revenues, every improvement an airport makes to its infrastructure – an improvement, it should be noted, the Canadian government had refused to make – the government receives more rent.

The net result of the exercise is the Federal government not only avoided major capital expenditures at a time when it could ill afford them, but in fact converted those expenditures into a substantial, and steadily increasing, annual revenue stream.

In a related vein, the airport rent structure also drives irrational business-decisions on the part of airports. As one small example, tenants at YWG often ask WAA personnel to undertake minor construction or maintenance tasks on their premises. WAA has personnel onsite to undertake that sort of work on WAA property. For many reasons it would make sense they also be able to provide that service to our tenants; the tenants are familiar with WAA staff, WAA personnel are onsite 24/7 and WAA staff are both familiar and compliant with the many airport security requirements associated with moving people, tools and equipment around the airport. WAA could easily undertake the work and because it would be undertaken primarily as a service to our tenants would do so on a cost-recovery basis.

However, because airport rent is calculated on gross revenue and because WAA would therefore have to include the charges to the tenant in its rent calculation, WAA has to charge more than the cost simply to stay whole. For example, a $1,000 charge has to be grossed-up by some 15 percent to capture (most of) the additional rent WAA will have to pay. The first ten percent of the gross-up covers the actual rent, but, because the formula creates an endless loop of rent charges on revenues, the additional five percent keeps WAA close to (though not quite) whole. As a result, WAA discourages tenants from having WAA personnel perform the work even though it would be in everyone's interest if they performed it. In the long-run this ends up costing the tenants more than they would have to pay were they able to use WAA personnel. Those costs in turn will almost inevitably be passed back to the tenant's customers.

The same grossing-up principle applies to Airport Improvement Fees and every other revenue generating activity at the airport. Because the AIF has to be included in rent, every dollar of AIF needed to cover a capital expense must be grossed-up to ensure the airport can collect what it needs to offset the capital cost.

And as a final example, consider airport policing costs. When airports were devolved to local control, the Federal government covered the cost of policing. With one change in the regulations, airport policing became an airport responsibility. WAA spends over $3 million every year to provide police services at YWG. We recover the expense through additional charges to tenants, licensees and carriers. Those charges form part of our revenue, which in turn means the Federal government collects an additional $300,000 in rent each year. That sort of outcome was never in the contemplation of the parties entering into the Ground Lease.

Naturally, WAA can only offer examples of the circumstances at YWG, but we are confident every major Canadian airport could point to similar situations related to the impact of the airport rent structure.

It's clear the Ground Rent arrangement is hampering airport competitiveness. It is equally clear the arrangement is no longer serving Canada's broader interest. It's time for a change.

Other Fees
Again, the CAC and others have set out in considerable detail the arguments against, and negative impacts of, Canada's excessive air travel fees and taxes.

WAA endorses the CAC's arguments and recommendations regarding Enhanced Economic Competitiveness.

<u>WAA Recommendations Related to System Costs</u>

6. Require the re-examination of every air transportation tax, fee, charge, rent or levy to ensure:

    a. Its burden is being appropriately shared by all who benefit from the activity in question;

b. It is maximizing the benefit to the consumers of transportation services.

7. Eliminate airport rent.

TRAVELLER SECURITY EXPERIENCE (CATSA)

WAA does not propose to reiterate the submissions made by CAC and others regarding the issues with CATSA. We endorse the CAC's submissions on the subject and offer a few additional points of emphasis.

The impact of CATSA's dysfunction at YWG is very real. As is the case at all Canadian airports, travel is more time-consuming and less appealing. The problems with CATSA simply drive business away. It remains a service provided inside government but not paid for by government.

CATSA has no tangible key performance metrics other than to live within its annual budget. It is not measured against any customer service standards whatsoever. In the absence of any requirement to meet minimum performance targets, it is not surprising air travellers are more and more frustrated by the experience of air travel in Canada. One indication of the problem is the steady decline in "Airport Service Quality" scores on matters within CATSA's control over the past number of years. Measured under the auspices of the Airports Council International at airports around the world, an ASQ score is the only global benchmarking programme measuring passengers' satisfaction while they are at an airport. They are based on the survey responses of random samplings of passengers at each airport and cover a wide variety of topics designed to provide insight into important elements of the customer experience at an airport.

Of greater concern are the longer term implications of Canadian airports competing for CATSA services. Some airports are now paying for additional hours or technology to mitigate the delays. As larger, better-resourced airports buy up CATSA services comparisons are inevitable. Our own community will begin to wonder ever more loudly why the problems here are worse than they are elsewhere. WAA's only alternative is to join the CATSA subsidization game and add more costs to our airport.

Security screening is a federal mandate. There is no reason why the level of service should not be comparable if not identical at all Canadian airports. It certainly must not be allowed to become a competitive tool differentiating one airport from another.

<u>WAA Recommendations Related to CATSA</u>

8. In conjunction with CAC recommendations, ensure CATSA:

   a. Operates under industry accepted Key Performance Metrics related to service delivery.

   b. Provides service consistent at all Canadian airports so that it cannot be used as a competitive tool to differentiate one Canadian airport from another.

LACK of COMPETITION

In our view, the need for Canada to focus on transportation consumers and ensure their connectivity is of paramount importance. The current situation at YWG is a symptom of Canada's failure to do so over the past ten to fifteen years. YWG is hampered by a basic lack of airline competition; we exist in a duopoly market.

If Transport Canada were to mandate full disclosure by air carriers of airport specific origin and destination data similar to the disclosure requirements imposed by U.S. regulators on carriers flying to the U.S. (including, somewhat ironically, Air Canada and WestJet), concrete proof of YWG's situation would be relatively straightforward. Unfortunately, we only receive such data on a confidential basis and so are not at liberty to disclose it without air carrier consent.

However, even without the confidential data, common sense and the data that can be disclosed will serve to make the point.

Passenger traffic at YWG falls into three categories:

1. Domestic
2. Transborder
3. International

Domestic, *mainline* traffic refers to flights operated by the WestJet or Air Canada families. It makes up the vast majority of all traffic at YWG. For example, in 2014 domestic mainline traffic made up over 70% of all traffic at YWG. More importantly, between them they carry 100% of the traffic between YWG and each of the major Canadian air hubs in Toronto, Vancouver, Calgary and Montreal.

A handful of small domestic carriers operate on regional routes the mainline carriers never served, or no longer serve. In 2014 it made up less than 9% of total traffic at YWG. The regional carriers operating at YWG are Perimeter Airlines, Calm Air, Bearskin and First Air.

Transborder traffic refers to flights to and from the U.S. In 2014, it accounted for approximately 13% of the total traffic at YWG.

At YWG, international travel is made up entirely of seasonal, sun-destination flights. There is no direct, scheduled year-round service from YWG to any other international destination. In 2014, international travel accounted for slightly less than 5% of total traffic.

Airlines are supply and demand driven businesses and price accordingly. As long as passenger demand remains strong, there is no reason for a carrier to alter its pricing. For example, according to a March 2015 Moody's Investor Services analysis, despite the recent dramatic drop in oil prices, both Air Canada and WestJet have recently indicated they do not intend to reduce their fares.[7]

The real story when it comes to the competitive landscape at YWG is found in the steadily increasing load factors on Air Canada and WestJet flying to and from YWG. "Load factors"

[7] Moody's Investor Services, Sector In-Depth, North American & European Airports, March 10, 2015, "Oil Drop Helps Most Airports But Exposes Ones Tied to Oil Industry"

indicate the percentage of occupied seats versus available seats on a plane. Over the past decade seat capacity at YWG has gradually been reduced. It has shifted away from smaller airports like Winnipeg, Ottawa and Halifax and been re-allocated to other markets. In pursuit of their “hub and spoke” models, Air Canada and WestJet have focused on connecting as many passengers as possible through their hubs in Toronto, Vancouver, Calgary and Montreal. When combined with a steady increase in demand over the same time period that reduction in supply has resulted in average load factors to and from YWG substantially in excess of their publicly disclosed, *system-wide* load factors for 2014 of 83.4% (Air Canada) and 81.4% (WestJet). As one would expect, as supply is squeezed, prices have increased and the propensity of Manitobans to travel decreases.

Our data shows the load factor for Winnipeg-Toronto is over 90%, which is consistent with anecdotal evidence of virtually every flight being completely full and of passengers having to change travel plans and stay longer or leave sooner than they would prefer simply due to the unavailability of seats. In WAA’s experience, seats are not only unavailable at a reasonable price, but far too often they are unavailable at *any* price.

The negative impact on the connectivity of an airport like YWG can also be seen by comparing where YWG passengers *want* to go relative to where they are *forced* to go in order to get there. Figure 1 compares YWG’s Top 10 Emplaned & Deplaned destinations to its Top 10 Origin & Destination markets. Emplaned & Deplaned, or “E&D” data shows the destination where YWG passengers first landed on their journey. Origin & Destination or “O&D” data shows the *ultimate* destination of YWG passengers.[8]

Figure 1
E&D vs O&D, 2012

Airport	ED Passenger	OD Passenger
Toronto	1,009,442	593,680
Calgary	418,805	264,900
Vancouver	341,872	237,900
Edmonton	196,556	188,610
Minneapolis/St Paul	192,534	16,280
Montreal	162,896	110,190
Ottawa	162,031	177,500
Chicago	134,495	28,670
Saskatoon	71,091	83,500

Figure 1 tells us almost 42% of all YWG passengers travelling through Toronto in 2012 were only connecting there; their ultimate destination was somewhere else. The number of YWG passengers connecting through Vancouver, Montreal and Calgary ranged from 31% to 37%. In the case of Chicago and Minneapolis/St. Paul the numbers of connecting passengers were 79% and 92% respectively.

[8] Source: InterVISTAS 2012 Market Study and DIIO Fmg. These figures are based on industry-accepted econometric models. They are within a few percentage points of accuracy either way. For the sake of comparability to other data used in this submission we have used 2012 figures.

In 2012, YWG's total passenger traffic was 3.53 million. That means almost 1.25 million of YWG's passengers did not want to go to any of those airports; they were only there because the airlines routed them there. The data for 2014, although not yet finalized, indicates the situation has, if anything, grown worse, as a still greater percentage of YWG passengers are being pushed through the hubs.

The following helps illustrate how being forced through hub airports is limiting the connectivity of YWG's passengers. It shows the Top 10 destinations with no direct scheduled service from YWG.

Figure 2
Top Ten Unserviced YWG Destinations

Rank	Destination	No. of Passengers
1	Halifax, NS	38,320
2	Victoria, BC	35,890
3	New York, NY	32,400
4	Manila, PH	31,600
5	Kelowna, BC	30,470
6	Hamilton, ON	23,330
7	Los Angeles, CA	22,960
8	Honolulu/Kahului, HA	20,550
9	Abbotsford, BC	20,270
10	London, UK	18,820

It is generally accepted that anything above 30,000 passengers per year travelling to a particular end destination warrants serious consideration for direct scheduled daily service from the origin to that destination. Figure 2 shows traffic patterns and volumes that could warrant direct service between YWG and an array of additional domestic, transborder and international destinations. Yet none is offered by the mainline carriers, as they continue to route traffic through their hubs.

What Figure 2 cannot show is the phenomenon of induced demand, the availability of additional supply generating additional demand. It has been YWG's experience that where capacity at YWG has been added and properly promoted the mere presence of that capacity has resulted in total traffic that exceeds the original O&D traffic. For example when a direct flight was added from YWG to Palm Springs, California the number of passengers travelling to Palm Springs quickly doubled the number who travelled there before the direct flight was available. This isn't surprising, as many travel decisions are based on the ease and convenience of travel as much as the price; more people are willing to travel to a destination where they don't have to connect to get there.

Squeezing YWG traffic through their hubs serves two purposes for the carriers. First, it generates more revenues for them by limiting supply. Secondly, and perhaps more importantly from a systemic perspective, it reinforces the hubs. The stronger the hub, i.e., the more traffic moving through it, the harder it is for a potential competitor to launch point to point service that overflies the hub. Furthermore, it enhances the carriers' ability to lobby government to restrict bilateral air agreements in the name of preserving Canadian jobs. By contrast the experience in many other countries (Australia, New Zealand and Singapore being prime examples) has been that consumers and the overall economy have benefitted greatly from more open access. There's no question closed access benefits the carriers and the hub airports, but in a country as large and diverse as Canada does it really benefit the consumer?

Canada's mainline carriers have adopted a logical business strategy aimed at enhancing shareholder returns. The net result, however, is it makes it much more expensive and much less convenient for Manitobans and anyone else in the YWG catchment area to travel by air to the places they want and need to go. The capacity squeeze to and from hub airports and YWG makes it more difficult for Manitoba businesses to expand their reach to new and existing markets and to attract new or expanded business into the Province. Without additional competition neither carrier has any incentive to stray from their current hub and spoke models that route traffic through their hubs. The inconvenience and additional expense to the customer flying to or from a city like Winnipeg doesn't factor into the equation.

There is no question the mainline carriers' choice of business strategy damages our region's connectivity. To the extent that strategy is a function of a free and open market, WAA has no basis to complain. However, it is our position the carrier's ability to choose that strategy is enabled by the artificial barriers to competition produced by Canada's national transportation policies. To be clear, we are *not* suggesting non-market structures or regulations should be put in place to generate competition artificially. Rather, the *artificial* barriers exist should be removed so the market in Winnipeg can be free to unfold as the market dictates.

In YWG's view there are two primary non-market barriers that ought to be removed:

- The federal government's protectionist international trade policy as it relates to "open skies"; and
- The federal policy as it relates to foreign ownership of Canadian carriers.

WAA endorses the CAC Submission and recommendations regarding open skies agreements.

However, we respectfully submit the CAC's approach to the current foreign ownership limits is more cautious than is warranted.

Where the CAC advocates moving to 49 percent for European investors (in the context of the Canada-EU agreement), WAA goes further and says the limit should be increased for *all* (non-sovereign) investors.

Foreign Ownership

The existing foreign ownership rules inhibit new investment. Airlines are capital intensive businesses; carriers must have access to the right fleets at the right time if they are to succeed. Access to capital has been and continues to be an issue in Canada.

Restricting access to capital limits competition by artificially increasing the cost of that capital. In the long run it does not serve the interests of Canadian consumers.

Under current rules foreign ownership is limited to 25 percent, but could be increased to 49 percent without amending the legislation. That increase would free up billions of dollars in potential foreign investment. The average cost of capital could be reduced, debt retired and services improved. It could, many say it *would*, be the difference that enable new carriers to enter the market.

Many observers including the Canadian Competition Commissioner[9], the Canadian Competition Review Panel[10] and others have recommended the foreign ownership limit should be increased to the maximum of 49 percent. The Competition Review Panel concluded that "increasing the level of foreign investment permitted in the air transportation sector would increase sustainable competition in the Canadian industry."

WAA concurs with these views and says the limit should, at a minimum, be increased to 49 percent across the board.

AD HOC POLICY-MAKING

This Review is timely to say the least. Without intending to cast blame or point fingers, the simple reality is Transport Canada has not had a focused policy strategy for some time. This has led to an *ad hoc* approach to policy initiatives and activities.

Surprisingly, in light of the CTA Review – which is clearly the proper forum in which to examine major policy initiatives related to the long-term future, governance and operation of Canada's airports – there are two very recent and ongoing examples of this *ad hoc* approach. They are the Air Sector Review undertaken by Transport Canada commencing in the summer of 2014 and the amendments to the *Aeronautics Act* introduced through the Government's *Second Budget Implementation Act* (Bill C-43), which came into effect December 2014.

Both have caused and are continuing to cause considerable – and in YWG's respectful opinion, quite unnecessary – effort on the part of the Canadian airport community. A clearly defined policy strategy would help to avoid just this sort of problem.

TANGIBLE IMPACT of THESE IMPEDIMENTS

The impact of the impediments described above is cumulative. Canada's airports will become increasingly uncompetitive the longer these impediments remain in place. And the longer they remain unaddressed the more radical and expensive will be the steps to address the problems they create. It is YWG's submission we should deal with the problems now when they are relatively manageable and solutions are at hand.

There is ample evidence of the impact Canada's policies are having on YWG as we speak. We need only look to the competition YWG faces from south of the Canada-U.S. border.

As it is for a number of Canadian airports, "leakage" of passengers to U.S. airports is a serious issue for YWG. In YWG's case the leakage is to three North Dakota airports. The airports in Grand Forks and Fargo, North Dakota are 2.5 and 4 hour drives respectively, south of Winnipeg.

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[9] Commissioner of Competition Bureau Submission to Competition Policy Review Panel, January 11, 2008, http://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/eng/02555.html>

[10] *Compete to Win*, Competition Policy Review Panel, Final Report June 2008 at p.-42. https://www.ic.gc.ca/eic/site/cprp-gepmc.nsf/vwapj/Compete_to_Win.pdf/$FILE/Compete_to_Win.pdf

The airport in Minot, North Dakota is 5 hours WSW of the City. The Grand Forks airport website boasts that "GFK is proud to be the closest U.S. international airport to Winnipeg, Manitoba, Canada."

WAA estimates that in 2012 some 280,000 transborder passengers from YWG's primary catchment area chose to fly out of Grand Forks International Airport (GKF), Minot International Airport (MOT), or Hector International Airport (FAR) in Fargo.

Other studies and submissions, including the Senate report cited above (Footnote 5) and the CAC Submission, accurately portray the cost disadvantage faced by Canadian airports relative to their U.S. counterparts. WAA agrees with those comments and specifically endorses the CAC Submission on the point.

While certainly not the only cost advantage favouring our American competitors, the contrast when it comes to property tax is particularly stark. North of the border, WAA *pays* municipal property taxes to the City of Winnipeg. South of the border, our competitors actually *collect* property taxes, which they use to offset capital costs. And as airports under the regulatory authority of the U.S. Department of Transport each is eligible for and has received federal grants to pay for the vast majority of their major capital expenditures. In short, taxpayers in North Dakota and across the United States heavily subsidize their operations.

The loss of those passengers to U.S. airports costs Winnipeg jobs and damages its economy. As part of the overall economic impact study of YWG conducted in 2012, WAA commissioned a number of microeconomic impact studies to provide a snapshot in time of the direct local labour generated by firms involved in providing passenger air services at YWG. These micro-studies demonstrate the extent of the potential economic benefits to the surrounding community and economy that are associated with the air passenger services. However, they do *not* quantify the full impact of the airport and its operations.

Every departure of a passenger flight from YWG generates labour hours for individuals with jobs involved in handling passengers, their baggage, cargo and the aircraft. These labour hours will differ based on a number of factors, one of them being whether the flight is domestic, transborder, or international. Domestic flights require the lowest number of labour hours, while international involve the most; transborder flights are roughly in the middle.

One of the micro-studies measured the annual direct local labour generated by a transborder return flight by a 136-seat Boeing 737-700 operating year round with four flights per week. The study measured the average impacts for a typical transborder flight using the specified aircraft type. The average labour impact is the sum of all of the labour hours from all jobs associated with each flight. The direct labour impact is 13 Full Time Equivalent jobs with an economic output of $3,575,000. When indirect and induced labour impacts are included, the total climbs to 30 FTEs with a total economic output of $6,109,000. Four flights per week operating year round means 208 individual return flights or a $29,400 impact every time the plane leaves and returns.

Simply to give a sense of the potential impact of the transborder traffic flying from North Dakota instead of YWG consider that 280,000 passengers is equivalent to anywhere from 1,030 Boeing 737-700 return flights (if every plane is full) to 1,184 flights (if we assume a more realistic 85% load factor). That amounts to between $30 and $35 million in annual economic output. At least as importantly, it would mean an additional 150 to 172.5 FTEs.

<u>WAA Recommendations Related to Competitiveness</u>

9. Require carrier disclosure of relevant and reliable market data related to passenger and cargo traffic at least comparable to the disclosure required of carriers operating in the United States.

10. Immediately increase the limit on non-sovereign foreign ownership of Canadian airlines to 49% regardless of the investor's nationality.

CONCLUSION

We live in a global economy. Canada's future depends on the health of its communities from coast to coast to coast. It is the people from Petty Harbour to Tofino to Iqaluit living and working and succeeding in their communities' day in and day out who will guarantee Canada's future. Their success over the next thirty years will depend on connectivity. If our communities have access to the markets they need, they will thrive; if not, they will whither and die.

As we said at the outset, Canada's National Transportation Policy must recognize Canada's consumers and the communities in which they live as the foundation upon which our national economy is built.

Currently Canada *has* no clear national transportation strategy; rather there is a mishmash of *ad hoc* policy initiatives driven by unclear and often competing, objectives. To be successful thirty years from now Canada cannot afford to continue blindly stumbling along as it has for the past ten. Excessive government taxes and fees and an inefficient and underfunded security regime have made our national air transportation system increasingly uncompetitive from a global perspective. Protectionist trade policies have resulted in a model that protects individual air carriers and artificially favours one community over the other. In the long run, the country's core will be hollowed out in favour of a few large centres.

The remarkable success of Canada's airports over the last two decades has been precisely *because* the federal government gave up the centralized command-and-control model in favour of local control. Even though airports are seen as strategic national assets that benefit all Canadians, the reality is they function most effectively when we recognize they are first and foremost strategic *community* assets.

If our airports and with them our communities are to thrive over the long-term:

- Government policy must recognize and reinforce airports as economic engines rather than as tollbooths from which and through which to extract revenue. It's time to force a re-examination of every fee, charge and tax imposed on the system to ensure it enhances rather than inhibits the communities that rely on Canada's airports;

- Canada's air security agency needs to be completely overhauled and given the tools and resources it needs to become a world leader in the secure and efficient processing of people and goods;

- Canada's international air policy must be geared to the advancement of the local economies that build the industries, jobs and communities upon which our future depends. It's time to abandon outdated protectionist policies and maximize foreign investment potential into Canada to stimulate the air transportation marketplace; and

- Canada must develop a coherent and comprehensive long-term air transportation strategy focused on Canadian consumers and the communities in which they live.

WAA would be pleased to respond to any questions the Panel may have regarding this submission, or to provide any additional information that may be of assistance in the Panel's deliberations.

Summary of WAA Recommendations in Addition to CAC Recommendations

1. **Amend the Canada Transportation Act to place Canadian communities and the individual and business consumers who live and work within them at the heart of Canada's National Transportation Policy.**

2. **Ensure effective coordination of transportation policy initiatives across relevant Federal departments and with provincial counterparts, including international trade, tourism, environment, Northern development.**

3. **Increase the number and scope of bilateral trade agreements to liberalize cargo traffic, particularly with countries where trade and the potential for trade is large, for example, the BRIC nations.**

4. **Invest in tourism promotion in the United States and elsewhere with a special (though not exclusive) emphasis on the North.**

5. **Foster the development of innovative arrangements between and among airports to meet the unique demands of the North.**

6. **Require the re-examination of every air transportation tax, fee, charge, rent or levy to ensure:**

    a. **Its burden is being appropriately shared by all who benefit from the activity in question;**

    b. **It is maximizing the benefit to the consumers of transportation services.**

7. **Eliminate airport rent.**

8. **In conjunction with CAC recommendations, ensure CATSA:**

    a. **Operates under industry accepted Key Performance Metrics related to service delivery.**

    b. **Provides service consistent at all Canadian airports so that it cannot be**

used as a competitive tool to differentiate one Canadian airport from another.

9. **Require carrier disclosure of relevant and reliable market data related to passenger and cargo traffic at least comparable to the disclosure required of carriers operating in the United States.**

10. **Immediately increase the limit on non-sovereign foreign ownership of Canadian airlines to 49% regardless of the investor's nationality.**