Can value be found in the European airport sector?

By Dermont **McCLOSKEY**

Private market investors looking to invest in the airport sector have seen pricing progressively step up over the last decade as the number of investable opportunities has declined. In this context, and the continued uncertainty arising from Brexit, we look at where value can be eked out in this ultra-competitive sector.

The airport sector has for many years been one of the most closely contested infrastructure sectors globally, with fund managers, specialist airport operators and institutional investors all vying to secure control of what is often seen as the 'trophy asset' in any investor's portfolio.

Nowhere is this more the case than in Europe, where widespread use of asset privatizations to upgrade and modernize transportation networks has engrained long-term patterns of private ownership within the sector.

However, at the end of 2018, only six M&A transactions worth a combined $853m have completed in European airport during the year[1], compared with $5.5bn worth of transactions in 2017 and $5.4bn in 2016.

The shortfall in investable opportunities has been coupled with an oversupply of capital looking to invest in a sector offering high barriers to entry, robust cash flows and regulatory safeguards.

In the last decade more than $3.8tn trillion of capital has been raised by specialist infrastructure fund managers, with a comparable sum having been invested directly by institutional investors and sovereign wealth funds according to Inframation analysis.

These inflows of capital have fueled competition within the sector and resulted in a transformation in airport ownership, with institutional investors and sovereign wealth funds now controlling over 30% of the region's airports compared with 18% when the assets first entered private sector hands (see Figure 2).

This trend looks set to accelerate as traditional M&A transactions within the sector continue to be dominated by those investors with the lowest cost of capital.

In western Europe, current sales in Gatwick, Brussels and Edinburgh airports all look set to complete in line with comparable airport transactions by fetching in excess of 20x EBITDA (Figure 3) which is significantly over >

Figure 1: European project finance activity, 2007 to December 2018

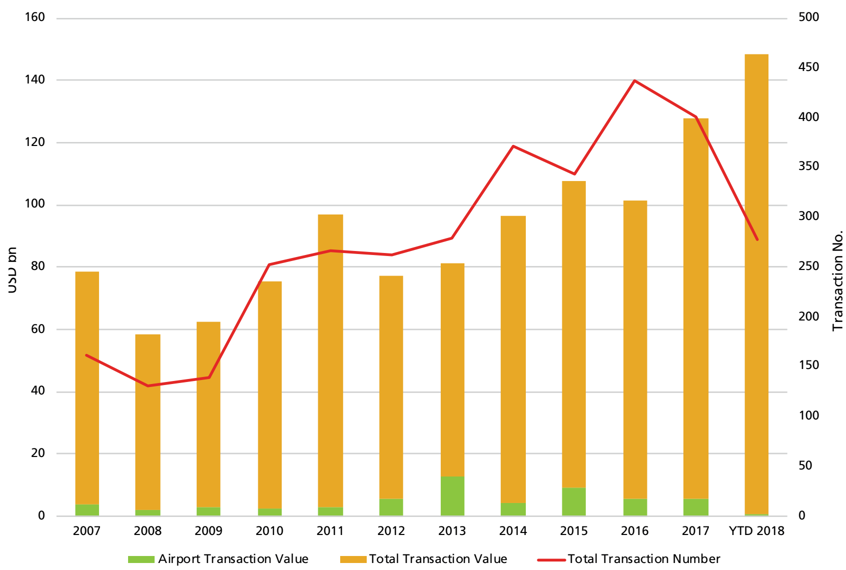
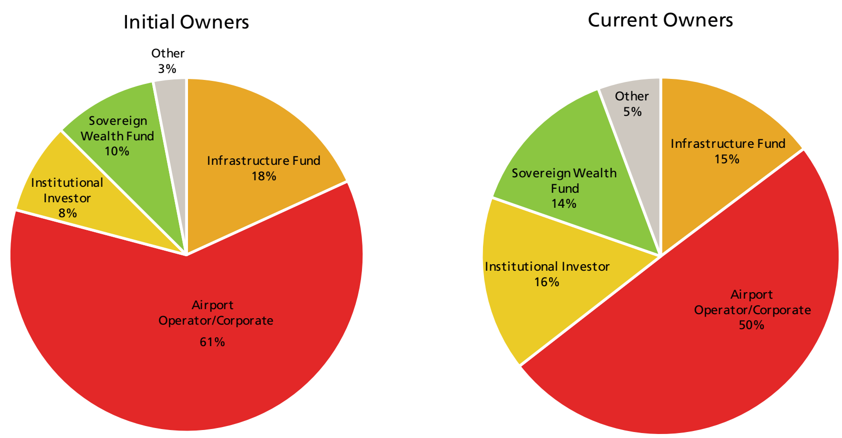


Figure 2: Ownership analysis of privately-owned European airports



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1. Not including Gatwick

average multiples amongst the listed airports in the GLIO Coverage (line). At the time of writing, Vinci Airports announced plans to acquire 50.01% of Gatwick Airport at an estimated 20x. Vinci also holds 8% of Aeroports de Paris (ADP). It has been rumored for a while now that the French government would sell a part, or all of its 50.6% stake in ADP. Current valuations would indicate the interest is in the region of €10bn.

This all takes place in the face of continued political and economic uncertainty arising from Brexit. In the most extreme scenario, this could lead to the loss of air traffic rights between the UK and Europe if consensus over the open-skies agreement fails to be reached.

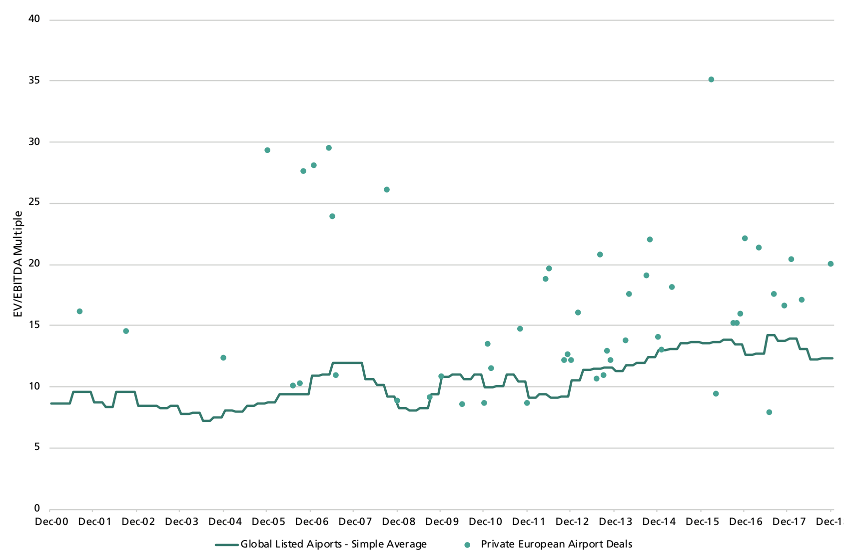
Even an orderly departure from the EU could pose a threat to flight destinations from the UK as any fall in the value of Sterling would likely have an adverse effect on passenger volumes. In the face of increased political uncertainty and ever higher asset valuations, it may not be unreasonable to question whether many directly investable opportunities remain within the European airport sector?

A European take-off

However one area where investors are increasingly turning their gaze is Central and Eastern Europe (CEE). In recent months, the sale of Sofia Airport has attracted at least six bids from teams including Manchester Airport Group, Beijing Construction Engineering Group, AENA, First State, Zurich Airport, Meridiam, Aeroports de Paris, India's GMR Infrastructure and Fraport. Vinci is set to be officially awarded Serbia's €1.5bn Belgrade Airport concession, and Montenegro's Podgorica and Tivat airports are seeking requests for qualifications in January.

Industry sources are bullish on the opportunity within the region, with positive traffic growth largely as a result of tourism driving increases in aeronautical and non-aeronautical revenues.

Figure 3: European airport EV/EBITDA multiples vs. listed airports average



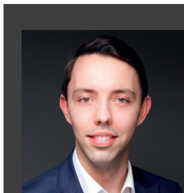
Source: GLIO & Inframation[2]

Airports in the Baltics, Bulgaria, Croatia, the Czech Republic, Greece, Hungary, Poland, Slovakia and Slovenia achieved double-digit passenger traffic growth in the first half of 2018, according to the Airports Council International (ACI) Europe.

Western Europe's largest airports, in contrast, did not achieve such high growth rates. Frankfurt was the highest with a 9.1% increase, followed by Amsterdam-Schiphol with 5.4%, Paris-CDG with 3.0% and London Heathrow 2.6%, said the ACI Europe report.

With nine of the ten largest European airports measured by passenger numbers – London Heathrow, Paris CDG, Amsterdam Schiphol, Frankfurt, Istanbul Ataturk, Madrid-Barajas, Barcelona, London Gatwick, Munich, and Rome-Fiumici – all located in Western Europe, CEE airports also tend to be more in the reach of small to mid-cap infrastructure funds.

The expectation is that investors in CEE airports will generate low double-digit IRRs, rather than the high single-digit returns prevalent in Western Europe today.



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1. All data accurate as of December 17, 2018
2. A full list of individual deals and multiples are available to GLIO Members on request.